

# IS IT “CHARITABLE” TO DISCRIMINATE?

## *The Necessary Transformation of Section 501(c)(3) into the Gold Standard for Charities*

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### I. INTRODUCTION

With federal subsidies to tax-exempt, charitable organizations (hereinafter, “charitable organizations”)<sup>1</sup> estimated to be approximately \$232 billion for fiscal years 2007 to 2011,<sup>2</sup> the public benefit of such organizations is an increasingly hot topic for Congress, the Internal Revenue Service (hereinafter, the “IRS”), and the entire nonprofit sector. In addition to the hefty economic cost of supporting tax-exempt, charitable organizations via the charitable contributions deduction, concerns over excessive compensation to nonprofit executives, the amount of charity care provided by nonprofit versus for-profit hospitals, and responsible corporate governance in the wake of the Enron and WorldCom scandals have led to a call for increased scrutiny of, and accountability by, such organizations.<sup>3</sup> Furthermore, the IRS’s inquiry into the alleged political campaign activities of charitable organizations surrounding the 2004 presidential election (notably, the NAACP and All Saints Episcopal church in California) are reviving the debate over the role of charitable organizations in our modern, politically-divided society.<sup>4</sup>

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<sup>1</sup> The terms “charitable organization,” “tax-exempt organization,” or “exempt organization” are used interchangeably in this Article to refer to nonprofit organizations that qualify for, and have been granted, an exemption from federal income tax pursuant to I.R.C. § 501(c)(3) (2006). In addition, any reference to “exemption” or “tax-exempt” status is intended to refer exclusively to such status under federal income tax law and does not imply exemption under other federal tax laws, or under state or local laws, unless otherwise indicated. *See also infra* notes 56-59 and accompanying text for the common practices of referring to all organizations exempt under Section 501(c)(3) collectively as “charitable” organizations.

<sup>2</sup> Office of Management and Budget, Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2007, 291-94, available at, <http://www.whitehouse.gov/omb/budget/fy2007/pdf/spec.pdf> (last visited Sep. 7, 2006) (estimating tax expenditures for corporate and individual income taxes with respect to the deductibility of charitable contributions to charitable organizations in (i) education, (ii) health, and (iii) other than education and health).

<sup>3</sup> *See* David L. Wolff and Michael D. Rosenbaum, *GAO Survey of Nonprofit Hospitals Latest Step in Congressional Investigation of Tax-Exempt Organizations*, 52 EXEMPT ORG. TAX REV. 265 (2006); Kurt Ritterpusch, *Grassley to Seek More Charitable Reforms Including Executive Compensation Changes*, Daily Tax Rep. (BNA) Jan. 13, 2006, at G-1; Diane Freda, *Sen. Grassley Queries Red Cross On Disaster Relief Role, CEO’s Exit*, Daily Tax Rep. (BNA) Jan. 3, 2006, at G-2; Steve Teske, *House Tax Panel Chairman Says Exemption for Hospitals Becoming Difficult to Justify*, Daily Tax Rep. (BNA) May 27, 2005, at G-1; and Steve Teske, *Grassley Wants Nonprofit Hospitals To Account for Charity Care Activities*, Daily Tax Rep. (BNA) May 26, 2005, at G-6.

<sup>4</sup> *See* Diane Freda, *Internal Revenue Service Ends 2004 Audit of NAACP, Finding No Political Intervention*, Daily Tax Rep. (BNA) Sep. 1, 2006, at G-5; Diane Freda, *IRS Finds Prohibited Political Activity In Nearly Three-Fourths of EO Exams*, Daily Tax Rep. (BNA) Feb. 27, 2006, at GG-1; Diane Freda, *Church Status in Question as IRS Looks Into Guest Pastor’s Anti-War Comments*, Daily Tax Rep. (BNA) Nov. 8, 2005, at G-6.

Amidst all of this heightened scrutiny of charitable organizations and their activities, the Independent Sector, a nonpartisan coalition of over 500 nonprofit organizations, convened the Panel on the Nonprofit Sector in late 2004 at the encouragement of the Senate Finance Committee. The Panel's mission was to provide recommendations to Congress "to improve the oversight and governance of charitable organizations."<sup>5</sup> In a final report released on June 22, 2005, the Panel provided over 120 recommendations, including certain governance changes for charitable organizations to adopt.<sup>6</sup> State legislatures are also joining the burgeoning scrutiny and reform of charitable organizations, with several states considering legislation that stops abusive practices and improves overall transparency and accountability of such organizations.<sup>7</sup>

Despite this recent focus on the transparency of charitable organizations and their activities, one recurring activity continues to fly under the radar of reformers (i.e., absent in any of the above-referenced reform proposals) – discrimination. As illustrated below, discrimination by charitable organizations occurs not only in the employment context, but more importantly in providing services or engaging in activities for which the organization was granted tax-exempt status (e.g., education). It has a variety of bases, including, but not limited to, sexual orientation, marital status, and religious belief or doctrine.

*Boy Scouts of America v. Dale* is perhaps the most renowned recent case involving discrimination by a charitable organization.<sup>8</sup> In that case, a local council of the Boy Scouts of America expelled James Dale, an assistant scoutmaster, after he publicly declared his homosexuality.<sup>9</sup> The New Jersey Supreme Court determined that the Boy Scouts' revocation of Dale's membership violated the state's public accommodations law, which prohibits discrimination on the basis of sexual orientation.<sup>10</sup> Adopting a divergent view, the United States Supreme Court concluded that the New Jersey law violated the Boy Scouts' First Amendment rights (specifically, the freedom of expressive association) and upheld the organization's right to exclude homosexuals from its membership.<sup>11</sup> Aside from its foundation in the First Amendment, the Supreme Court's decision raised a fundamental issue that remains unanswered – should a charitable organization continue to enjoy the benefits of tax-exempt status if it engages in discrimination?<sup>12</sup>

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<sup>5</sup> Panel on the Nonprofit Sector, <http://www.nonprofitpanel.org/about/> (last visited Sep. 7, 2006).

<sup>6</sup> [http://www.nonprofitpanel.org/final/Panel\\_Final\\_Report.pdf](http://www.nonprofitpanel.org/final/Panel_Final_Report.pdf) (last visited Sep. 7, 2006). The Panel issued a supplemental report on April 24, 2006 containing recommendations in nine different areas with respect to charitable organizations. Diane Freda, *Panel Releases Long-Awaited Second Report On Needed Industry Reforms*, Daily Tax Rep. (BNA) Apr. 25, 2006, at G-7.

<sup>7</sup> Fred Stokeld, *State Legislatures Joining Charity Reform Bandwagon*, 108 Tax Notes, July 11, 2005, at 183; see also, Dolores W. Gregory, *As States Attempt to Ramp Up Oversight of Public Charities, Some Look to Sarbanes-Oxley as Model for Audit Requirements*, Daily Tax Rep. (BNA) Sep. 13, 2005, at J-1.

<sup>8</sup> *Boy Scouts of America v. Dale*, 530 U.S. 640, 120 S.Ct. 2446 (2000).

<sup>9</sup> *Id.* at 644; see *infra* note 127.

<sup>10</sup> *Dale v. Boy Scouts of America*, 734 A.2d 1196, 1230 (N.J. 1999) (finding that the Boy Scouts constituted a place of public accommodation subject to the New Jersey public accommodations law).

<sup>11</sup> *Boy Scouts*, 530 U.S. at 659.

<sup>12</sup> See J. Christine Harris, *Should Boy Scouts' Policy On Gays Preclude Tax-Exempt Status?*, 31 EXEMPT ORG. TAX REV. 32 (2001).

Before exploring the answer to that question, it is useful to further illustrate that the type of discrimination present in the *Boy Scouts* case only scratches the surface with respect to seemingly widespread discriminatory practices or policies of charitable organizations:

- In June 2006, an adjunct professor that questioned his church's stance on same-sex marriage was dismissed by the church-owned university that employed him.<sup>13</sup>
- In April 2006, a Baptist-affiliated university expelled a student that announced on his personal website that he was gay.<sup>14</sup> In a statement released to the local NBC affiliate, the university president stated that "There are places students with predispositions can go such as San Francisco and the left coast or to many of the state schools."<sup>15</sup>
- In the Fall of 2005, two 16-year-old girls were expelled from a private Lutheran high school on the suspicion of being lesbians. In a letter sent home to parents, the principal stated that although officials had not witnessed any physical contact between the girls, their friendship was "uncharacteristic of normal girl relationships and more characteristic of a lesbian one."<sup>16</sup> The students filed suit against the school for invasion of privacy and discrimination, seeking readmission, unspecified damages, and an injunction barring the school from excluding gay and lesbian students.<sup>17</sup>
- In late September 2005, a private Christian school expelled a 14-year-old student because her parents are lesbians.<sup>18</sup> A statement from the school's superintendent explained that the family failed to meet its admissions criteria.<sup>19</sup>

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<sup>13</sup> Todd Hollingshead, *BYU fires teacher over op-ed stance*, SALT LAKE TRIB., June 22, 2006. The article refers to four other "high-profile firings" of professors by Brigham Young University from 1993 to 1996 due to controversies with doctrine of the Latter Day Saints Church. *Id.*

<sup>14</sup> Mark Pitsch, *Student expelled from University of Cumberlands for being gay*, COURIER-JOURNAL, Apr. 11, 2006, available at <http://www.courier-journal.com/apps/pbcs.dll/article?AID=/20060411/NEWS0104/604110369> (last visited Sep. 7, 2006). The University's sexual conduct policy states that, "Any student who engages in or promotes sexual behavior not consistent with Christian principles (including sex outside marriage and homosexuality) may be suspended or asked to withdraw from the University of the Cumberlands." *Id.* In an official statement, Jim Taylor, the University's president, stated that "We are different by design and are non-apologetic about our Christian beliefs." *Id.*

<sup>15</sup> Robert Marus, *Gay student's expulsion spawns uproar at Kentucky Baptist school*, ASSOC. BAPTIST PRESS, Apr. 11, 2006, available at <http://www.abpnews.com/944.article> (last visited Sep. 7, 2006). The statement was released to WLEX-TV, an NBC affiliate in Lexington, Kentucky.

<sup>16</sup> *Lutheran school tests legality of expelling gays*, SAN DIEGO UNION-TRIBUNE, Dec. 30, 2005, available at [http://www.signonsandiego.com/uniontrib/20051230/news\\_1n30expel.html](http://www.signonsandiego.com/uniontrib/20051230/news_1n30expel.html) (last visited Sep. 7, 2006).

<sup>17</sup> *Id.*

<sup>18</sup> Robert Paul Reyes, *Christian School Expels Student Because Parents Are Lesbians*, AMERICAN CHRONICLE, Sep. 24, 2005, available at <http://www.americanchronicle.com/articles/viewArticle.asp?articleID=2562> (last visited Sep. 7, 2006).

<sup>19</sup> Letter from Leonard Stob, Superintendent, <http://www.ocschools.org/letterfromsuperintendent.pdf> (last visited Sep. 7, 2006).

- In early 2003, a Catholic independent school fired a religion teacher after her name appeared among the signers of a statement endorsing abortion rights in a full-page ad in the local newspaper.<sup>20</sup> Upon dismissal by the EEOC of her employment discrimination claim, the teacher filed suit against the school, the Catholic diocese and its bishop in federal district court. The court dismissed all of her claims. Her appeal is pending before the Third Circuit.<sup>21</sup>
- In 2003, a Catholic elementary school in Ohio fired one of its teachers because she divorced and remarried without first obtaining an annulment.<sup>22</sup> In the same year, a Catholic school in Kentucky dismissed a fifth-grade teacher after learning she had remarried in a Presbyterian service without first obtaining an annulment of her first marriage.<sup>23</sup>
- In 1998, a Baptist home for children in Kentucky terminated a female employee after approximately seven months of employment because her lesbian lifestyle was contrary to the home's core values. The decision to dismiss her was made after a photograph of the employee and her acknowledged life partner was displayed at the Kentucky State Fair, thus placing the home on notice of her lesbian lifestyle.<sup>24</sup>
- A Christian-affiliated law school's current "Policy on Nondiscrimination" with respect to both admissions and employment practices reads: "The School of Law does not discriminate on the basis of sexual orientation, *but does discriminate on the basis of sexual misconduct*, including, but not limited to, non-marital sexual misconduct, homosexual conduct, or the encouragement or advocacy of any form of sexual behavior that would undermine the Christian identity or faith mission of the University."<sup>25</sup>

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<sup>20</sup> John Shiffman, *U.S. court hears case of teacher fired over stance*, PHIL. INQUIRER, Jan. 18, 2006.

<sup>21</sup> *Id.*

<sup>22</sup> Randall Chase, *Teacher challenges church teaching*, WASH. TIMES, Nov. 15, 2003, available at <http://www.washtimes.com/national/20031114-113845-6019r.htm> (last visited Sep. 7, 2006).

<sup>23</sup> *Id.*

<sup>24</sup> *Pedreira v. Kentucky Baptist Homes for Children, Inc.*, 186 F.Supp.2d 757, 759 (W.D. Ky. 2001). The home issued a public statement addressing the dismissal, stating that "[i]t is important that we stay true to our Christian values. Homosexuality is a lifestyle that would prohibit employment." *Id.*

<sup>25</sup> Liberty University School of Law Policy on Nondiscrimination (with emphasis), available at <http://www.liberty.edu/academics/law/index.cfm?PID=8533> (last visited Sep. 7, 2006). In the interests of full disclosure, the policy further states: "This policy statement is neither intended to discourage, nor is it in fact applicable to, any analytical discussion of law and policy issues involved in the regulation of sexual behavior, or to discussions of any recommendations for changes in existing law. Discussions of these matters are both practiced and are welcomed within our curriculum." *Id.*

In comparison, the statement of nondiscrimination of the Columbus School of Law of The Catholic University of America with respect to admissions, available at <http://law.cua.edu/admissions/CSL/nondiscrimination.cfm> (last visited Sep. 7, 2006), states similarly: "The university fully accepts the teachings of the Catholic church with regard to homosexual conduct and sexual conduct outside the bounds of matrimony, as set forth by the Magisterium of the Catholic Church. Consistent with those teachings, the university does not discriminate purely on the basis of an individual's sexual orientation *without regard to homosexual conduct or other actions that undermine the*

Because many charitable organizations receive governmental support as well as private donations by reason of their tax-exempt status, the primary question raised by the above instances of alleged, actual, or potential discrimination is whether such organizations should continue to receive such tax benefits if they engage in discrimination?<sup>26</sup> Currently, federal income tax law with respect to charitable organizations does not explicitly address nor proscribe discrimination by such organizations.<sup>27</sup> The only possible restraint on discrimination exists in the public policy doctrine enunciated by the United States Supreme Court in *Bob Jones University v. United States*,<sup>28</sup> which granted the Treasury Department (i.e., the IRS by delegation) the power to revoke the tax-exempt status of an organization whose purpose violates “established public policy.”<sup>29</sup> However, the public policy doctrine, as discussed in greater detail in Part II of this Article, has only been used as the basis for revocation with respect to organizations that participated in racial discrimination, advocated civil disobedience, or involved themselves in an illegal activity.<sup>30</sup> Although arguably well-intentioned, the doctrine presents more questions than it answers, the most important of which is: What constitutes clearly “established public policy?”<sup>31</sup> For instance, is prohibiting discrimination on the basis of sexual orientation a clearly established public policy? If an established public policy changes, denying protection to a previously protected segment of the population, are charitable organizations then free to discriminate against the members of such segment? In addition to the fact that these questions remain unanswered and, arguably, unanswerable, the public policy doctrine is criticized routinely because it places too much discretion in a regulatory agency (i.e., the IRS).<sup>32</sup>

This Article attempts to fill the void in current federal income tax law with respect to charitable organizations’ discriminatory practices by proposing an amendment to Section 501(c)(3)<sup>33</sup> that explicitly prohibits such practices. Inherent in this proposal is the notion that discrimination by a charitable organization in any circumstance (employment, provision of services, etc.) is intrinsically incompatible with the organization’s charitable purpose and mission. As necessary background, Part II of this Article provides a statutory and regulatory framework, including an analysis of the meaning of charitable under Section 501(c)(3). It further

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*university’s Catholic identity.*” (emphasis added). The Non-Discrimination statement of the Villanova University School of Law, available at <http://www.law.villanova.edu/admissions/nondiscrimination/> (last visited Sep. 7, 2006), states: “As a Roman Catholic and Augustinian institution, the School of Law strongly affirms the teaching of the Church on the rights and dignity of all persons, and hence condemns discrimination on the basis of a person’s sexual orientation. This position is consistent with the Church’s teaching on human sexuality, which does not endorse homosexual conduct. The School of Law accordingly reaffirms its commitment to providing an inclusive and supportive community for all, regardless of sexual orientation.”

<sup>26</sup> See David A. Brennen, *Tax Expenditures, Social Justice and Civil Rights: Expanding the Scope of Civil Rights Laws to Apply to Tax-Exempt Charities*, 2001 BYU L. REV. 167, 169 (2001) [hereinafter, Brennen, *Tax Expenditures*]; see also, David A. Brennen, *The Power of the Treasury: Racial Discrimination, Public Policy and “Charity” in Contemporary Society*, 33 U.C. DAVIS L. REV. 389 (2000) [hereinafter, Brennen, *Racial Discrimination*].

<sup>27</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 169.

<sup>28</sup> *Bob Jones Univ. v. U.S.*, 461 U.S. 574 (1983), *aff’d* 639 F.2d 147 (4<sup>th</sup> Cir. 1980).

<sup>29</sup> *Bob Jones Univ.*, 461 U.S. at 591.

<sup>30</sup> Brennen, *Racial Discrimination*, *supra* note 26, at 391 fn2 (citing Rev. Rul. 75-384, 1975-2 C.B. 204, Rev. Rul. 71-447, 1971-2 C.B. 230, and Gen. Couns. Mem. 39,862 (Nov. 22, 1991)).

<sup>31</sup> See *infra* notes 115-117 and accompanying text.

<sup>32</sup> See *infra* notes 111-113 and accompanying text.

<sup>33</sup> Unless otherwise indicated, all “Section” references are to the Internal Revenue Code of 1986, as amended.

scrutinizes the failure of such statutory and regulatory framework, as well as the judicially-created public policy doctrine, to resolve the issue posed herein adequately. On the foundation of such failures, Part III of this Article examines noteworthy proposals that attempt similarly to offer viable solutions. Finally, Part IV of the Article offers a comprehensive solution to the problem of discrimination in the charitable sector without relying on other existing laws, which are questionably applicable or lack the necessary extensiveness. The addition of a non-discrimination requirement transforms Section 501(c)(3) into the “gold standard” for all tax-exempt organizations, ensuring that their beneficiaries are as diverse and all encompassing as the taxpaying public from whom such organizations draw their support.<sup>34</sup>

## II. THE EVOLVING MEANING OF “CHARITABLE”

### A. OVERVIEW – WHAT IS “DISCRIMINATION”?

Any attempt to define “discrimination” can cause consternation and incite controversy. Nevertheless, it is necessary for purposes of the discussion herein to identify the meaning of the word “discrimination” or “discriminate.” A legal dictionary defines it as: “The effect of a law or established practice that confers privileges on a certain class or that denies privileges to a certain class because of race, age, sex, nationality, religion, or handicap.”<sup>35</sup> The legal dictionary further provides: “Differential treatment; esp., a failure to treat all persons equally when no reasonable distinction can be found between those favored and those not favored.”<sup>36</sup> In the notes to such definition, an illuminating observation is made with respect to discrimination:

The dictionary sense of “discrimination” is neutral while the current political use of the term is frequently non-neutral, pejorative. . . . For some, it may be enough that a practice is called discriminatory for them to judge it wrong. Others may be mystified that the first group condemns the practice without further argument or inquiry. Many may be led to the false sense that they have actually made a moral argument by showing that the practice discriminates (distinguishes in favor of or against). The temptation is to move from “X distinguishes in favor of or against” to “X discriminates” to “X is wrong” without being aware of the equivocation involved.<sup>37</sup>

In light of the above comment, this Article attempts to avoid any equivocation by relying on a more universal definition of discrimination; namely, “unequal treatment of persons, for a reason which has nothing to do with legal rights or ability.”<sup>38</sup> This more colloquial definition

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<sup>34</sup> Tax-exempt organizations draw their support “directly” from the general public by means of charitable contributions from donors who receive a corresponding deduction under I.R.C. § 170(a)(1) (2006). *See infra* notes 40 and 41 and accompanying text. Such organizations also receive support “indirectly” from the general public in the form of their tax-exempt status, which arguably constitutes a government subsidy or appropriation. *See infra* notes 198-203 and accompanying text.

<sup>35</sup> BLACK’S LAW DICTIONARY (8<sup>th</sup> ed. 2004).

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*, citing ROBERT F. FULLINWIDER, THE REVERSE DISCRIMINATION CONTROVERSY: A MORAL AND LEGAL ANALYSIS, 11-12 (1980).

<sup>38</sup> *See* <http://dictionary.law.com/default2.asp?selected=532&bold=|||> (last visited Sep. 7, 2006).

applies adeptly to the above illustrations in that those charitable organizations imposed unequal or differential treatment in the context of hiring or firing employees, or in providing the services or activities for which they were granted tax-exempt status (i.e., education). Acknowledging the slippery slope that the use of the term engenders, this Article proceeds to discuss bases for federal income tax exemption, including a charitable purpose, and whether discrimination comports with such bases or purposes.

## B. OVERVIEW OF FEDERAL INCOME TAX EXEMPTION

In order to discuss the incompatibility of constituting a charitable organization while engaging in discrimination, it is necessary to be familiar with how an organization qualifies for exemption. Accordingly, this Article provides a brief overview of the federal income tax exemption statute and the regulatory tests that must be satisfied before exemption is granted.

Section 501(c)(3) provides for the exemption from federal income tax of nonprofit corporations and certain other entities “organized and operated exclusively for religious, charitable, scientific, . . . or educational purposes, . . . no part of the net earnings of which inures to the benefit of any private shareholder or individual. . . .”<sup>39</sup> The principal benefit of being exempt under Section 501(c)(3) is that the organization is entitled to receive charitable contributions that are tax-deductible to its donors under Section 170(a)(1).<sup>40</sup> For the most part, only organizations exempt under Section 501(c)(3) are eligible for this invaluable benefit.<sup>41</sup>

The meaning of each of the eight specific exempt purposes listed in the statute (i.e., religious, charitable, educational, etc.) is defined in applicable regulations and in numerous administrative rulings issued by the IRS. The meaning of “charitable” as enumerated in Section 501(c)(3) and the common practice of referring to the entities listed in the section collectively as charitable are discussed in greater detail below.<sup>42</sup> In addition to the statutory and regulatory definitions of what purposes fall within Section 501(c)(3), the IRS has determined that other qualifying purposes meet the overall public benefit principle of Section 501(c)(3) based on an expansive interpretation of “charitable.”<sup>43</sup>

In determining whether an organization fulfills its exempt purpose(s), the language of Section 501(c)(3) establishes both an “organizational test” and an “operational test,” and if an organization seeks to qualify for exemption thereunder it must not fail to meet either test.<sup>44</sup> The organizational test relates solely to the language used in the organization’s governing documents; its articles of incorporation (if a nonprofit corporation) or trust instrument (if a charitable trust).

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<sup>39</sup> I.R.C. § 501(c)(3) (2006). Specifically, Section 501(a) provides that “[a]n organization described in subsection (c) or (d) . . . shall be exempt from taxation under this subtitle. . . .” I.R.C. § 501(a) (2006).

<sup>40</sup> I.R.C. § 170(a)(1) (2006), which provides that “there shall be allowed as a deduction any charitable contribution . . . payment of which is made within the taxable year.” Charitable contributions must be made primarily to either governmental entities or charitable organizations under Section 501(c)(3). I.R.C. § 170(c)(1), (2) (2006).

<sup>41</sup> Certain veterans organizations, fraternal organizations and cemetery organizations, which are exempt from federal income tax under other subsections of Section 501(c) are also entitled to receive tax-deductible contributions per § 170(c)(3), (4), and (5), respectively.

<sup>42</sup> See *infra* notes 56 to 59 and accompanying text.

<sup>43</sup> See Brennen, *Tax Expenditures*, *supra* note 26, at 178.

<sup>44</sup> Treas. Reg. § 1.501(c)(3)-1(a)(1) (as amended in 1990).

Under the test as set forth in the regulations, an organization is organized exclusively for one or more tax-exempt, charitable purposes only if its articles of organization: (i) limit its purpose to one or more exempt purposes, and (ii) do not expressly empower it to engage, otherwise than as insubstantial part of its activities, in activities that in themselves do not further one or more exempt purposes.<sup>45</sup> The organizational test also imposes requirements as to the distribution of the organization's assets upon dissolution.<sup>46</sup>

The operational test is intended to ensure that the organization's resources and activities are devoted primarily to its exempt purposes. The regulations break down the operational test into two components commonly referred to as (i) the primary purpose or activity test, and (ii) the private inurement prohibition.<sup>47</sup> Under the primary purpose or activity test, an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it "engages *primarily* in activities which accomplish one or more of such exempt purposes in Section 501(c)(3)."<sup>48</sup> An organization will not be regarded as primarily furthering its exempt purposes if "*more than an insubstantial part* of its activities is not in furtherance of an exempt purpose."<sup>49</sup>

Under the private inurement prohibition, the regulations provide that the operational test will not be met by an organization "if its net earnings *inure in whole or in part* to the benefit of private shareholders or individuals."<sup>50</sup> The term "private shareholder or individual" is defined as "persons having a personal and private interest in the activities of the organization,"<sup>51</sup> such as officers, directors, or other persons in a position to assert influence or control over the organization's operations and activities.<sup>52</sup> The prohibition is absolute – any amount of inurement is impermissible.

As mentioned previously and discussed in greater detail below, the *Bob Jones University* decision imposes an additional, non-statutory requirement on an organization seeking tax-exempt status – do not violate the public policy doctrine.<sup>53</sup> However, the courts and the IRS have failed to articulate a clear definition of what constitutes "established public policy," leaving the doctrine open to the IRS's unfettered discretion and allowing discrimination potentially to flourish in areas other than race, civil disobedience, and illegality.<sup>54</sup>

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<sup>45</sup> Treas. Reg. § 1.501(c)(3)-1(b)(1)(i) (as amended in 1990).

<sup>46</sup> Treas. Reg. § 1.501(c)(3)-1(b)(4) (as amended in 1990). The regulations require that the organization either in its Articles or under governing state law, must explicitly dedicate its assets to one or more exempt purposes in the event of dissolution.

<sup>47</sup> Treas. Reg. § 1.501(c)(3)-1(c)(1), (2) (as amended in 1990).

<sup>48</sup> Treas. Reg. § 1.501(c)(3)-1(c)(1) (as amended in 1990) (emphasis added).

<sup>49</sup> *Id.* (emphasis added).

<sup>50</sup> Treas. Reg. § 1.501(c)(3)-1(c)(2) (as amended in 1990).

<sup>51</sup> Treas. Reg. § 1.501(a)-1(c) (as amended in 1990). Gen. Couns. Mem. 39,862 (Dec. 2, 1991) describes the term as encompassing "persons who, because of their particular relationship with an organization, have an opportunity to control or influence its activities."

<sup>52</sup> BRUCE R. HOPKINS, *THE LAW OF EXEMPT ORGANIZATIONS* § 19.3, 488 (8th ed. 2003 & Supp. 2006).

<sup>53</sup> See *infra* notes 85 to 107 and accompanying text.

<sup>54</sup> See Brennen, *Tax Expenditures*, *supra* note 26 at 178-179 n.48.

### C. THE STATUTORY IMPACT OF “CHARITABLE”

The failure of the public policy doctrine to adequately check discrimination and the recent focus on charitable organizations’ transparency and accountability revives the age-old conundrum of such organizations’ expected role in our society. If accountability necessarily implies that organizations must accomplish the purposes for which they were granted tax-exempt status, what is meant by the use of the term “charitable”? More importantly, does our notion of “charitable” apply to all purposes enumerated in Section 501(c)(3) so that if we conclude that the antithesis of “charitable” is discrimination, the result is a non-discrimination requirement applicable to all organizations described under Section 501(c)(3)? An abundance of legal scholarship and other commentary focuses on the meaning of charitable and its historical origins in our society and as later adopted in federal income tax law.<sup>55</sup> This Article does not intend to duplicate this extensive commentary, but rather attempts to summarize it succinctly and in a manner that is relevant to the interaction of discrimination with a charitable purpose or existence.

Organizations that receive an exemption from federal income tax under Section 501(c)(3) are commonly referred to as “charitable” organizations.<sup>56</sup> The term “charitable” is used as a collective term despite the fact that it is one of many descriptive terms used in the statute.<sup>57</sup> In other words, the term “charitable” is regarded as including “religious, scientific, educational . . .” organizations.<sup>58</sup> The collective use of charitable may be attributed to the fact that all of the organizations described in Section 501(c)(3) are eligible to receive tax-deductible charitable contributions, as explained previously.<sup>59</sup> The term charitable originates from the English common law of charitable trusts; specifically, from the definition of “charitable purposes” in the Preamble to the Statute of Charitable Uses of 1601.<sup>60</sup> Under the common law of trusts, the term charitable encompasses “trusts for the relief of poverty; trusts for the advancement of education, trusts for the advancement of religion; and trust for other purposes beneficial to the community, not falling under any of the preceding heads.”<sup>61</sup>

For purposes of common law in the United States, the most important and relevant concept taken from English law is an “expansive view” of what constitutes charitable.<sup>62</sup> Legal scholars and courts over the past centuries have concluded similarly “that it is not only

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<sup>55</sup> See *infra* note 234 and accompanying text.

<sup>56</sup> HOPKINS, *supra* note 52, § 5.1, at 103.

<sup>57</sup> *Id.*

<sup>58</sup> *Id.*

<sup>59</sup> See *infra* note 40 and accompanying text; see also, I.R.C. § 170(c)(2) (2006).

<sup>60</sup> HOPKINS, *supra* note 52, § 5.1, at 104, *citing* 43 Eliz., c.4. A review of the Statute of Charitable Uses reveals how the term became an expansive concept in that twenty-one separate charitable activities are enumerated therein. “The activities enumerated include not only relief of aged, impotent, and poor people, but also maintenance of schools of learning and houses of correction, the repair of bridges and churches, and the ‘marriage of poor maids.’” Charles A. Borek, *Decoupling Tax Exemption for Charitable Organizations*, 31 WM. MITCHELL L. REV. 183, 193 (2004). See also Rochelle Korman, *Charitable Class and Need: Whom Should Charities Benefit?*, NYU TOPICS IN PHILANTHROPY (2002), at 3-4, available at <http://www.law.nyu.edu/ncpl/libframe.html> (last visited Sep. 7, 2006) (explaining that the “preamble to the English Statute of Charitable Uses of 1601 in effect codified the scope of charity that had existed in practice for more than 200 years . . .”).

<sup>61</sup> HOPKINS, *supra* note 52, § 5.1, at 104, *citing* *Comm’rs for Special Purposes of Income Tax v. Pemsel*, A.C. 531, 583 (1891).

<sup>62</sup> Borek, *supra* note 60, at 195.

impossible, but a mistake to attempt to formulate a clear definition of charity because ‘charitable activity constantly changes...’” and the question of what is charitable arises in a ‘number of different contexts.’”<sup>63</sup> This is clearly reflected not only in the current Restatement (Second) of Trusts, which is explicitly modeled after the Statute of Charitable Uses in that it enumerates categories of charitable purposes,<sup>64</sup> but also in the Restatement’s comments. These comments provide that “[t]he common element of all charitable purposes is that they are designed to accomplish objects which are beneficial to the community,”<sup>65</sup> and “[t]here is no fixed standard to determine what purposes of such social interest to the community; the interests of the community vary with time and place.”<sup>66</sup>

In enacting Section 501(c)(3), Congress never clearly articulated whether it was guided by the common law definition of charitable, emanating from English common law, or the more “popular and ordinary” usage of the term – namely, relief of the poor.<sup>67</sup> Although arguably a semantic difference, it affects two important implications: (i) “the meaning to be ascribed to the term *charitable* as used in . . . [Section] 501(c)(3),” and (ii) “whether the entirety of the section is intended to describe organizations that are in some sense *charitable*.”<sup>68</sup> Under canons of statutory construction, the disjunctive enumeration of purposes in Section 501(c)(3) (i.e., “religious, charitable, scientific, . . . or educational purposes . . .”) leads to the conclusion that Congress intended to grant tax-exempt status to any organization organized and operated for one of such enumerated purposes.<sup>69</sup> Accordingly, one conclusion is that each of the eight exempt purposes enumerated in Section 501(c)(3) “are not overlain with a requirement that all organizations, to be exempt under that section, must qualify as entities that are *charitable* in the common law sense.”<sup>70</sup>

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<sup>63</sup> Korman, *supra* note 60, at 6-7, quoting John P. Persons, John J. Osborn, Jr., and Charles F. Feldman, *Criteria for Exemption under Section 501(c)(3)*, published in *Research Papers*, sponsored by the Commission on Private Philanthropy and Public Needs, Vol. IV at 1934-35 (1977). See also *Jackson v. Phillips*, 14 Allen (Mass.) 539, 556 (1867), wherein Justice Gray of the Massachusetts Supreme Court in defining charity enunciated the standard for a “charitable class”:

A charity in the legal sense, may be more fully defined as a gift, to be applied consistently with existing laws, *for the benefit of an indefinite number of persons*, either by bringing their minds and hearts under the influence of education or religion, by relieving their bodies from disease, suffering or constraint, by assisting them to establish themselves in life, or by erecting or maintaining public buildings or works or otherwise lessening the burdens of government. (emphasis added).

<sup>64</sup> *Id.* at 198. RESTATEMENT (SECOND) OF TRUSTS § 368 (1959) provides that: “Charitable purposes include: (a) the relief of poverty; (b) the advancement of education; (c) the advancement of religion; (d) the promotion of health; (e) governmental or municipal purposes; (f) other purposes the accomplishment of which is benefit to the community.” *Id.*, n.65.

<sup>65</sup> *Id.*, citing RESTATEMENT (SECOND) OF TRUSTS § 368, cmt. a.

<sup>66</sup> *Id.*, citing RESTATEMENT (SECOND) OF TRUSTS § 368, cmt. b.

<sup>67</sup> HOPKINS, *supra* note 52, § 5.1, at 104 and § 5.2, at 106.

<sup>68</sup> *Id.*, § 5.2, at 106.

<sup>69</sup> *Id.*, § 5.2, at 106, citing *Reiter v. Sonotone Corp.* 442 U.S. 330, 339 (1979) (“Canons of construction ordinarily suggest that terms connected by a disjunctive be given separate meanings, unless the context dictates otherwise.”). Hopkins further explains that a competing statutory construction canon provides that “related statutory provisions should be interpreted together,” citing *Kokoska v. Belford*, 417 U.S. 642 (1974), which he states is particularly relevant since I.R.C. § 170(c)(2) (definition of “charitable contribution” for purposes of the deduction) “reiterates the separate and disjunctive purposes or functions described in IRC § 501(c)(3).” *Id.*

<sup>70</sup> HOPKINS, *supra* note 52, § 5.2, at 107. Hopkins further explains that this conclusion conforms with another canon of statutory construction – “statutes are to be construed to give effect to each word and that no one part of a statute

Although the statutory construction canons lead to the conclusion that all organizations exempt under Section 501(c)(3) are not subject to the common law definition of charitable, legislative history, in the form of a 1939 report of the House of Representatives on exempting certain organizations, appears to illustrate otherwise.<sup>71</sup>

The exemption from taxation of money or property devoted to charitable and other purposes is based upon the theory that the Government is compensated for the loss of revenue by its relief from financial burdens which would otherwise have to be met by appropriations from other public funds, and by the benefits resulting from the promotion of general welfare.<sup>72</sup>

The use of the terms “public” and “general welfare” in the report appears to establish an obligation to follow the common law meaning of charitable.<sup>73</sup> Earlier legislative history lends further support to a broader interpretation of the term charitable.<sup>74</sup>

The current regulations interpreting the meaning of charitable in Section 501(c)(3) were promulgated in 1959, broadening the federal income tax meaning of the term immensely. The regulations acknowledge unmistakably that an organization may qualify under one of the eight enumerated purposes set forth in Section 501(c)(3), regardless of whether any such individual purpose comports with the common law definition of charitable.<sup>75</sup> The regulation explains:

The term “charitable” is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall within the broad outlines of “charity” as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by the law; or (iv) to combat community deterioration and juvenile delinquency.<sup>76</sup>

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should be interpreted so as to render another part of the statute redundant,” *citing* *Jarecki v. G.D. Searle & Co.*, 367 U.S. 303 (1961). *Id.*, n.26.

<sup>71</sup> HOPKINS, *supra* note 52, § 5.2, at 108.

<sup>72</sup> *Id.*, *citing* 48 H.R. REP. NO. 1860, 75<sup>TH</sup> CONG., 3D SESS. 19 (1938). *See also*, Brennen, *Tax Expenditures*, *supra* note 26 at 188-189, fn.90.

<sup>73</sup> HOPKINS, *supra* note 52, § 5.2, at 108. The author also states that, to the contrary, the language “charitable and other purposes” may infer “intent to invoke a narrower meaning of the term *charitable*.” *Id.*

<sup>74</sup> *Id.*, *citing* 44 Cong. Rec. 4150 (1909) (the sponsor of the 1909 tax exemption statute, which was imposed only on corporations at that time, stated that the provision was drafted to relieve from income tax liability those organizations “devoted exclusively to the relief of the suffering, to the alleviation of our people, and to all things which commend themselves to every charitable and just impulse.”).

<sup>75</sup> HOPKINS, *supra* note 52, § 5.2, at 110.

<sup>76</sup> Treas. Reg. § 1.501(c)(3)-1(d)(2) (as amended in 1990).

These regulations integrated “the concept that the meaning of charity . . . [is] not static, but . . . [is] meant to evolve over time to reflect changing circumstances and the changing views of public benefit.”<sup>77</sup> Undeniably, the IRS has liberally and expansively interpreted the meaning of charitable to address the ever-changing needs of the general public.<sup>78</sup>

Notwithstanding, courts have not readily adopted the separateness of the purposes enumerated in Section 501(c)(3) and affirmed in the regulations.<sup>79</sup> One federal court of appeals concluded that the “term ‘charitable’ is a generic term and includes literary, religious, scientific and educational institutions.”<sup>80</sup> Still another appellate court announced in multiple decisions that charitable trust rules should be applied in determining the meaning of charitable, and that it was Congress’ intent to apply such rules to “those organizations commonly designated charitable in the law of trusts.”<sup>81</sup> In *Bob Jones University*, the United States Supreme Court noted that Congress permitted deductibility of “charitable contributions” under Section 170(a) only to certain eligible organizations, which are “virtually identical” to those enumerated in Section 501(c)(3).<sup>82</sup> Accordingly, the Supreme Court concluded that Congress intended to provide tax benefits to organizations serving “charitable” purposes, regardless of an organization’s specific activities (e.g., religious, educational or scientific).<sup>83</sup> In other words, each of the eight enumerated purposes in Section 501(c)(3) fall within a broad classification of “charitable.”<sup>84</sup>

Accordingly, the Supreme Court’s decision in *Bob Jones University*, in announcing the public policy doctrine, solidified this broad view that all tax-exempt organizations described in Section 501(c)(3) are considered “charitable,” as discussed further below.

#### D. THE PUBLIC POLICY DOCTRINE’S IMPACT ON “CHARITABLE”

##### 1. Overview – *Bob Jones University v. United States*

The controversy that culminated in the Supreme Court’s decision in *Bob Jones University* began in early 1970 with a federal district court issuing a preliminary injunction that compelled the IRS to deny tax exemption to private schools in Mississippi with sustained racially-discriminatory admissions policies.<sup>85</sup> Until 1970, the IRS granted tax-exempt status to private

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<sup>77</sup> MARION R. FREMONT-SMITH, GOVERNING NONPROFIT ORGANIZATIONS 101 (2004).

<sup>78</sup> *Id.* at 245.

<sup>79</sup> HOPKINS, *supra* note 52, § 5.2, at 110.

<sup>80</sup> U.S. v. Proprietors of Social Law Library, 102 F.2d 481, 483 (1st Cir. 1939).

<sup>81</sup> HOPKINS, *supra* note 52, § 5.2, at 111, *citing* Pennsylvania Co. for Ins. on Lives v. Helvering, 66 F.2d 284, 285 (D.C. Cir. 1933) and International Reform Fed’n v. District Unemployment Board, 131 F.2d 337, 339 (D.C. Cir. 1942). *Cf. infra* note 101.

<sup>82</sup> *Bob Jones Univ.*, 461 U.S. at 587-88, adopting the Fourth Circuit’s similar analysis. *See* *Bob Jones Univ. v. U.S.*, 639 F.2d 147, 151 (4<sup>th</sup> Cir. 1980).

<sup>83</sup> *Id.*

<sup>84</sup> HOPKINS, *supra* note 52, § 5.2, at 107 n.22 and 111.

<sup>85</sup> *Green v. Kennedy*, 309 F.Supp. 1127 (D.D.C. 1970). *See* Charles O. Galvin & Neal Devins, *A Tax Policy Analysis of Bob Jones Univ. University v. U.S.*, 36 VAND. L. REV. 1353, 1357 (1983) (“The Green court suggested that the IRS would not be permitted to grant tax-exempt status to institutions that violate the government’s public policy of nondiscrimination.”). In *Green v. Connally*, 330 F. Supp. 1150 (D.D.C.), *aff’d sub nom. Coit v. Green*,

schools regardless of any racially-discriminatory admissions policy.<sup>86</sup> In response to the injunction, the IRS discontinued granting exemptions in such instances, as well as prohibited deductions of charitable contributions to schools that racially discriminate.<sup>87</sup> In addition to notifying all private schools, including Bob Jones University, the IRS issued a revenue ruling that formally established this new policy and required such schools to adopt and maintain a policy of nondiscrimination with respect to students in its admissions, scholarship and loan programs, and athletic and other school-administered programs.<sup>88</sup>

Located in Greenville, South Carolina, Bob Jones University was created “to conduct an institution of learning ..., giving special emphasis to the Christian religion and the ethics revealed in the Holy Scriptures.”<sup>89</sup> Based on its founders’ belief that the Bible forbids interracial dating and marriage, Bob Jones University sustained a racially-discriminatory admissions policy.<sup>90</sup> Upon being formally notified by the IRS of the new nondiscrimination requirement for private schools, Bob Jones University filed suit in 1971 attempting to enjoin the IRS from revoking its tax exemption.<sup>91</sup> The university was unsuccessful.<sup>92</sup> On January 19, 1976, the IRS

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404 U.S. 997 (1971), the district permanently enjoined the IRS from granting tax-exempt status to any Mississippi school that failed to publicly sustain a nondiscrimination policy.

<sup>86</sup> *Bob Jones Univ.*, 461 U.S. at 577.

<sup>87</sup> I.R.S. News Release (July 10, 1970). See Brennen, *Racial Discrimination*, *supra* note 26, at 400-401

<sup>88</sup> Rev. Rul. 71-447, 1971-2 C.B. 230. In explaining the basis for the ruling, the IRS states:

Under common law, the term “charity” encompasses all three of the major categories identified separately under section 501(c)(3) of the Code as religious, educational, and charitable. Both the courts and the Internal Revenue Service have long recognized that the statutory requirement of being “organized and operated exclusively for religious, charitable, \*\*\* or educational purposes” was intended to express the basic common law concept. Thus, a school asserting a right to the benefits provided for in section 501(c)(3) of the Code as being organized and operated exclusively for educational purposes must be a common law charity in order to be exempt under that section.

In concluding that a school without a racially nondiscriminatory policy with respect to students is not “charitable,” the IRS relies on the charitable trust principle that “the purpose of the trust may not be illegal or contrary to public policy,” citing Restatement (Second), Trusts (1959) Sec. 377, Comment c. The IRS subsequently released guidelines for determining whether private schools had adequately publicized their racially nondiscriminatory policy. Rev. Proc. 72-54, 1972-2 C.B. 834, *amplified by* Rev. Proc. 75-50, 1975-2 C.B. 587. The guidelines require schools to: (i) demonstrate their racially nondiscriminatory policy in their governing documents (charter, bylaws) and catalogs, (ii) make their policy known to all segments of the community through newspapers and broadcast media, and (iii) keep detailed records evidencing their compliance with such guidelines. Furthermore, in Rev. Rul. 75-231, 1975-1 C.B. 158, the IRS announced its denial of tax-exempt status to any religious organization with racially discriminatory policies, even if sincere religious belief served as the foundation for the discrimination. See Galvin & Devins, *supra* note 85, at 1358 n.23.

<sup>89</sup> *Bob Jones Univ.*, 461 U.S. at 579-580. Although not affiliated with any particular Christian denomination, the university is “dedicated to the teaching and propagation of its fundamentalist Christian religious beliefs.” *Id.* at 580.

<sup>90</sup> *Id.* at 580. Specifically, the university admitted no black students until 1971. From 1971 to May 1975, it continued its discrimination against unmarried blacks, but accepted applications from black students married within their race. *Id.* In accordance with the Fourth Circuit’s decision in *McCrary v. Runyon*, 515 F.2d 1082 (4<sup>th</sup> Cir. 1975), *aff’d* 427 U.S. 160 (1976), which determined that racial exclusion from private schools was illegal, the university admitted unmarried blacks. However, it maintained a disciplinary rule that prohibited interracial dating and marriage, and denied admissions to prospective students and expelled enrolled students that violated the rule. *Bob Jones Univ.*, 461 U.S. at 580-581.

<sup>91</sup> *Bob Jones Univ.*, 461 U.S. at 581. The university received a letter from the IRS dated November 30, 1970. In addition to stating the IRS’s new policy, the letter also announced the IRS’s “intention to challenge the tax-exempt status of private schools practicing racial discrimination in their admissions policies.” *Id.*

revoked the university's charitable exemption retroactive to the date the university was notified by letter of the IRS's change in policy for private schools.<sup>93</sup> As a vehicle for challenging the revocation of its exemption, the university filed suit in federal district court seeking a refund of federal unemployment tax paid to the IRS. The government counterclaimed for unpaid taxes. The district court determined that the revocation of the university's exempt status exceeded the IRS's delegated powers (from the Department of the Treasury) and violated the university's First Amendment religious rights.<sup>94</sup> The Fourth Circuit reversed the district court decision on appeal, stating that an educational institution must be "charitable in the common law sense, and . . . not be contrary to public policy" to be eligible for exemption.<sup>95</sup> Furthermore, the court determined that the university clearly failed this requirement since its "racial policies violated the clearly defined public policy, rooted in our Constitution, condemning racial discrimination and, more specifically, the government policy against subsidizing racial discrimination in education, public or private."<sup>96</sup>

Upon granting certiorari, the Supreme Court affirmed the Fourth Circuit's decision by a vote of eight to one, upholding the IRS's revocation of Bob Jones University's tax-exempt status.<sup>97</sup> The Supreme Court noted that since the IRS's announced policy change in 1970, an organization, in order to qualify for exempt status under Section 501(c)(3), must first within one of the eight categories set forth in the statute and, second, demonstrate that its activities are not contrary to established public policy.<sup>98</sup> In response to the university's argument that the eight categories in the statute are disjunctive and, thus, an organization need not also qualify as "charitable" to be tax-exempt, the Court observed that although Section 501(c)(3) does not explicitly impose a public policy limitation, Congress nevertheless intended that "entitlement to tax exemption depends on meeting certain common law standards of charity – namely, that an institution . . . must serve a public purpose and not be contrary to established public policy."<sup>99</sup> The Court further observed the interactions between Sections 170 and 501(c)(3), explaining that "§ 170 reveals that Congress' intention was to provide tax benefits to organizations serving

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<sup>92</sup> In *Bob Jones Univ. v. Simon*, 416 U.S. 725 (1974), the Supreme Court determined that I.R.C. §7421(a) (the Tax Anti-Injunction Act) did not permit the university to obtain judicial review through an injunctive action prior to the assessment or collection of any tax. *Bob Jones Univ.*, 461 U.S. at 581.

<sup>93</sup> *Bob Jones Univ.*, 461 U.S. at 581.

<sup>94</sup> *Id.* at 582.

<sup>95</sup> *Id.* See *Bob Jones Univ.*, 639 F.2d at 147.

<sup>96</sup> *Id.*, citing *Bob Jones Univ.*, 639 F.2d at 151.

<sup>97</sup> *Bob Jones Univ.*, 461 U.S. at 585.

<sup>98</sup> *Id.*

<sup>99</sup> *Id.* at 586 (footnotes omitted). In response to the university's "plain language" argument that Section 501(c)(3) was devoid of any "charitable" overlay to all of the purposes delineated therein, the Court stated:

It is a well-established canon of statutory construction that a court should go beyond the literal language of a statute if reliance on that language would defeat the plain purpose of the statute . . . 'And it is well settled that, in interpreting a statute, the court will not look merely to a particular clause in which general words may be used, *but will take in connection with it the whole statute . . . and the objects and policy of the law....*'

*Id.* In addition, the Court explained:

The Court's reading of § 501(c)(3) does not render meaningless Congress' action in specifying the eight categories of presumptively exempt organizations, as petitioners suggest. . . . To be entitled to tax-exempt status under § 501(c)(3), an organization must first fall within one of the categories specified by Congress, and in addition must serve a valid charitable purpose.

*Id.* at 592, n.19.

charitable purposes. The form of § 170 simply makes plain what common sense and history tell us: in enacting both § 170 and § 501(c)(3), Congress sought to provide tax benefits to charitable organizations, to encourage development of private institutions that serve a useful public purpose or supplement or take the place of public institutions of the same kind.”<sup>100</sup> According, as set forth previously in the discussion on the meaning of “charitable,” the *Bob Jones University* decision solidified the view that there is a “charitable” overlay to all exempt organizations described in Section 501(c)(3), thereby providing the means necessary to impose a public policy limitation on all such exempt organizations.<sup>101</sup>

To support its conclusion that Bob Jones University violated an “established” public policy and, thus, could not be considered charitable, the Supreme Court stated that “[a]n unbroken line of cases following *Brown v. Board of Education* establishes beyond doubt this Court’s view that racial discrimination in education violates a most fundamental national public policy, as well as rights of individuals.”<sup>102</sup> In addition to *Brown*, the Court relied on the civil rights acts passed by Congress as well as executive orders issued over a forty-year period to conclude that eliminating racial discrimination in education and elsewhere was an established national public policy.<sup>103</sup> Accordingly, the Court relied on the aggregated pronouncements of all three branches of government as constituting established public policy.

The Supreme Court rejected the university’s argument that the Treasury (IRS by delegation) overstepped its lawful bounds in issuing the 1970 and 1971 rulings and notices, noting that Treasury has consistently received “broad authority” from Congress to interpret tax

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<sup>100</sup> *Id.* at 587-588 (footnotes omitted). The Court proceeded to enunciate a fairly broad standard for tax exemption: Charitable exemptions are justified on the basis that the exempt entity confers a public benefit—a benefit which the society or the community may not itself choose or be able to provide, or which supplements and advances the work of public institutions already supported by tax revenues. History buttresses logic to make clear that, to warrant exemption under § 501(c)(3), an institution must fall within a category specified in that section and must demonstrably serve and be in harmony with the public interest. The institution’s purpose must not be so at odds with the common community conscience as to undermine any public benefit that might otherwise be conferred.

*Id.* at 591-592 (footnotes omitted).

<sup>101</sup> *Cf.* Miriam Galston, *Public Policy Constraints On Charitable Organizations*, 3 VA. TAX REV. 291, 292 (1984) (opining that the U.S. Supreme Court in *Bob Jones Univ.* “misread the common law of charity into the [Internal Revenue] Code while confusing the public policy and public benefits strands of charitable trust law. . . . when read properly trust law does not provide the theoretical foundation for public policy constraints in the area of federal tax law.”).

As the lone dissenter in *Bob Jones Univ.*, Justice Rehnquist rejected similarly the notion there existed a charitable overlay to each of the delineated purposes in Section 501(c)(3). He concluded that “the legislative history of §501(c)(3) unmistakably makes clear that *Congress has decided* what organizations are serving a public purpose and providing a public benefit within the meaning of §501(c)(3) and has clearly set forth in §501(c)(3) the characteristics of such organizations.” *Bob Jones Univ.*, 461 U.S. at 615. The Justice concludes by stating that he agrees with the majority that there exists a “strong national policy in this country opposed to racial discrimination. I agree with the Court that Congress has the power to further this policy by denying §501(c)(3) status to organizations that practice racial discrimination. But as of yet Congress has failed to do so. Whatever the reasons for the failure, this Court should not legislate for Congress.” *Id.* at 622 (footnotes omitted). *See also* Galvin & Devins, *supra* note 85, at 1363.

<sup>102</sup> *Bob Jones Univ.*, 461 U.S. at 593.

<sup>103</sup> *Id.* at 593-595; *see also* Brennan, *Racial Discrimination*, *supra* note 26, at 403-404.

laws.<sup>104</sup> Furthermore, the Court concluded that IRS's primary responsibility, guided by the Internal Revenue Code, is to determine whether an entity is "charitable" under Sections 170 and 501(c)(3), which also "may necessitate later determinations of whether given activities so violate public policy that such an entity cannot be deemed to provide a public benefit worthy of 'charitable' status."<sup>105</sup> Finally, in response to the university's argument that the public policy doctrine violated their First Amendment free exercise rights, the Court affirmed that certain compelling governmental interests can justify regulating certain religiously-based conduct.<sup>106</sup> In finding that the government's interest in eradicating racial discrimination in education was sufficiently compelling to overcome any First Amendment concerns, the Court concluded that the "[d]enial of tax benefits will inevitably have a substantial impact on the operation of private religious schools, but will not prevent those schools from observing their religious tenets."<sup>107</sup>

## 2. Critique of the Public Policy Doctrine

Although considered to be the correct result, the Supreme Court's decision in *Bob Jones University* has nevertheless been deliberated and criticized extensively. The Supreme Court has been disparaged for concluding that a charitable overlay to Section 501(c)(3) exists and imposing a public policy limitation on the statute.<sup>108</sup> The Court has likewise been rebuked for "abdicating its supervisory powers to the IRS . . . and supplant[ing] the role of Congress as lawmaker by making broad tax policy pronouncements," rather than exercising the oversight necessary to ensure that the IRS properly enforces the tax laws.<sup>109</sup>

The doctrine has also been criticized consistently as lacking legal or statutory authority and a "clearly defined scope of applicability."<sup>110</sup> Since the IRS's adoption of its racial nondiscrimination policy in 1970, Congress has neither enacted any law that codifies the public policy doctrine nor provided the IRS with "legal authority to act solely on public policy grounds."<sup>111</sup> As a consequence, some scholars question whether the IRS is the appropriate

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<sup>104</sup> *Id.* at 596.

<sup>105</sup> *Id.* at 597-598. See also Brennen, *Racial Discrimination*, *supra* note 26, at 404-405, discussing legislative events occurring after the IRS's adoption of the public policy limitation in 1970, which made "an unusually strong case of legislative acquiescence . . . and ratification" by Congress. *Id.*

<sup>106</sup> *Bob Jones Univ.*, 461 U.S. at 603, *citing* Prince v. Massachusetts, 321 U.S. 158, 170 (1944) (Court held that "neutrally cast child labor laws prohibiting sale of printed materials on public streets could be applied to prohibit children from dispensing religious literature.").

<sup>107</sup> *Id.* at 603-604. The Court further concluded that the government's interest "substantially outweighs whatever burden denial of tax benefits places on petitioners' exercise of their religious beliefs. The interests asserted by petitioners [the university] cannot be accommodated with that compelling governmental interest, . . . and no 'less restrictive means' . . . are available to achieve the governmental interest." *Id.* at 604 (citations omitted).

<sup>108</sup> Galvin & Devins, *supra* note 85, at 1379-1380; see also Galston, *supra* note 101.

<sup>109</sup> *Id.*

<sup>110</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 186. For his other scholarship on discrimination and tax-exempt charities, see Brennen, *Racial Discrimination*, *supra* note 26, and David A. Brennen, *Charities and the Constitution: Evaluating the Role of Constitutional Principles in Determining the Scope of Tax Law's Public Policy Limitation for Charities*, 5 FLA. TAX REV. 779 (2002) [hereinafter, Brennen, *Charities and the Constitution*].

<sup>111</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 186-187, n.83; see also, Brennen, *Racial Discrimination*, *supra* note 26, at 446 ("Congress has passed no law that affirmatively states that the Treasury shall, pursuant to its own determinations of 'established public policy,' grant or deny tax-exempt status based on race. Additionally, Congress has not ratified, expressly or implicitly, the Court's interpretation that the public policy power emanates from the Treasury's obligation to interpret the term 'charitable' in section 501(c)(3) of the Code."). However, Congress did

federal agency to determine if a charitable organization violates an established public policy.<sup>112</sup> In his concurrence in *Bob Jones University*, Justice Powell appears to agree by asserting that this task belongs to Congress:

[W]here the philanthropic organization is concerned, there appears to be little to circumscribe the almost unfettered power of the Commissioner [of Internal Revenue]. This may be very well so long as one subscribes to the particular brand of social policy the Commissioner happens to be advocating at the time . . . , but application of our tax laws should not operate in so fickle a fashion. Surely, social policy in the first instance is a matter for legislative concern.<sup>113</sup>

One scholar, Professor David Brennan, argues that this lack of IRS authority forced the Supreme Court in *Bob Jones University* to rely on an expansive interpretation of “charitable” in Section 501(c)(3) as justification for the IRS’s public policy power.<sup>114</sup> In disagreeing with such an expansive view of “charitable,” Brennan concludes that the Supreme Court’s decision fails to “address the limits of the Treasury’s ability to determine when or if a particular ‘public policy’ is sufficiently ‘established’” in contexts other than racial discrimination.<sup>115</sup> Accordingly, Brennan raises a fundamental issue – which sources of law or current policy should the IRS consult to determine that a national public policy exists? Federal constitutional law? Federal civil rights laws? States’ laws?<sup>116</sup> In *Bob Jones University*, the Supreme Court looked to all three branches of government to conclude an established public policy existed. Is this the proper standard to be applied in all instances? As accentuated further by another legal scholar, “it may also be quite validly asserted that there is a federal public policy, either presently in existence or in the process of development, against other forms of discrimination, such as discrimination on the basis of

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enact Section §501(i) of the Code in 1976, which prohibits certain discrimination by social clubs. The statutory language used in Section 501(i) limits its applicability to social clubs exempt from federal income tax under Section 501(c)(7); public charities exempt from federal income tax under Section 501(c)(3) are not covered. I.R.C. §501(i) (2006) provides:

[A]n organization which is described in [§501] (c)(7) [a social club] shall not be exempt from taxation . . . for any taxable year if, at any time during such taxable year, the charter, bylaws, or other governing instrument, of such organization, or any written policy statement of such organization contains a provision which provides for discrimination against any person on the basis of race, color or religion.

Justice Rehnquist referred to the existence of Section 501(i) in his *Bob Jones Univ.* dissent as evidence that if Congress “wants to add a requirement prohibiting racial discrimination to one of the tax-benefit provisions, it is fully aware of how to do it.” *Bob Jones Univ.*, 461 U.S. at 621.

<sup>112</sup> See Brennan, *Racial Discrimination*, *supra* note 26, at 411-428.

<sup>113</sup> *Bob Jones Univ.*, 461 U.S. at 611-12, quoting Commissioner v. “Americans United” Inc., 416 U.S. 752, 774-75 (1974) (Blackmun, J., dissenting). See also Hatfield, Milgram & Monticciolo, *Bob Jones Univ. University: Defining Violations of Fundamental Public Policy*, NYU TOPICS IN PHILANTHROPY (2000), at 14, available at <http://www.law.nyu.edu/ncpl/libframe.html> (last visited Sep. 7, 2006); and Gavins & Devins, *supra* note 85, at 1373.

<sup>114</sup> *Id.*

<sup>115</sup> Brennan, *Racial Discrimination*, *supra* note 26, at 407; see also *supra* note 103 and accompanying text.

<sup>116</sup> *Id.* at 436-439. For instance, there is no established national public policy against discrimination on the basis of sexual orientation. Although numerous municipalities and some states have enacted anti-discrimination ordinances and laws, there is no established federal law specifically addressing this kind of discrimination. In deed, Congress’s actions to date fail to “come within the standards envisioned by the *Bob Jones Univ.* Court for proving the existence of a fundamental national public policy against sexual orientation discrimination.” Hatfield, *et. al*, *supra* note 113, at 78, 86-87.

marital status, national origin, religion, handicap, sexual preference, and age.”<sup>117</sup> The lack of a clearly defined source of public policy is only compounded by the significant evidentiary burden placed on the IRS to determine and prove that an organization’s activities violate a fundamental public policy.<sup>118</sup>

In conclusion, the absence of a clearly defined public policy results in the IRS balancing its unfettered discretion in exercising public policy power with the heavy burden of proving that a policy is established. This difficult balancing act may explain why the IRS has used the public policy doctrine as the basis for revocation only in instances involving racial discrimination, civil disobedience, or illegal activity.<sup>119</sup> Furthermore, the lack of a defined public policy also leaves charitable organizations in the precarious position of monitoring the current political climate to ensure their activities do not violate a contemporary public policy.<sup>120</sup> Although the codification of the public policy doctrine has been proposed as a solution for its lack of legal or statutory authority,<sup>121</sup> it is the doctrine’s lack of defined scope and the difficulty balancing act imposed on the IRS in applying the doctrine that prevent the doctrine from being more effective in addressing discrimination by charities. As illustrated in Part I of this Article, reliance on the doctrine to combat discrimination on the basis of marital status, sexual orientation, or even religion has been futile since such bases are not “established” public policy. Only Congress’s enactment of a well-defined nondiscrimination requirement in Section 501(c)(3) will effectively cease discrimination by charitable organizations.

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<sup>117</sup> HOPKINS, *supra* note 52, § 5.4, at 125. Hopkins cites to the following as support of his statement: Title VII of the Civil Rights Act of 1964, as amended, 42 U.S.C. § 2000e *et seq.*; Executive Order 11246, as amended, 30 Fed. Reg. 12319 (1965); Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681 *et seq.*; the Rehabilitation Act Amendments of 1974, 29 U.S.C. § 621 *et seq.*; and the Age Discrimination Act of 1975, 89 Stat. 713. *See also* Gay Rights Coalition of Georgetown Univ. Law Center & D.C. v. Georgetown Univ., 536 A.2d 1, 38 (D.C. Ct. App. 1987) (Court held that Georgetown University violated the District of Columbia’s human rights act, which prohibits an educational institution from discriminating against any individual on the basis of his or her sexual orientation (D.C. Code, Title 1 § 1-2520), and concluded that the “eradication of sexual orientation discrimination is a compelling government interest”). *Cf.* Hatfield et. al, *supra* note 113, at 86-87 (concludes the non-existence of “a fundamental national public policy against sexual orientation discrimination.”).

<sup>118</sup> Hatfield et. al, *supra* note 113, at 16. The authors further note that the “IRS may also be loathe to jeopardize its own independence. Taking action against an organization for violating public policy, the IRS risks being reined in by the Congress or the President. Already unpopular, it may seem foolhardy to IRS officials to take a stand on controversial political issues.” *Id.* The IRS acknowledges this difficulty in its own training materials on the public policy doctrine: “Deciding a case on the basis of public policy rather than a specific law is difficult because it requires discerning what the public policy involved really is.” *See* Jean Wright and Jay H. Rotz, *Illegality and Public Policy Considerations*, MATERIALS FOR IRS EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION TECHNICAL INSTRUCTION PROGRAM FOR FY 1994, at 9, available at <http://www.irs.gov/pub/irs-tege/eotopic194.pdf> (last visited Sep. 7, 2006).

<sup>119</sup> *See supra* note 30 and accompanying text.

<sup>120</sup> *See* Galvin & Devins, *supra* note 85, at 1373-74. The authors point out that “an organization’s survival may depend on the views of the particular administration in office. For example, President Carter had sought to impose racial quotas on tax-exempt private schools to further the nondiscrimination requirement. In contrast, President Reagan . . . attempted to lift nonstatutory regulations governing tax-exempt private schools. Although neither president succeeded, the threat remains that similar acts by the Executive branch could bankrupt organizations whose existences depend on tax exemptions.” *Id.*

<sup>121</sup> Brennen, *Racial Discrimination*, *supra* note 26, at 446

E. *BOY SCOUTS OF AMERICA V. DALE* – A MISSED OPPORTUNITY TO CLARIFY THE PUBLIC POLICY DOCTRINE’S SCOPE?

One scholar propounds that the Supreme Court’s decision in *Boy Scouts of America v. Dale*<sup>122</sup> “implicates fundamental aspects of true democracy” – the intersection of First Amendment free expression rights with state and social goals to eradicate discrimination (i.e., via anti-discrimination laws).<sup>123</sup> Clearly, the First Amendment right to free expression prevailed.<sup>124</sup> Although it is difficult to argue that the inherent weaknesses of the public policy doctrine resulted in the Supreme Court’s *Boy Scouts* decision, it is certainly plausible to argue that the decision only further exploited the doctrine’s weaknesses, ultimately leading to IRS inaction in its wake. Because the public policy doctrine lacks a “clearly defined scope of applicability,”<sup>125</sup> the Boy Scouts remains a charitable organization under Section 501(c)(3) despite its explicit and unapologetic discrimination in excluding homosexual members. Although the *Boy Scouts* decision did not involve federal income tax law ostensibly, in upholding the Boy Scouts’ ban on homosexuals on the basis of their First Amendment right of expressive association, the decision did resurrect the issue of what constitutes an “established” public policy and whether the Boy Scouts’ discriminatory policy should preclude it from being described as charitable under Section 501(c)(3).<sup>126</sup> Accordingly, in the world of charitable organizations and tax-exempt law, the Supreme Court’s *Boy Scouts* decision is more significant for what it did not address than for what it did.

In the case, a local council of the Boy Scouts expelled James Dale, an assistant scoutmaster, from its membership after he publicly declared his homosexuality.<sup>127</sup> Dale filed suit in the state superior court alleging the Boy Scouts’ violation of the New Jersey public accommodations law, which prohibited discrimination on the basis of sexual orientation in places of public accommodation.<sup>128</sup> The court’s Chancery Division granted summary judgment in favor of the Boy Scouts, but was reversed by the Appellate Division.<sup>129</sup> The New Jersey Supreme Court determined that the Boy Scouts’ revocation of Dale’s membership violated the state public accommodations law by revoking Dale’s membership based on his confirmed homosexuality.<sup>130</sup> The Court held that the application of the state law did not violate the Boy Scouts’ First Amendment right of expressive association because members could still effect the organization’s purposes with Dale as a member.<sup>131</sup> The Court further concluded that the State had a compelling interest in eradicating “the destructive consequences of discrimination from our

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<sup>122</sup> *Boy Scouts*, 530 U.S. at 640.

<sup>123</sup> Brennan, *Charities and the Constitution*, *supra* note 110, at 840.

<sup>124</sup> *Id.*

<sup>125</sup> *See supra* note 110 and accompanying text.

<sup>126</sup> *See Harris*, *supra* note 12, at 32.

<sup>127</sup> *Boy Scouts*, 530 U.S. at 644. Dale’s homosexuality was “declared” via an interview with a local newspaper at a conference on gay and lesbian teenagers’ health. The interview was published along with his photograph and a caption identifying him as a leader in the Rutgers University Lesbian/Gay Alliance. *Id.*

<sup>128</sup> *Id.* at 640.

<sup>129</sup> *Id.*

<sup>130</sup> *Id.*; *see also Dale*, 734 A.2d at 1230 (finding that the Boy Scouts constituted a place of public accommodation subject to the New Jersey public accommodations law).

<sup>131</sup> *Boy Scouts*, 530 U.S. at 640.

society” and that its public accommodations law restrained no more speech than necessary to accomplish its purpose.<sup>132</sup>

Adopting a divergent view, the United States Supreme Court concluded that the New Jersey law violated the Boy Scouts’ First Amendment right of expressive association and upheld the organization’s right to exclude homosexuals from its membership.<sup>133</sup> The Supreme Court began its opinion by referring to its prior decision in *Roberts v. United States Jaycees*<sup>134</sup> where the Court discerned that “implicit in the right to engage in activities protected by the First Amendment [is] a corresponding right to associate with others in pursuit of a wide variety of political, social, economic, educational, religious, and cultural ends.”<sup>135</sup> The Court concluded that this “right is crucial in preventing the majority from imposing its views on groups that would rather express other, perhaps unpopular, ideas.”<sup>136</sup> In its “limited” inquiry into the Boy Scouts’ viewpoints, the Supreme Court found that the organization’s foundation of encouraging its youth membership to be “morally straight” and “clean” would be significantly burdened by Dale’s presence, which would “promote homosexual conduct as a legitimate form of behavior.”<sup>137</sup> Thus, the notion that Dale’s very presence constitutes a message buttresses the Court’s opinion.<sup>138</sup> By finding that the Boy Scouts’ expression would be burdened by Dale’s compelled membership, the Supreme Court summarily concluded that the New Jersey’s interests embodied in its public accommodations law failed to justify such a “severe intrusion” on the Boy Scouts’ rights to freedom of expressive association.<sup>139</sup>

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<sup>132</sup> *Id.* at 640, 647.

<sup>133</sup> *Id.* at 659.

<sup>134</sup> *Roberts v. U.S. Jaycees*, 468 U.S. 609 (1984). In *Roberts*, the Supreme Court affirmed the application of a Minnesota antidiscrimination law by holding that the First Amendment right of expressive association did not sanction the Jaycees’ exclusion of women. The Court stated that any restrictions on the freedom of association “may be justified by regulations adopted to serve compelling state interests, unrelated to the suppression of ideas, that cannot be achieved through means significantly less restrictive of associational freedoms.” *Id.* at 623. Furthermore, the Court found that the Minnesota statute did not “impose any serious burdens on the male members’ freedom of expressive association” and the government’s compelling interest in eradicating gender discrimination outweighed any resulting constraints. *Id.* at 626.

<sup>135</sup> *Boy Scouts*, 530 U.S. at 647, quoting *Roberts v. U.S. Jaycees*, 468 U.S. at 622.

<sup>136</sup> *Id.* at 647-648. The Court elaborated that the protection of such right is “especially important in preserving political and cultural diversity and in shielding dissident expression from suppression by the majority.” *Id.*, quoting *Roberts v. U.S. Jaycees*, 468 U.S. at 622.

<sup>137</sup> *Boy Scouts*, 530 U.S. at 641.

<sup>138</sup> Andrew Koppelman, *Signs of the Times: Dale v. Boy Scouts of America and the Changing Meaning of Nondiscrimination*, 23 CARDOZO L. REV. 1819, 1827 (2002). Koppelman continues: “The Court holds that anyone who associates with him [Dale] is therefore propounding a point of view. It evidently agrees with the claim in the Scouts’ brief that the exclusion of openly gay people was the only way that the Scouts could avoid taking a public position on the morality of homosexual conduct.” *Id.* at 1827-28.

<sup>139</sup> *Boy Scouts*, 530 U.S. at 641, 659. Koppelman notes that the Supreme Court, in holding that the state’s interests do not outweigh the Boy Scout’s rights, fails to discuss what New Jersey’s interests are. Koppelman, *supra* note 138, at 1835 n.81.

In his spirited dissent,<sup>140</sup> Justice Stevens was concerned that under the majority's standard, "the right of free speech effectively becomes a limitless right to exclude for every organization, whether or not it engages in any expressive activities."<sup>141</sup> Relying on the Court's prior decision in *Roberts*, Justice Stevens concluded that the New Jersey law did not "impose any serious burdens" on the Boy Scouts' "collective effort on behalf of [its] shared goals," nor did it compel the Boy Scouts to communicate any message that it did not wish to endorse.<sup>142</sup> Similarly, Justice Souter contended in his dissent that the Court's decision converts "the right of expressive association into an easy trump of any antidiscrimination law."<sup>143</sup> While this Article does not address the propriety of either the majority or the dissenting opinions in *Boy Scouts* with respect to the constitutional right of a charitable organization to discriminate,<sup>144</sup> this Article does raise a fundamental issue not addressed by the Supreme Court's decision – namely, whether a charitable organization's First Amendment right of expressive association might "trump" an IRS determination that the organization no longer meets the definition of "charitable" under Section 501(c)(3) due to its discriminatory practices.

To date, the Supreme Court has not addressed whether denying or revoking an organization's tax-exempt status based on its discriminatory membership policy or other exclusionary practice violates that organization's First Amendment right to expressive

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<sup>140</sup> *Boy Scouts*, 530 U.S. at 663-700. Justices Souter, Ginsberg and Breyer joined in Justice Stevens's dissent. Justice Stevens commenced his dissent with Justice Brandeis' notion that it is a state's right to experiment with "things social;" specifically, a "single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country." *Id.* at 664 (quoting *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting)). Stevens concluded that New Jersey constituted the "courageous" state to which Justice Brandeis referred and, therefore, the Supreme Court should not prevent or deter such experimentation (i.e., eliminating discrimination on the basis of sexual orientation). *Id.*; see also Erica L. Stringer, *Has the Supreme Court Created a Constitutional Shield for Private Discrimination Against Homosexuals? A Look at the Future Ramifications of Boy Scouts of America v. Dale*, 104 W. VA. L. REV. 181, 196 (2001-2002).

<sup>141</sup> *Boy Scouts*, 530 U.S. at 695 (Stevens, J., dissenting). Justice Stevens continues:

The only apparent explanation for the majority's holding, then, is that homosexuals are simply so different from the rest of society that their presence alone – unlike any other individual's – should be singled out for special First Amendment treatment. Under the majority's reasoning, an openly gay male is irreversibly affixed with the label "homosexual." That label, even though unseen, communicates a message that permits his exclusion wherever he goes. His openness is the sole and sufficient justification for his ostracism. Though unintended, reliance on such a justification is tantamount to a constitutionally prescribed symbol of inferiority.

*Id.* at 696; see also Koppelman, *supra* note 138, at 1823. See generally Evelyn Brody, *Entrance, Voice and Exit: The Constitutional Bounds of the Right of Association*, 35 U.C. DAVIS L. REV. 821 (2002).

<sup>142</sup> *Boy Scouts*, 530 U.S. at 664-65 (quoting *Roberts v. U.S. Jaycees*, 468 U.S. at 626-27). Earlier in his dissent, Justice Stevens challenged the propriety of the majority's message-based conclusions and the Boy Scouts' asserted nature of its values by pointing out that Dale was an exemplary member of the organization for greater than 12 years, attained the rank of Eagle Scout (an honor accorded to only the top three percent of all members), and selected to be Assistant Scoutmaster. It was only after Dale's homosexuality was revealed that the Boy Scouts revoked his membership, determining that he did "not meet the high standards of membership which the BSA seeks to provide for American youth." *Id.* at 665; see also Stringer, *supra* note 140, at 196.

<sup>143</sup> *Boy Scouts*, 530 U.S. at 701-2 (Souter, J., dissenting).

<sup>144</sup> For a more thorough discussion of the implications of the Supreme Court's decision in *Boy Scouts* with respect to the right of organizations to discriminate, see Andrew Koppelman, *Should Noncommercial Enterprises Have an Absolute Right to Discriminate?*, 67-FALL LAW & CONTEMP. PROBS. 27 (2004). Cf. Dale Carpenter, *Expressive Association and Anti-Discrimination Law after Dale: A Tripartite Approach*, 85 MINN. L. REV. 1515, 1517 (2001).

association.<sup>145</sup> As discussed in Part IV of this Article, the Court has sustained limitations on charitable organizations' other First Amendment rights (i.e., free speech, free exercise of religion) as a condition to exemption under Section 501(c)(3).<sup>146</sup> Notwithstanding, it is ambiguous whether the Court would similarly conclude, based on facts similar to those in *Boy Scouts*, that an organization's constitutional right to expressive association would not be seriously constrained by a revocation or denial of its Section 501(c)(3) exemption.<sup>147</sup> However, it seems unambiguous, in light of the current administration and political climate, that any governmental agency would argue that a compelling governmental interest to eradicate discrimination based on sexual orientation currently exists. Since the public policy doctrine lacks a clearly defined scope of applicability, such discrimination by charitable organizations is effectively sanctioned by current income tax law and its primary enforcer, the IRS.

### III. ALTERNATIVE PROPOSALS COMBATING DISCRIMINATION BY CHARITABLE ORGANIZATIONS

This Article is not the first to address the issue of discrimination by charitable organizations. Professor David Brennen is a pioneering scholar on the convergence of laws addressing discrimination, primarily racial, and federal income tax law governing tax-exempt organizations. Accordingly, he has analyzed and advocated potential solutions to the discrimination problem. Each of these proposed solutions has its strengths and weaknesses, and, therefore, provides valuable insights in formulating the proposal advocated in this Article. Accordingly, this Article explores these proposed solutions in greater detail below.

#### A. THE PUBLIC POLICY DOCTRINE – CLARIFICATION AND EXPANDED SCOPE?

As stated above, Professor Brennen has written extensively on the public policy doctrine as announced in *Bob Jones University*, its inherent flaws, and the proper determination of its applicability.<sup>148</sup> Some of his criticisms were discussed and evaluated previously in Part II of this Article.<sup>149</sup> He ultimately concludes that the judicially-created public policy doctrine is not the proper vehicle to combat racial discrimination and that the IRS is likely not the proper administrative agency to interpret and enforce the public policy doctrine.<sup>150</sup> In evaluating options to better apply, and effect the purposes of, the public policy doctrine, he suggests codification of the doctrine, thereby providing the necessary statutory authority for its effective application to charitable organizations.<sup>151</sup> He also advocates Congressional authorization of a federal agency other than the Treasury (i.e., IRS by delegation) to “review and rule upon complaints of discrimination by tax-exempt charities,” arguing that other agencies are better equipped at addressing such issues.<sup>152</sup> Finally, in exploring the role of constitutional law

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<sup>145</sup> Brennen, *Charities and the Constitution*, *supra* note 110, at 843.

<sup>146</sup> See *infra* notes 243 to 254 and accompanying text.

<sup>147</sup> Brennen, *Charities and the Constitution*, *supra* note 110, at 843-844.

<sup>148</sup> See generally, Brennen, *Racial Discrimination*, *supra* note 26, and Brennen, *Charities and the Constitution*, *supra* note 110.

<sup>149</sup> See *supra* notes 110-116 and accompanying text.

<sup>150</sup> Brennen, *Racial Discrimination*, *supra* note 26, at 446.

<sup>151</sup> *Id.*

<sup>152</sup> *Id.* at 446-47.

principles in establishing the doctrine’s scope, Professor Brennen concludes that that the IRS’s almost exclusive reliance on constitutional law principles in determining the boundaries of “established public policy” is inappropriate.<sup>153</sup> While observing that the public policy doctrine originates in the Internal Revenue Code (i.e., Section 501(c)(3)) and is therefore a statutory, not constitutional, principle, he illustrates that in most instances charities are private, not state, actors and, thus, are generally not subject to constitutional law limitations such as the Equal Protection Clause of the Fourteenth Amendment.<sup>154</sup> Professor Brennen ultimately concludes that the IRS should “engage in a type of analysis that considers a variety of sources constitutional, non-constitutional, federal and non-federal – in deciding if a particular charity is in violation of ‘established public policy.’”<sup>155</sup>

Principally, this Article concurs with Professor Brennen’s critique of the public policy doctrine and how the doctrine’s inherent flaws prevent its from combating effectively most discrimination by charitable organizations. However, none of the proposed fixes appears to address adequately the doctrine’s flaws. While the doctrine has been effective in eradicating racial discrimination in education, its lack of a clearly defined source of “established public policy” as well as the significant evidentiary burden placed on the IRS to determine and prove that an organization’s principles violate a fundamental public policy have rendered the doctrine woefully inadequate in combating other forms of discrimination. As previously illustrated in Part I of this Article, reliance on the doctrine to combat discrimination on the basis of marital status or sexual orientation is nonexistent and futile since such discrimination does not violate any “established” public policy. Although the existence of a national public policy against discrimination on the basis of sexual orientation has been posited,<sup>156</sup> the current administration and political climate clearly refute such a conclusion. Therein lies another fatal flaw of the doctrine – its potential exposure to the whims of current political climate due mostly to its lack of a clearly defined source of established public policy.<sup>157</sup> Despite these exposed flaws and extensive criticism by legal scholars, Congress has failed to step up and statutorily fix the doctrine’s deficiencies. Accordingly, the public policy doctrine is clearly not the best solution to combat effectively the continued problem of discrimination by charitable organizations.

## B. EXPANDING CIVIL RIGHTS LAWS’ APPLICABILITY TO CHARITABLE ORGANIZATIONS

### I. Overview

In addition to his scholarship evaluating the public policy doctrine, Professor Brennen has also explored the expansion of the civil rights laws’ scope as a means to combat discrimination by charitable organizations.<sup>158</sup> Although this expansion approach, outlined below, possesses more potential than any proposed fix to the public policy doctrine, it still fails to provide a comprehensive solution to the kinds of discrimination illustrated in this Article.

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<sup>153</sup> Brennen, *Charities and the Constitution*, *supra* note 110, at 848.

<sup>154</sup> *Id.*

<sup>155</sup> *Id.* at 849.

<sup>156</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 184; HOPKINS, *supra* note 52, § 5.4, at 125.

<sup>157</sup> In his *Bob Jones Univ.* concurrence, Justice Powell cautioned that conforming an organization’s activities to established government policy “ignores the important role played by tax exemption in encouraging diverse, indeed often sharply conflicting, activities and viewpoints.” *Bob Jones Univ.*, 461 U.S. at 609 (Powell, J., concurring).

<sup>158</sup> Brennen, *Tax Expenditures*, *supra* note 26.

Although federal protection of an individual citizen's civil rights are contained in a "framework of laws consisting of the Constitution, statutes, regulations, executive actions, and court interpretation," these laws do not apply comprehensively to any potential violator of such rights.<sup>159</sup> For instance, civil rights protection afforded by the Constitution does not apply normally unless the violator is a "state actor," of which most charitable organizations are not.<sup>160</sup> Accordingly, charitable organizations are free to discriminate on any basis without penalty unless they are subject to certain "federal statutes that impose civil rights restrictions on private, nonstate actors."<sup>161</sup> Such applicable federal statutes currently forbid discrimination based on race, gender, disability and age in programs and activities that receive "federal financial assistance" (hereinafter, "FFA").<sup>162</sup>

The enforcement mechanism with respect to such statutes' nondiscrimination requirements is contained directly in the statute, compelling the awarding governmental agency to promulgate regulations that effect the statute's objectives.<sup>163</sup> In addition to being defined statutorily as a "grant, loan, or contract other than a contract of insurance or guaranty,"<sup>164</sup> FFA has also been judicially interpreted in the context of these civil rights laws.<sup>165</sup> Essentially, FFA

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<sup>159</sup> *Id.* at 179.

<sup>160</sup> *Id.* *See id.* at 179-180 n.51 for further discussion on limited instances where charitable organizations might be deemed to be a "state actor." This Article similarly focuses on charitable organizations as private actors.

<sup>161</sup> *Id.* at 179-180.

<sup>162</sup> *Id.* at 171; *see, e.g.*, Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (2006) ("No person in the U.S. shall, on the ground of race, color, or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance . . . ."); Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681(a) (2006) ("No person in the U.S. shall, on the basis of sex, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any education program or activity receiving Federal financial assistance . . . ."); Rehabilitation Act of 1973, 29 U.S.C. § 794(a) (2006) ("No otherwise qualified individual by reason of her or his disability, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance . . . .").

<sup>163</sup> *See, e.g.*, Title VI, 20 U.S.C. § 2000d-1 (2006), which provides:

Each Federal department and agency which is empowered to extend Federal financial assistance to any program or activity, by way of grant, loan, or contract other than a contract of insurance or guaranty, is authorized and directed to effectuate the provisions of section 2000d of this title with respect to such program or activity by issuing rules, regulations, or orders of general applicability which shall be consistent with achievement of the objectives of the statute authorizing the financial assistance in connection with which the action is taken.

*Id.*; *see also* Title IX, 20 U.S.C. § 1682 (2006). The apparently standard regulation issued by federal agencies pursuant to §2000d-1 states:

The term "federal financial assistance" includes (1) grants and loans of Federal funds, (2) the grant or donation of Federal property and interests in property, (3) the detail of Federal personnel, (4) the sale and lease of, and the permission to use (on other than a casual or transient basis), Federal property or any interest in such property without consideration or at a nominal consideration, or at a consideration which is reduced for the purpose of assisting the recipient, or in recognition of the public interest to be served by such sale or lease to the recipient, and (5) any Federal agreement, arrangement, or other contract which has as one of its purposes the provision of assistance.

*See, e.g.*, 7 C.F.R. § 15.2 (Department of Agriculture); 28 C.F.R. § 42.101 (Department of Justice); 45 C.F.R. § 80.13 (Department of Health, Education and Welfare).

<sup>164</sup> *See Id.*

<sup>165</sup> *See* Brennen, *Tax Expenditures*, *supra* note 26, at 171 n.10 (*citing* Grove City College v. Bell, 465 U.S. 555 (1984) (college deemed recipient of FFA because its students received federal grants); NCAA v. Smith, 525 U.S.

constitutes “funds received directly or indirectly from the federal government.”<sup>166</sup> Thus, charitable organizations that receive direct assistance from the federal government in the form of grants or loans or that receive fees from direct recipients of FFA are required to comply with these civil rights’ laws.<sup>167</sup> To address the large number of charitable organizations which do not fall into either of these situations, Professor Brennen embarks down the arduous path of determining whether such organizations may be deemed to receive FFA in the form of certain tax benefits; principally, the income tax exemption for charitable organizations and the income tax deduction for persons making contributions to such organizations.<sup>168</sup> In making this determination, he analyzes the two federal district court opinions that reached opposite conclusions as to whether tax exemption constitutes FFA.<sup>169</sup>

In *McGlotten v. Connally*,<sup>170</sup> the federal district court determined that certain federal tax benefits constitute FFA under Title VI of the Civil Rights Act of 1964. The plaintiff in *McGlotten* filed suit to enjoin the IRS from granting exemptions to nonprofit social clubs and fraternal organizations that excluded non-white persons from their membership.<sup>171</sup> In responding to the plaintiff’s three separate counts for relief,<sup>172</sup> the *McGlotten* court specifically addresses whether various tax benefits, mainly in the form of an exemption and a deduction for contributions, granted to certain nonprofit organizations constitute FFA under Title VI of the Civil Rights Act of 1964.<sup>173</sup> The court ultimately concluded that the tax benefits granted to fraternal organizations (i.e., tax exemption and deduction for certain contributions to the organization) did constitute FFA under Title VI.<sup>174</sup> In the absence of convincing legislative history, the court relied on the “plain purpose” of Title VI in reaching its conclusion – “clearly to eliminate discrimination in programs or activities benefiting from federal financial assistance.”<sup>175</sup>

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459 (1999) (even though its college and university members received FFA, NCAA’s receipt of dues from such institutions did not constitute FFA); and *Richard Foss v. Chicago*, 817 F.2d 34 (7<sup>th</sup> Cir. 1987) (even though City of Chicago received federal funding, the City’s Fire Department not considered a recipient of FFA).

<sup>166</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 171.

<sup>167</sup> *Id.* at 171-172; *see also* *Grove City College*, 465 U.S. at 563.

<sup>168</sup> I.R.C. § 501(a) (2006) and I.R.C. § 170(a)(1) (2006), respectively.

<sup>169</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 172, 200-207.

<sup>170</sup> *McGlotten v. Connally* 338 F. Supp. 448 (D.D.C. 1972).

<sup>171</sup> *Id.* Nonprofit social clubs are exempt from federal income tax under § 501(c)(7), which describes such clubs as ones “organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.” I.R.C. § 501(c)(7) (2006). Fraternal organizations are exempt under § 501(c)(8), which describes such organizations as “operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under a lodge system, and providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents.” I.R.C. § 501(c)(8) (2006). I.R.C. § 170(c)(4) authorizes a deduction for certain contributions to fraternal organizations (i.e., contributions “used exclusively for religious, charitable, scientific, literary or education purposes . . .”).

<sup>172</sup> The three separate counts of relief sought by plaintiff are: (i) the Internal Revenue Code’s grant of certain tax benefits is unconstitutional; (ii) such benefits are not authorized by the Code, and (iii) such tax benefits constitute FFA under Title VI of the Civil Rights Act of 1964. *McGlotten*, 338 F. Supp. at 450.

<sup>173</sup> *McGlotten*, 338 F. Supp. at 450.

<sup>174</sup> *Id.* at 461-62.

<sup>175</sup> *Id.* at 461.

However, the *McGlotten* court determined that the exemption granted to nonprofit social clubs under Section 501(c)(7) did not constitute FFA.<sup>176</sup> The court reasoned that such exemption “limited as it is to member-generated funds and available regardless of the nature of the activity of the particular club, does not operate as a ‘grant’ of Federal funds,” and thus was not covered by Title VI.<sup>177</sup> Essentially, Congress determined, according to the court, that member-generated funds should not be taxed in that they are merely “shifted from one pocket to another, both within the same pair of pants. Thus the exclusion of member generated revenue reflects a determination that as to these funds the organization does not operate as a separate entity.”<sup>178</sup> In other words, as to such funds, social clubs are deemed to not function as entities separate and apart from their members.<sup>179</sup> Finally, the court reasoned that since exemption under Section 501(c)(7) was granted to a club regardless of its activities, “there is no mark of Government approval inherent in the designation of a group as exempt. Congress has simply chosen not to tax a particular type of revenue because it is not within the scope [of income] sought to be taxed by the statute.”<sup>180</sup> An opposite conclusion was reached by the court with respect to fraternal organizations because their tax exemption “operates in fact as a subsidy in favor of the particular activities these groups are pursuing,”<sup>181</sup> and was not “simply a way of defining taxable income.”<sup>182</sup> In conclusion, as Brennen points out, under *McGlotten*, a tax benefit will likely constitute FFA if Congress intended the benefit to constitute more than an “income-defining provision” and if the grant of the benefit is conditional on the benefiting organization limiting its activities to certain “government-specified purposes.”<sup>183</sup>

Contrary to *McGlotten*, the federal district court in *Bachmann v. American Society of Clinical Pathologists*<sup>184</sup> concluded that tax exemption by itself does not constitute FFA for purposes of section 504 of the Rehabilitation Act of 1973.<sup>185</sup> In *Bachmann*, the plaintiff sued the American Society of Clinical Pathologists (“ASCP”) for ASCP’s denial of her request for special testing conditions during an examination conducted by ASCP, alleging that such denial constituted discrimination against a handicapped person in violation of the Rehabilitation Act.<sup>186</sup> Although ASCP received no direct funding from the federal government, plaintiff contended that it received “indirect financial assistance” in form of its tax-exempt status.<sup>187</sup> The court stated that, “[a]lthough tax exempt status confers a substantial economic advantage on ASCP, not every

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<sup>176</sup> *Id.* at 462.

<sup>177</sup> *Id.*; *see id.* at 457-459.

<sup>178</sup> *Id.* at 458.

<sup>179</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 202.

<sup>180</sup> *McGlotten*, 338 F. Supp. at 458.

<sup>181</sup> *Id.* at 462.

<sup>182</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 203.

<sup>183</sup> *Id.* at 203-204.

<sup>184</sup> *Bachmann v. American Soc’y of Clinical Pathologists*, 577 F. Supp. 1257 (D.N.J. 1983).

<sup>185</sup> *Id.* at 1264.

<sup>186</sup> *Id.* at 1258.

<sup>187</sup> *Id.* at 1263. Although ASCP was not receiving FFA at the time of the lawsuit, it nevertheless conceded that it received two grants from the Department of Health, Education and Welfare during the period in which plaintiff applied to take the examination. *Id.* at 1260. However, the court determined that plaintiff was not subject to discrimination under the program or activity for which the FFA was received. *Id.* at 1263, *citing* *Brown v. Sibley*, 650 F.2d 760, 767 (5th Cir.1981) (“the receipt of federal financial assistance by a multiperson entity, for specific application to certain programs or activities, does not, without more, bring all of those multiple programs or activities within the reach of section 504.”).

item of economic value granted by the federal government counts as financial assistance within the meaning of section 504 of the Rehabilitation Act.”<sup>188</sup> Relying on the “plain meaning” of section 504, the court concluded that “the term ‘assistance’ connotes a transfer of government funds by way of subsidy, not merely an exemption from taxation.”<sup>189</sup> In addition to relying on administrative regulations that did not include tax-exemption as constituting FFA, the court found persuasive a the Supreme Court’s decision in *Grove City College v. Bell*<sup>190</sup> where Title IX was deemed applicable based on the educational institution’s receipt of federal grants and student loans, not its tax exempt status.<sup>191</sup>

Because Professor Brennen is advocating for a more expansive application of the civil rights laws to charitable organizations, he concludes accordingly that the broader judicial interpretations of FFA in *Grove City College* and *McGlotten* are “the preferred method of interpretation in terms of maximizing protections to those persons whose federal civil rights are violated.”<sup>192</sup> By instituting this broader interpretation, Brennen argues that parties to a civil rights suit will expend more time on determining whether discrimination has occurred rather than whether the correct form of government assistance was received in order for the civil rights law to apply.<sup>193</sup> Notwithstanding the social justice implications of a broader view of FFA, Brennen acknowledges that the lack of a Supreme decision specifying that certain tax benefits constitute FFA allows courts to interpret the term narrowly and decline to impose civil rights constraints on “nontraditional defendants,” as the *Bachman* decision illustrates.<sup>194</sup> If the tax benefit received by the defendant organization in *Bachman* was in the form of a government grant or loan, concludes

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<sup>188</sup> *Bachmann*, 577 F. Supp. at 1263.

<sup>189</sup> *Id.* at 1264.

<sup>190</sup> *Grove City College v. Bell*, 465 U.S. 555 (1984).

<sup>191</sup> *Bachmann*, 577 F. Supp. at 1264-1265, citing *Grove City College*, 465 U.S. at 555. Brennen quickly points out that the *Bachmann* court’s narrow interpretation of FFA is “clearly at odds” with the broader notion espoused by the Supreme Court in *Grove City College*, where the Court “urges against such a narrow view.” Brennen, *Tax Expenditures*, *supra* note 26, at 206. To support his conclusion, Brennen quotes the Supreme Court:

Nothing in [Title IX] suggests that Congress elevated form over substance by making the application of the nondiscrimination principle dependent on the manner in which a program or activity receives federal assistance. There is no basis in [Title IX] for the view that only the institutions that themselves apply for federal aid or receive checks directly from the Federal Government are subject to regulation. As the Court of Appeals observed, “by its all inclusive terminology [Title IX] appears to encompass all forms of federal aid to education, direct or indirect.” We have recognized the need to “accord [Title IX] a sweep as broad as its language,” and we are reluctant to read into Title IX a limitation not apparent on its face.

*Grove City College*, 465 U.S. at 564. See also Galvin & Devins, *supra* note 85, at 1375, citing Bittker & Kaufman, *Taxes and Civil Rights: ‘Constitutionalizing’ the Internal Revenue Code*, 82 YALE L.J. 51, 62 (1972) (“[T]he ‘tax-subsidy’ rationale of the *McGlotten* case has implications beyond the area of racial restrictions. . . . *McGlotten*’s logic apparently prohibits the granting of tax allowances to a fraternal order that imposes such restrictions (based on its customers’ religion, national or ethnic origin, political allegiance, sex, and perhaps other characteristics). . . . Finally, nothing in *McGlotten* limits its reach to income, estate and gift taxes; ‘subsidies’ in the form of exemptions, deductions, special rates, and similar allowances may be found in other federal taxes, as well as in state and local taxes.”).

<sup>192</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 207.

<sup>193</sup> *Id.*

<sup>194</sup> *Id.* Brennen defines “nontraditional defendants” as “those civil rights defendants who are not state actors and who do not receive traditional forms of FFA like government loans or grants.” *Id.* n.206.

Brennen, the plaintiff would have likely succeeded in her argument that the Rehabilitation Act applied.<sup>195</sup>

Other than its general interpretation of FFA under the civil rights' laws, the United States Supreme Court has not specifically considered whether certain tax benefits like tax-exemption constitute FFA.<sup>196</sup> However, as Professor Brennen points out, the Court has concentrated on the related issue of whether certain tax benefits should be considered government expenditures or government neutrality for constitutional law purposes – the well-known “tax expenditure” theory or conundrum in federal income tax law.<sup>197</sup> Although the propriety of the tax expenditure theory is well beyond the scope of this Article, a brief explanation and illustration of the concept is necessary to fully comprehend Professor Brennen’s conclusion with respect to the expanded applicability of the civil rights laws to charitable organizations.

The primary question that drives the tax expenditure theory is whether the receipt of a tax benefit (e.g., deduction, exclusion, exemption) should be legally regarded as equivalent to a direct government grant of money.<sup>198</sup> To illustrate, if an organization is deemed to qualify for tax-exempt status under Section 501(c)(3), should that organization be viewed, for legal purposes, as receiving a direct government grant of money (i.e., in the form of forgone income taxes)? Under the tax expenditure theory, the organization’s exemption is deemed equivalent to a direct government outlay of cash.<sup>199</sup> A similar analysis could be employed with respect to the charitable contribution deduction – the tax expenditure theory treats the amount of the deduction as equivalent to a direct government grant of money to the taxpayer claiming the deduction.<sup>200</sup> Such equivalency under the tax expenditure theory “applies only to tax benefits enacted to implement social policy – not those intended as a further delineation of the appropriate tax base.”<sup>201</sup> For instance, tax benefits received by a social club exempt under Section 501(c)(7) (as in the *McGlotten* case) would not be equated with a government grant or loan since the club’s

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<sup>195</sup> *Id.*

<sup>196</sup> *Id.* at 173; see *Grove City College*, 465 U.S. at 563. Cf. *Walz v. Tax Comm. of New York*, 397 U.S. 664, 675 (1970) (“The grant of a [state property] tax exemption is not sponsorship since the government does not transfer part of its revenue to churches but simply abstains from demanding that the church support the state. No one has ever suggested that tax exemption has converted libraries, art galleries, or hospitals into arms of the state or put employees ‘on the public payroll.’ There is no genuine nexus between tax exemption and establishment of religion.”).

<sup>197</sup> See Brennen, *Tax Expenditures*, *supra* note 26, at 173, 208-25; see also *infra* note 203.

<sup>198</sup> *Id.* at 208-209, citing STANLEY S. SURREY, *PATHWAYS TO TAX REFORM: THE CONCEPT OF TAX EXPENDITURES* 6-7, 30-49 (1973); STANLEY S. SURREY & PAUL R. MCDANIEL, *TAX EXPENDITURES* 1-30 (1985).

<sup>199</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 209. See, e.g., *Regan v. Taxation With Representation of Washington*, 461 U.S. 540, 544 (1983) (“Both tax exemptions and tax deductibility are a form of subsidy that is administered through the tax system. A tax exemption has much the same effect as a cash grant to the organization of the amount of tax it would have to pay on its income. Deductible contributions are similar to cash grants of the amount of a portion of the individual’s contributions.”); *Walz v. Tax Commission*, 397 U.S. at 699 (In his concurrence, Justice Harlan agrees with Justice Douglas that “exemptions do not differ from subsidies as an economic matter”); *Id.* at 704 (Justice Douglas stating that “[a] tax exemption is a subsidy”).

<sup>200</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 209.

<sup>201</sup> *Id.* at 209-210, citing SURREY, *supra* note 198, at 6 (“The federal . . . tax system consists . . . of two parts: one part comprises the structural provisions necessary to implement the income tax . . . ; the second part comprises a system of tax expenditures under which . . . financial assistance programs are carried out through special tax provisions rather than through direct Government expenditures.”).

exemption is not intended to effect any social policy, but simply defining taxable income.<sup>202</sup> Accordingly, under the tax expenditure theory, a tax benefit or expenditure that accomplishes a social purpose and a direct government outlay for the identical purpose are equivalent, both economically and for constitutional law purposes.<sup>203</sup>

Although Brennan primarily accepts the economic equivalence concept contained in the tax expenditure theory to support his thesis, he appears to join other scholars in limiting its impact in the constitutional law context.<sup>204</sup> He contends that economic equivalence for purposes of interpreting and applying federal civil rights laws differs from applying such equivalence in a case involving constitutional law.<sup>205</sup> For example, government or state involvement is crucial in determining whether a First Amendment violation occurs due to government funding. However, such involvement is less critical in applying federal civil rights laws where the existence of government funding to a private individual or entity is significant as well as “whether Congress intended that the financial benefit support the private party’s activities.”<sup>206</sup> Professor Brennan ultimately concludes that “tax expenditure theory can and should be used to equate tax benefits received by charities with government grants and loans received by various private parties.”<sup>207</sup> In other words, a charitable organization’s income tax exemption should be treated as FFA for purposes of subjecting that organization to federal civil rights laws.

## 2. *Critique of the Civil Rights Laws’ Expansion Proposal*

Again, this Article principally agrees with Professor Brennan’s approach with respect to charitable organizations and discrimination – “Discriminate if you choose, but not with federal subsidies.”<sup>208</sup> While the persuasiveness and viability of Professor Brennan’s civil rights laws’ expansion proposal are undeniable, the proposal’s very weakness is its reliance on such laws to

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<sup>202</sup> *Id.* at 227; *see also supra* notes 178-183 and accompanying text.

<sup>203</sup> *Id.* at 210. “Constitutional equivalence” is best illustrated by an example. While a church’s income tax exemption may be economically equivalent to the receipt of a direct government grant under the tax expenditure theory, the two benefits may not be similarly permissible under constitutional law principles (i.e., lack constitutional equivalence). The direct government grant may be seen as violating the First Amendment Establishment Clause while the tax exemption may be seen as government neutrality and thus, constitutionally permissible. *See e.g., Walz*, 397 U.S. at 674-75 (Supreme Court held that an exemption from state property tax for land and buildings owned by churches and used solely for religious worship did not violate First Amendment’s Establishment Clause. The Court characterized such exemptions as “benevolent neutrality” that neither advanced nor inhibited religion and created only a minimal and remote “entanglement” between church and state.).

<sup>204</sup> Brennan, *Tax Expenditures*, *supra* note 26, at 210 and 224.

<sup>205</sup> *Id.* at 224. Brennan states that “scholars contend that courts should place less emphasis on economic equivalence when making constitutional law decisions and more emphasis on the particular constitutional context. For example, one scholar ‘calls for a case-by-case determination [] of equivalence by considering the particular constitutional contexts, the specific tax and direct spending programs at issue, and the appropriate perspective in each of those contexts.’” *Id.* at 210, *citing* Edward A. Zelinsky, *Are the Tax “Benefits” Constitutionally Equivalent to Direct Expenditures?*, 112 HARV. L. REV. 379, 382 (1998). Brennan ultimately concludes that the appropriateness of such “scholars’ calls for less strict adherence to the tax expenditure theory in constitutional cases” is beyond the scope of his thesis. *Id.* at 224.

<sup>206</sup> Brennan, *Tax Expenditures*, *supra* note 26, at 224; *see also* Galvin & Devins, *supra* note 85, at 1376 (“Thus, a tax exemption might be permissible under the establishment clause but impermissible under the Civil Rights Act of 1964.”).

<sup>207</sup> Brennan, *Tax Expenditures*, *supra* note 26, at 224-225; *see also* Galvin & Devins, *supra* note 85, at 1378 n.118 (Article adopts “the view that tax exemptions are government aid for purposes of the 1964 Civil Rights Act.”).

<sup>208</sup> Brennan, *Tax Expenditures*, *supra* note 26, at 228.

combat the kind of ongoing discrimination by charitable organizations illustrated in Part I of this Article. First and foremost, current civil rights laws are limited in their application, protecting against discrimination on the basis of race, color, national or ethnic origin, religion, sex or gender, age, and disability.<sup>209</sup> They do not prohibit discrimination on the bases of sexual orientation or marital status,<sup>210</sup> both of which appear to be the most common instances of discrimination currently engaged in by charitable organizations.<sup>211</sup> Brennen even refers to discrimination on the basis of sexual orientation as “harmful discriminatory behavior” by charitable organizations,<sup>212</sup> but fails to further explain how his proposal to expand the application of civil rights laws as currently written will combat such harmful discrimination. An additional hurdle created by Professor Brennen’s proposal is its reliance on a more expansive interpretation of FFA. Although this Article agrees with Professor Brennen’s conclusion that FFA should include such tax benefits as exemption and deductibility of contributions by donors to the organization, the Supreme Court has not made such a determination and lower courts are not in agreement, as illustrated by the decisions in *McGlotten* and *Bachman*.<sup>213</sup> Until the Supreme Court addresses this issue directly, the use of civil rights laws to combat the discrimination problem fails to comprehensively address the problem. Furthermore, as with all issues involving statutory interpretation, it can be argued that if Congress intended to extend the nondiscrimination provisions in the civil rights’ laws specifically to charitable organizations it could have done so by including specific language in the statutes or by directing the promulgation of administrative regulations.<sup>214</sup> As stated by the Second Circuit in a case attempting to expand civil rights protection granted by Title VII, Congressional inaction can be “strong evidence of congressional intent.”<sup>215</sup>

Despite the merits of Professor Brennen’s proposal, which was published over six years ago, it unfortunately does not reflect current reality. Even if courts interpreted FFA broadly enough to encompass tax benefits such as exemption and the charitable contributions deduction, current civil rights laws would not prohibit charitable organizations from discriminating on the basis of sexual orientation and marital status. To truly accomplish Professor Brennen’s goal of combating *all* discrimination by charitable organizations, current civil rights laws would need to be amended and expanded to prohibit discrimination on such bases. For such statutory

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<sup>209</sup> See *supra* note 162; see also Brennen, *Tax Expenditures*, *supra* note 26, at 179 n.49.

<sup>210</sup> See *e.g.*, *Simonton v. Runyon*, 232 F.3d 33, 35 (2d Cir. 2000) (“Although congressional inaction subsequent to the enactment of a statute is not always a helpful guide, Congress’s refusal to expand the reach of Title VII is strong evidence of congressional intent in the face of consistent judicial decisions refusing to interpret ‘sex’ to include sexual orientation.”); *Wrightson v. Pizza Hut of Am., Inc.*, 99 F.3d 138, 143 (4th Cir.1996) (“Title VII does not afford a cause of action for discrimination based upon sexual orientation.”); *Williamson v. A.G. Edwards & Sons, Inc.*, 876 F.2d 69, 70 (8th Cir.1989) (“Title VII does not prohibit discrimination against homosexuals.”); *DeSantis v. Pacific Tel. & Tel. Co.*, 608 F.2d 327, 329-330 (9th Cir. 1979) (“Title VII’s prohibition of ‘sex’ discrimination applies only to discrimination on the basis of gender and should not be judicially extended to include sexual preference such as homosexuality.”); see also Brennen, *Tax Expenditures*, *supra* note 26, at 170 n.6.

<sup>211</sup> See *supra* notes 13-25 and accompanying text. Because instances of alleged or actual discrimination must either be reported in the press or result in a lawsuit in which a court decision is issued, there is no way to verify, other than by these means, the amount and type of occurrences of discrimination involving charitable organizations.

<sup>212</sup> Brennen, *Tax Expenditures*, *supra* note 26, at 169.

<sup>213</sup> See *supra* notes 170-191, and 196, and accompanying text.

<sup>214</sup> See *generally*, Title VI of the Civil Rights Act of 1964, 42 U.S.C. § 2000d (2006). A similar criticism can be levied equally against the proposal set forth in this Article.

<sup>215</sup> *Simonton*, *supra* note 210, 232 F.3d at 35.

amendments to occur, Congressional intent must exist to prohibit such discrimination by private actors other than just charitable organizations – for example, the business community. The existence of such intent is dubious at best. Nevertheless, as proposed below, a more tailored legislative fix could prove more effective in preventing federal public monies (i.e., tax benefits) from being utilized by charitable organizations to discriminate against any class of citizens.

#### IV. AMENDMENT OF SECTION 501(c)(3) TO ESTABLISH A NONDISCRIMINATION REQUIREMENT FOR TAX EXEMPTION

Part I of this Article illustrates the ostensibly common practice of discrimination by charitable organizations.<sup>216</sup> As discussed in Part II, federal income tax law with respect to charitable organizations does not explicitly address nor proscribe discrimination by such organizations.<sup>217</sup> The only possible restraint on discrimination exists in the public policy doctrine enunciated by the Supreme Court in *Bob Jones University*. However, as discussed previously, the public policy doctrine is fraught with limitations, including the lack of a clearly defined source of “established public policy.”<sup>218</sup> As a consequence, the doctrine has only been used as the basis to deny or revoke tax-exempt status of organizations that participated in racial discrimination, advocated civil disobedience, or involved themselves in an illegal activity.<sup>219</sup> As further illustrated in Part III of this Article, current civil rights’ laws are limited in their application and do not prohibit currently the most common bases of discrimination by charitable organizations – sexual orientation and marital status. In addition, even if certain discrimination is covered by the civil rights’ laws, such laws do not apply to a charitable organization unless it receives FFA.<sup>220</sup> The issue of whether FFA should be confined narrowly to a direct government grant or loan or include such “indirect” benefits as tax exemption and the charitable contributions deduction is not resolved definitively.<sup>221</sup> Accordingly, the existing deficiencies in current federal law effectively sanction most discrimination by charitable organizations.

##### A. THE PROPOSAL

In light of the above, this Article propounds that the most effective and comprehensive solution to eliminate discrimination by charitable organizations is the enactment of a broad and well-defined nondiscrimination requirement within Section 501(c)(3). As stated in this Article’s introduction, inherent in this proposal is the notion that discrimination by a charitable organization in any circumstance (employment, provision of services, etc.) is intrinsically incompatible with the organization’s charitable purpose and mission. This nondiscrimination provision should be based on currently existing language in the civil rights’ laws referenced in Part III but expanded to reflect the bases on which charitable organizations are most commonly discriminating – sexual orientation and marital status. Because it is contained in a federal income tax exemption statute, Congress may be more open to such an expanded prohibition

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<sup>216</sup> See *supra* notes 13-25 and accompanying text.

<sup>217</sup> See *supra* note 27 and accompanying text.

<sup>218</sup> See *supra* notes 110-118 and accompanying text.

<sup>219</sup> See *supra* note 30.

<sup>220</sup> See *supra* notes 162-164 and accompanying text.

<sup>221</sup> See *supra* notes 170-196 and accompanying text.

since its applicability is limited to nonprofit organizations exempt from federal income tax and not to for-profit, private actors like businesses. This proposal can be instituted by adding a subparagraph to Section 501(c)(3) similar to the following:

(A) No organization described under subsection (c)(3) shall exclude from participation in, deny the benefits of, or subject to discrimination in, any of its programs or activities, including its employment practices, any person in the United States on the basis of race, color, national or ethnic origin, sex or gender, age, handicap, disability, religion, marital status, or sexual orientation.<sup>222</sup>

Many reasons support the proposal set forth above. By not relying on an ill-defined public policy doctrine or civil rights' laws that are questionably applicable, a nondiscrimination requirement in Section 501(c)(3) offers a more comprehensive solution to the problem presented in this Article. Furthermore, by imposing the requirement directly in the statute that grants tax-exempt status, a strong and symbolic message is being sent to both potential and existing charitable organizations that discriminatory policies and practices are fundamentally inconsistent with tax-exempt status under Section 501(c)(3). Instead, *nondiscriminatory* practices and policies comport with the commonly accepted notion of being "charitable" and conferring public benefit.<sup>223</sup> More importantly, a statutory prohibition on discrimination transforms Section 501(c)(3) into the "gold standard" for all organizations exempt from federal income tax under Section 501(a).<sup>224</sup> Since a corresponding benefit of being exempt under Section 501(c)(3) is the ability to provide donors a charitable contributions deduction under Section 170,<sup>225</sup> such transformation ensures that charities' beneficiaries are as diverse and all encompassing as the taxpaying public from whom such organizations draw their support. In other words, the flow of tax-deductible dollars generated by the Section 170 deduction should not be used to discriminate against a particular segment of society since the significant cost of providing such tax benefit (an estimated \$232 billion over the next five years) is bore by all taxpayers.<sup>226</sup>

In line with the above arguments, the granting of a tax exemption under Section 501(c)(3) to an organization can be viewed as resulting in a "social contract" between the organization, the

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<sup>222</sup> See *infra* note 310 and accompanying text for possible exceptions to this nondiscrimination requirement.

<sup>223</sup> See *supra* note 117 and accompanying text (arguing that a federal public policy either exists or is presently in development against discrimination on the basis of sexual orientation or marital status, among other bases). See generally, Johnny Rex Buckles, *The Community Income Theory of the Charitable Contributions Deduction*, 80 IND. L. J. 947, 977 (2005) ("[C]harities primarily produce community income. In theory, charities exist for no reason other than to benefit the community.").

<sup>224</sup> See *supra* note 39. In addition to its definition with respect to the monetary standard, "gold standard" is defined generally as a "benchmark" or "something that serves as a standard by which others may be measured or judged." MERRIAM-WEBSTER ONLINE DICTIONARY (2006). It is defined similarly as "[a] model of excellence." THE AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE, (4<sup>th</sup> ed. 2000).

<sup>225</sup> See *supra* note 40 and accompanying text.

<sup>226</sup> See *supra* note 2 and accompanying text; see also, Andrew Chamberlain and Mark Sussman, *Charities and Public Goods: The Case for Reforming the Federal Income Tax Deduction for Charitable Gifts*, TAX FOUNDATION SPECIAL REPORT, No. 137 at p. 7 (2005), available at <http://www.taxfoundation.org/publications/show/1191.html> (last visited Sept. 7, 2006) ("The charitable deduction shifts part of the cost of private charitable giving onto the rest of society.").

government and taxpayers.<sup>227</sup> Although not proposed as constituting a legally enforceable obligation,<sup>228</sup> this social contract concept suggests that there are certain purposes and activities that society attributes to an organization with “charitable” tax-exempt status under Section 501(c)(3). In contrast, certain actions, such as discrimination, do not comport with society’s notion of what constitutes a charity and, thus, violate or undermine this social contract. A charitable organization’s violation of this social contract will likely cause a shift in the public’s perception and support, with unfavorable results to the organization. This is best illustrated by the adverse impact that negative publicity can have on a charitable organization’s receipt of donations and other financial support. For instance, both the United Way of the National Capital Area, in response to its publicized financial scandal, and the Boy Scouts of America, as a result of its exposed ban on homosexual members, suffered such adverse financial impact.<sup>229</sup> Finally, to further bolster the notion of a social contract, the Supreme Court alluded to the existence of such a contract in explaining its expansive view of “charitable” (i.e., that a charitable overlay to Section 501(c)(3) exists) in *Bob Jones University*:

When the Government grants exemptions or allows deductions *all taxpayers are affected; the very fact of the exemption or deduction for the donor means that other taxpayers can be said to be indirect and vicarious "donors."* Charitable exemptions are justified on the basis that the exempt entity confers a public benefit--a benefit which the society or the community may not itself choose or be able to provide, or which supplements and advances the work of public institutions already supported by tax revenues. History buttresses logic to make clear that, to warrant exemption under § 501(c)(3), an institution must fall within a category specified in that section and must demonstrably serve and be in harmony with the public interest. *The institution's purpose must not be so at odds*

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<sup>227</sup> The notion of equating tax-exempt status under Section 501(c)(3) with a “social contract” was espoused by Kim Brombacher, one of the research assistants contributing to this article.

<sup>228</sup> This social contract theory should not be equated with assertions made by litigations in recent cases that an “express or implied contract arises between an organization and the federal government” upon granting of exempt status under Section 501(c)(3). HOPKINS, *supra* note 52, § 5.5(g), at p. 24 (Suppl. 2006) (citations omitted) (“The principal contention in this regard has been that tax exemption accorded to hospitals gives rise to a contract obligating the exempt hospital to provide medical care to uninsured patients without regard to their ability to pay for the care. This assertion, however, has been uniformly rejected.”). Similarly, tax exemption does not create third-party beneficiaries to any such implied contract nor does it create a private right of action to such beneficiaries. *Id.* at 25 (citations omitted).

<sup>229</sup> See, e.g., Brad Wolverton, *D.C. United Way Dealer Sentenced to Jail Time*, Chronicle of Philanthropy, May 17, 2004, available at <http://philanthropy.com/free/update/2004/05/2004051701.htm> (last visited Sep. 7, 2006) (“Since news reports about Mr. Suer's actions started appearing in 2002, the United Way of Washington has suffered incalculable harm. . . . During the organization's 2003-4 fund-raising campaign, private donations shrank to \$38-million; in 2001, the group raised more than \$90-million. The organization, which formerly employed about 90 people, now has 35 employees.”); Jacqueline L. Salmon, *Area United Way's Ex-Chief Admits \$500,000 Fraud*, Washington Post, Mar. 5, 2004, at B01, available at [http://www.washingtonpost.com/ac2/wp-dyn?pagename=article&contentId=A31702-2004Mar4&not\\_Found=true](http://www.washingtonpost.com/ac2/wp-dyn?pagename=article&contentId=A31702-2004Mar4&not_Found=true) (last visited Sep. 7, 2006); Jon E. Dougherty, *United Way chapters reject Boy Scouts, Ban on homosexual scoutmasters ticks off super-charity*, WorldNetDaily, July 20, 2000 available at [http://www.worldnetdaily.com/news/article.asp?ARTICLE\\_ID=15422](http://www.worldnetdaily.com/news/article.asp?ARTICLE_ID=15422) (last visited Sep. 7, 2006) (In response to the Supreme Court’s decision in *Dale*, the Southeastern New England chapter of United Way adopted a new policy that would cut off funding to any group that “discriminate[s] for any reason, including sexual orientation. . . . [T]he charity sent letters outlining the policy to 65 groups that receive about \$7.3 million in funding. . . .”); Lambda Legal, *The Impact of the Boy Scouts of America's Anti-Gay Discrimination*, available at <http://www.lambdalegal.org/cgi-bin/iowa/news/fact.html?record=1325> (last visited Sep. 7, 2006).

*with the common community conscience as to undermine any public benefit that might otherwise be conferred.*<sup>230</sup>

In setting forth its proposal, this Article embraces this social contract premise and affirms that discrimination of the kind illustrated in Part I is at odds with the common community conscience and the notion of what constitutes a charity and, therefore, undermines any public benefit that such charities otherwise confer. Accordingly, in light of such discriminatory practices or policies, such charities should no longer be considered “charitable” and, thus, tax-exempt under Section 501(c)(3).

In addition to the difficulties discussed below,<sup>231</sup> another possible effect of this Article’s proposal may be a reduction in the number of organizations that qualify for exempt status under Section 501(c)(3). However, such a reduced eligibility for Section 501(c)(3) exempt status is neither a novel nor an exceedingly unpopular notion. With approximately 1.1 million organizations currently exempt under Section 501(c)(3) (including over 63,400 organizations added in fiscal year 2005)<sup>232</sup> whose assets exceed \$1.9 trillion,<sup>233</sup> many commentators have propounded alternatives to the current tax-exemption scheme that could effectively limit the number of charitable organizations.<sup>234</sup> As stated by one such commentator with respect to his proposal that rethinks the current exemption scheme, “[s]uch a position, of course, would cut a

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<sup>230</sup> *Bob Jones Univ.*, 461 U.S. at 591-92 (emphasis added).

<sup>231</sup> See *infra* notes to and accompanying text.

<sup>232</sup> IRS Business Master File (December 2005), Tables 21 and 22, available at <http://www.irs.gov/taxstats/article/0..id=102174.00.html> (last visited Sep. 7, 2006). The number of organizations exempt under Section 501(c)(3) is actually larger than 1.046 million reported by the IRS because certain organizations, such as churches, integrated auxiliaries, subordinate units, and conventions or associations of churches, need not apply for recognition of tax-exemption, unless they specifically request a ruling. In addition, such organizations are not required to file annual information returns with the IRS. *Id.*

<sup>233</sup> Diane Freda, *Latest IRS Statistics Show Assets of Charitable Organizations Increasing*, Daily Tax Rep. (BNA) Aug. 28, 2006, at G-5.

<sup>234</sup> See, e.g., Thomas Kelley, *Rediscovering Vulgar Charity: A Historical Analysis of America’s Tangled Nonprofit Law*, 73 *FORDHAM L. REV.* 2437, 2491-92 (2005) (proposes altering the definition of charity to include 2 distinct categories – (i) a “vulgar” charity, whose mission and resources are devoted exclusively to serving the poor, and which is subject to a permissive destination-of-income test so as to more liberally earn support for its cause, and (ii) non-vulgar charities that are currently regarded as “public benefit organizations” under Section 501(c)(3)); John D. Colombo, *The Role of Access in Charitable Tax Exemption*, 82 *WASH. U. L.Q.* 343 (2004) (in cases where nonprofit entities provide “commercially similar” services to for-profit (e.g., nonprofit hospital) as well as other instances, the primary criterion of exemption under Section 501(c)(3) should be one of “enhancing access;” namely, to provide access to services to underserved populations or services to the general population not otherwise provided by for-profit entities); Borek, *supra* note 60, 31 *WM. MITCHELL L. REV.* at 222 and 225 (Since the “combination of tax deductions and exemptions is “more the result of historical accident than any cognizable jurisprudential logic,” the article proposes the “decoupling” of the charitable contribution deduction and exemption and redefining “charitable” from a “catch-all category of exempt activities not otherwise delineated” to a term “reserved for organizations the primary purpose of which is to benefit the poor); Lars G. Gustafsson, *The Definition of “Charitable” for Federal Income Tax Purposes: Defrocking the Old and Suggesting Some New Fundamental Assumptions*, 33 *HOUS. L. REV.* 587, 647 (1996) (“Given the broad scope of the term charitable under trust law, it does not serve well for income tax exemption and deductibility purposes. Organizations that would hardly stand a chance of receiving a direct subsidy from the government receive an indirect subsidy by virtue of their section 501(c)(3) status. It is one thing for a society to recognize (and, in some cases to tolerate) an organization’s existence; it is a far different matter to require society to financially support, even indirectly, that organization.”).

very wide swath through current exempt organizations . . . but it would end the current uncertainty. . . .<sup>235</sup>

Ultimately, if an organization’s exemption under Section 501(c)(3) is denied or revoked due to a nondiscrimination requirement, that organization may still qualify for exempt status under Section 501(c)(4) as a “social welfare” organization.<sup>236</sup> However, donations to social welfare organizations do not qualify for the charitable contribution deduction under Section 170(a).<sup>237</sup> Nevertheless, such lack of deductibility accomplishes one of the core themes to the proposal set forth herein – the stream of tax-deductible dollars received by charitable organizations should not be used to discriminate against any member of society.

## B. DIFFICULTIES AND POTENTIAL CRITICISMS

The proposed inclusion of a nondiscrimination requirement within Section 501(c)(3) is not intended to end all necessary discussion on the real problem of discrimination by charitable organizations. Rather, the proposal set forth herein is intended to raise awareness to the problem and to provide a solution that is more comprehensive than federal law currently provides. As with all new legal foundations, there are difficulties in applying this nondiscrimination requirement to the tax-exempt organization community as it is currently structured. This Article attempts to confront some of those difficulties and likely criticisms below while acknowledging that many potential issues are beyond its scope and will require further discussion.

### 1. *Constitutionality Issues*

One of the major criticisms of the proposal set forth in this Article will likely mirror those lobbied against the New Jersey Supreme Court’s decision in *Dale v. Boy Scouts of America*,<sup>238</sup> namely, that a broad, nondiscrimination requirement within Section 501(c)(3) violates an organization’s First Amendment rights to free speech, religious expression, and association, among others.<sup>239</sup> In other words, the imposition of such a nondiscrimination requirement would

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<sup>235</sup> Colombo, *supra* note 234, at 386.

<sup>236</sup> Section 501(c)(4) grants tax-exempt status to “[c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.” I.R.C. § 501(c)(4) (2006). However, there may be an argument that discriminatory policies or practices conflict with the regulatory definition of social welfare, which provides that, “[a]n organization is operated exclusively for the promotion of social welfare if it is *primarily engaged in promoting in some way the common good and general welfare of the people of the community*. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements.” Treas. Reg. § 1.501(c)(4)-1(a)(2)(i) (as amended in 1990) (emphasis added).

<sup>237</sup> See *supra* note 40.

<sup>238</sup> *Dale*, 734 A.2d at 1196.

<sup>239</sup> See Roy Whitehead, Jr. and Walter Block, *The Boy Scouts, Freedom of Association, and the Right to Discriminate: A Legal, Philosophical, and Economic Analysis*, 29 OKLA. CITY U.L. REV. 851 (2004). Although the article does not address tax exemption issues, it vehemently argues that “[f]reedom of association is a necessary condition of a civilized order; laws prohibiting discrimination violate this freedom and must be repealed. All of them.” *Id.* at 882. See also Erez Reuveni, *On Boy Scouts and Anti-Discrimination Law: The Associational Rights of Quasi-Religious Organizations*, 86 B.U. L. REV. 109, 113 (2006) (contends that “quasi-religious” organizations like the Boy Scouts deserve “greater associational protections” than purely secular organizations under the First

violate the First Amendment because it “would significantly affect . . . [an organization’s] ability to advocate public or private viewpoints.”<sup>240</sup> As previously discussed in Part II of this Article, the Supreme Court has not addressed whether denying or revoking an organization’s tax-exempt status based on a discriminatory policies or practices violates that organization’s First Amendment right.<sup>241</sup> However, the Supreme Court has sustained other restrictions on charitable organizations’ activities as a condition to exemption under Section 501(c)(3), dismissing any claim that such restrictions violated the organization’s First Amendment rights. In reviewing one such decision below, it is important to note that that tax exemption is typically viewed as a Congressional grant or gift, not a constitutional right or privilege.<sup>242</sup>

In *Regan v. Taxation With Representation of Washington*,<sup>243</sup> a nonprofit organization was organized to promote what it perceived to be the “public interest” in the area of federal taxation.<sup>244</sup> Taxation With Representation of Washington (TWR) was formed in a reorganization involving two other non-profit corporations, one of which was exempt under Section 501(c)(3) and the other of which was exempt under Section 501(c)(4) due to its lobbying activities. In denying TWR’s application for exemption under Section 501(c)(3), the IRS determined that a substantial part of TWR’s activities would consist of attempting to influence legislation in violation of the “no substantial part” limitation on lobbying activities contained in Section 501(c)(3).<sup>245</sup> In addressing TWR’s argument that such lobbying limitation violated its First Amendment rights,<sup>246</sup> the Supreme Court first explained that “[b]oth tax exemptions and tax-deductibility are a form of subsidy that is administered through the tax system,” analogizing

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Amendment; specifically, courts should acknowledge such organizations’ religious character to “better effectuate the underlying purposes of the [First Amendment’s] religion clauses.”), Christopher Ramey, *Revealing the Inadequacy of AB17: How Dictating Morality Upon Faith-Based Organizations Will Wreak Havoc on California’s Economy*, 26 T. JEFFERSON L. REV. 125 (2003) (rejects California’s then-proposed legislation AB17 (requires, beginning in 2007, employers with state contracts valued at \$100,000 or more to provide the same benefits to spouses and domestic partners of employees) as imposing on the moral convictions of faith-based organizations that contract with the State), and Dale Carpenter, *Expressive Association and Anti-Discrimination Law after Dale: A Tripartite Approach*, 85 MINN. L. REV. 1515 (2001).

<sup>240</sup> *Boy Scouts*, 530 U.S. at 650.

<sup>241</sup> See *supra* note 145 and accompanying text.

<sup>242</sup> See *Christian Echoes National Ministry, Inc. v. U.S.*, 470 F.2d 849, 857 (10<sup>th</sup> Cir. 1972) (“*In light of the fact that tax exemption is a privilege, a matter of grace rather than right, we hold that the limitations contained in Section 501(c)(3) withholding exemption from nonprofit corporations do not deprive Christian Echoes of its constitutionally guaranteed right of free speech.*”) (emphasis added).

<sup>243</sup> *Regan v. Taxation With Representation of Washington*, 461 U.S. 540 (1983).

<sup>244</sup> *Id.* at 540.

<sup>245</sup> Section 501(c)(3) provides that “no substantial part of the activities of . . . [the organization] is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h) ), . . .” I.R.C. 501(c)(3) (2006).

<sup>246</sup> The Supreme Court also dismisses TWR’s argument that the lobbying limitation within Section 501(c)(3) violates the equal protection component of the Fifth Amendment’s Due Process Clause, finding that it was rational for Congress to decide that it would subsidize lobbying by veteran’s organizations even though it would not subsidize substantial lobbying by other charities. *Regan*, 461 U.S. at 541. The Court explained that veterans have “been obliged to drop their own affairs and take up the burdens of the nation,” and that the U.S. has a long tradition of “compensating veterans for their past contributions by providing them with numerous advantages,” which has been deemed legitimate. *Id.* at 551-552.

such benefits to cash grants to the organization.<sup>247</sup> The Court further clarified that “Congress chose not to subsidize lobbying as extensively as it chose not to subsidize other activities that non profit organizations undertake to promote the public welfare.”<sup>248</sup>

Although it agreed with TWR’s assertion that “the government may not deny a benefit to a person because he exercises a constitutional right,” the Court countered by stating that the Internal Revenue Code does not restrict TWR’s ability to receive deductible contributions in support of its non-lobbying activities.<sup>249</sup> Rather, “Congress has merely refused to pay for lobbying out of public monies.”<sup>250</sup> To support its conclusion, the Court cited its prior decision in *Cammarano v. United States*,<sup>251</sup> which involved a Treasury Regulation that forbade business deductions for lobbying expenses, where it determined similarly that “Congress is not required by the First Amendment to subsidize lobbying.”<sup>252</sup> In *Cammarano*, the Supreme Court further rejected the “notion that First Amendment rights are somehow not fully realized unless they are subsidized by the State.”<sup>253</sup>

Of particular importance, the Court reminded TWR that it still qualified for exemption under Section 501(c)(4) as a social welfare organization and could obtain deductible contributions for its non-lobbying activities by returning to the dual structure from which it originated (i.e., an entity exempt under Section 501(c)(3) for non-lobbying activities and a related entity exempt under Section 501(c)(4) that performed a lobbying function).<sup>254</sup> However, the Court did caution that TWR needed to ensure that the charitable organization did not subsidize the Section 501(c)(4) entity, “otherwise, public funds might be spent on an activity Congress chose not to subsidize.”<sup>255</sup>

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<sup>247</sup> *Id.* at 544. The Court explained that “[a] tax exemption has much the same effect as a cash grant to the organization of the amount of tax it would have to pay on its income. Deduction contributions are similar to cash grants of the amount of a portion of the individual’s contributions.” *Id.*

<sup>248</sup> *Id.* at 544.

<sup>249</sup> *Id.* at 545.

<sup>250</sup> *Id.*; see also *Christian Echoes*, 470 F.2d at 857 (“The Congressional purposes evidenced by the 1934 [lobbying limitation] and 1954 [political campaign prohibition] amendments are clearly constitutionally justified in keeping with the separation and neutrality principles particularly applicable in this case and, more succinctly, the principle that government shall not subsidize, directly or indirectly, those organizations whose substantial activities are directed toward the accomplishment of legislative goals or the election or defeat of particular candidates.”).

<sup>251</sup> *Cammarano v. U.S.*, 358 U.S. 498 (1959).

<sup>252</sup> *Id.* at 513. In *Cammarano*, the Court further rejected TWR’s reliance on *Speiser v. Randall*, 357 U.S. 513 (1958), which involved a California rule which required any taxpayer seeking a property tax exemption “to sign a declaration stating that he did not advocate the forcible overthrow of the Government of the U.S.” The Supreme Court stated in that case that “[t]o deny an exemption to claimants who engage in speech is in effect to penalize them for the same speech.” *Id.* at 518.

<sup>253</sup> *Id.* at 515 (Douglas, J., concurring); see also *Christian Echoes*, 470 F.2d at 857 (“The taxpayer [charitable organization] may engage in all such activities [lobbying and political campaign intervention] without restraint, subject, however, to withholding of the exemption or, in the alternative, the taxpayer may refrain from such activities and obtain the privilege of exemption. The parallel to the ‘Hatch Act’ prohibitions relating to political activities on the part of certain federal and state employees is clear: The taxpayer may opt to enter an area of federal employment subject to the restraints and limitations upon his First Amendment rights. Conversely, he may opt not to receive employment funds at the public trough in the areas covered by the restraints and thus exercise his First Amendment rights unfettered.”).

<sup>254</sup> *Regan*, 461 U.S. at 552-53.

<sup>255</sup> *Id.* at 544. To do so, the two entities should be separately incorporated and maintain records “adequate to show that tax deductible contributions are not used to pay for lobbying.” *Id.* at n.6.

In his concurrence, Justice Blackmun reminded the Court that “§ 501(c)(3) organizations retain their constitutional right to speak and to petition the government” and agreed with the majority that a Section 501(c)(3) organization’s free speech rights are preserved “because it is free to make known its views on legislation through its § 501(c)(4) affiliate without losing tax benefits for its non-lobbying activities.”<sup>256</sup> Nevertheless, Justice Blackmun still cautioned:

Should the IRS attempt to limit the control these organizations exercise over the lobbying of their 501(c)(4) affiliates, the First Amendment problems would be insurmountable. It hardly answers one person’s objection to a restriction on his speech that another person, outside his control, may speak for him. Similarly, an attempt to prevent § 501(c)(4) organizations from lobbying explicitly on behalf of their § 501(c)(3) affiliates would perpetuate § 501(c)(3) organizations’ inability to make known their views on legislation without incurring the unconstitutional penalty. *Such refusals would extend far beyond Congress’ mere refusal to subsidize lobbying.*<sup>257</sup>

The practical lesson to take away from the Supreme Court’s decision in *Regan v. Taxation With Representation* is that Section 501(c)(4) provides a constitutional safety hatch when imposing restrictions on the activities and possible constitutional rights of charitable organizations.<sup>258</sup> Less than two decades after the above Supreme Court decision, the D.C. Circuit adopts this very approach in addressing a controversy involving a church that violated the absolute prohibition on engaging in political activities contained in Section 501(c)(3).<sup>259</sup> In *Branch Ministries v. Rossotti*,<sup>260</sup> the plaintiff, doing business as the Church at Pierce Creek, a tax-exempt church (“CPC”), placed a full-age advertisement in two newspaper four days before the 1992 presidential election. The advertisements urged Christians not to vote for then-candidate Bill Clinton due to his “positions on certain moral issues.”<sup>261</sup> Each advertisement stated that it was co-sponsored by CPC and solicited tax-deductible donations in support of its cause.<sup>262</sup> In response, the IRS invoked a church tax inquiry followed by a church tax examination, as statutorily prescribed.<sup>263</sup> Ultimately concluding that the placement of the advertisements violated the statutory prohibition on political campaign activity, the IRS revoked

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<sup>256</sup> *Id.* at 553.

<sup>257</sup> *Id.*

<sup>258</sup> Even Professor Brennan acknowledges that his proposal – expanding applicability of federal civil rights laws to charitable organizations – was not intended to apply to tax benefits granted to “noncharities” (e.g., business leagues exempt under I.R.C. § 501(c)(6)), because such charities “are tax-exempt because they are inappropriate objects of taxation and, hence, are not exempt for social policy reasons. Accordingly, these noncharitable mutual benefit organizations that are exempt from income tax do not receive the type of tax benefit that, under tax expenditure theory, is equivalent to a direct grant of government funds.” Brennan, *Tax Expenditures*, *supra* note 26, at 225-26.

<sup>259</sup> Section 501(c)(3) provides that an organization can be exempt thereunder provided that it “does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.” I.R.C. § 501(c)(3) (2006).

<sup>260</sup> *Branch Ministries v. Rossotti*, 211 F.3d 137 (D.C. Cir. 2000).

<sup>261</sup> *Id.* at 138. Each advertisement displayed the headline “Christians Beware” and declared that Bill Clinton’s stances on abortion, homosexuality, and the distribution of condoms to teenage students violated the Bible. *Id.* at 140.

<sup>262</sup> *Id.* at 140.

<sup>263</sup> *See* I.R.C. § 7611 (2006).

CPC's tax-exempt status under Section 501(c)(3).<sup>264</sup> CPC challenged the revocation, purporting that it violated its free speech and free exercise rights under the First Amendment and the Religious Freedom Restoration Act of 1993.<sup>265</sup>

In response to CPC's free exercise claim, the D.C. Circuit found that CPC failed to establish that its free exercise rights had been substantially burdened and that the governmental lacked a compelling interest justifying such burden.<sup>266</sup> The court further concluded that CPC's loss of a "conditional privilege for failure to meet the condition" (i.e., loss of its exemption for failing to meet the political campaign prohibition) did not constitute an unconstitutional burden on its free exercise right. This would only be true, explained the court, "if the receipt of the privilege (in this case the tax exemption) is condition 'upon conduct proscribed by a religious faith, or ... denie[d] ... because of conduct mandated by religious belief, thereby putting substantial pressure on an adherent to modify his behavior and to violate his beliefs.'"<sup>267</sup> The court concluded the only effect of the revocation will be a "decrease in the amount of money available to the Church for its religious practices. . . . such a burden 'is not constitutionally significant.'"<sup>268</sup> Furthermore, the court found that CPC's alleged burden was "overstated" since churches receive "unique treatment" under the Internal Revenue Code, thereby rendering the revocation's impact "more symbolic than substantial."<sup>269</sup>

In citing the Supreme Court's decision in *Regan v. Taxation With Representation*, the D.C. Circuit concluded that "an alternate means of communication" was available to CPC in the formation and operation of an affiliated organization exempt under Section 501(c)(4).<sup>270</sup> The court explained that while Section 501(c)(4) organizations are subject to a similar ban on political campaign activities, such organizations may form a political action committee that can participate in political campaigns without limitation.<sup>271</sup> However, the court reminded CPC that it could not channel its tax-deductible contributions to fund the political action committee, since Congress has chosen not to subsidize such First Amendment activities.<sup>272</sup>

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<sup>264</sup> *Branch Ministries*, 211 F.3d at 140.

<sup>265</sup> *Id.* 140-141.

<sup>266</sup> *Id.* at 142, citing *Jimmy Swaggart Ministries v. Board of Equalization*, 493 U.S. 378, 384-85 (1990) ("[T]he free exercise inquiry asks whether government has placed a substantial burden on the observation of a central religious belief or practice and, if so, whether a compelling governmental interest justifies the burden."), and 42 U.S.C. § 2000bb-1(a), (b) ("Governmental shall not substantially burden a person's exercise of religion" in the absence of a compelling government interest that is furthered by the least restrictive means.).

<sup>267</sup> *Id.*, citing *Jimmy Swaggart Ministries*, 493 U.S. at 391-92.

<sup>268</sup> *Branch Ministries*, 211 F.3d at 142, citing *Jimmy Swaggart Ministries*, 493 U.S. at 391; see also *Hernandez v. Commissioner*, 490 U.S. 680, 700 (1989) (the "contention that an incrementally larger tax burden interferes with [ ] religious activities ... knows no limitation").

<sup>269</sup> *Branch Ministries*, 211 F.3d at 142. The court further explained that if CPC did not intervene in future political campaigns, "it may hold itself out as a 501(c)(3) organization and receive all the benefits of that status. All that will have been lost, in that event, is the advance assurance of deductibility in the event a donor should be audited." *Id.* at 142-143.

<sup>270</sup> *Id.* at 143.

<sup>271</sup> *Id.*, citing Treas. Reg. §1.527-6(f), (g) (1980). The court reminded CPC that the "related 501(c)(4) organization must be separately incorporated; and it must maintain records that will demonstrate that tax-deductible contributions to the Church have not been used to support the political activities conduct by the 501(c)(4) organization's political action arm." *Id.*

<sup>272</sup> *Branch Ministries*, 211 F.3d at 143-144, citing *Regan*, 461 U.S. at 548.

As in *Regan*, where the availability of a Section 501(c)(4) organization as an alternate means of communication was deemed “essential to the constitutionality of section 501(c)(3)’s restrictions on lobbying,”<sup>273</sup> such availability was likewise essential in *Branch Ministries* to sustain the constitutionality of Section 501(c)(3)’s prohibition on political campaign activities. Accordingly, it seems probable that the availability of such an alternate means of communication might be of similar utility in sustaining the constitutionality of a nondiscrimination requirement within Section 501(c)(3).

## 2. *Negative Impact on Pluralism*

A corresponding criticism to the constitutionality issue is the contention that a nondiscrimination requirement in Section 501(c)(3) effectively stifles open and diverse dialogue on controversial topics like sexual orientation. Specifically, such a requirement will squelch the “pluralism” implicit in the existence and purposes of the nonprofit sector. The Boy Scouts argued similarly in their brief that “American pluralism thrives on difference” and that “controversial questions of personal morality, often involving religious conviction, are best tested and resolved within the private marketplace of ideas, and not as the subject of government-imposed orthodoxy.”<sup>274</sup> Acknowledging the values of pluralism and “autonomy of diverse groups,” one scholar responded poignantly to that argument:

But it doesn’t follow that these values should always take priority over the effort to break up entrenched patterns of discrimination and include, in socially valued activities, people who have traditionally been outcasts. The harms of discrimination are particularly acute for children; gay youth suffer severe developmental harm when forced to lie and hide their identities, which is precisely what the Boy Scouts’ policy requires of the millions of gay adolescents who discover their sexuality when they are already members. The prevention of such harm is not a trivial state interest.<sup>275</sup>

Furthermore, as established above in the discussion on the Supreme Court’s decisions in *Regan* and *Branch Ministries*, a charitable organization’s free speech rights are preserved through its ability to form and effectively control a Section 501(c)(4) social welfare organization, which would not be subject to a nondiscrimination requirement.<sup>276</sup>

Regardless of which side one takes on this provocative issue of pluralism, the more pertinent question from a tax-exempt law point of view remains whether the stream of tax-deductible dollars received by charitable organizations should be used to achieve that pluralism at the cost of discriminating against a particular segment of society. As stated above, this Article contends that only organizations that do not discriminate should be granted the “gold standard” of tax-exempt status – exemption under Section 501(c)(3). Despite its elimination of

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<sup>273</sup> *Branch Ministries*, 211 F.3d at 143; see also *FCC v. League of Women Voters*, 468 U.S. 364, 400 (1984) (confirming that this was “an accurate description of its holding [in *Regan*].”).

<sup>274</sup> Koppelman, *supra* note 138, at 1835, citing Brief for Petitioner at 45 and 47, *Boy Scouts of America v. Dale*, 530 U.S. 640 (2000).

<sup>275</sup> Koppelman, *supra* note 138, at 1835-36 (citations omitted).

<sup>276</sup> See *supra* note 256 and accompanying text.

discriminatory policies and practices, the proposal set forth herein does not completely thwart pluralism. Rather, to truly effect it, organizations with discriminatory policies or practices can thrive in tax-exempt status under Section 501(c)(4) or some other applicable subsection of Section 501(c), with the only cost being incurred by their members and supporters who are denied a Section 170 deduction for the dollars they contribute in support of such discrimination.

### 3. *Applicability to Religious Organizations*

One of the more perplexing issues raised by the proposal set forth in this Article is how best to apply it to religious organizations. This issue is especially pertinent in that most of the instances of alleged or actual discrimination illustrated in Part I of this Article involve church-affiliated or owned schools, universities, and service providers (e.g., children’s home).<sup>277</sup> Before discussing how best to address this difficult issue, a brief overview of the exemption of religious organizations, including churches, is necessary.

#### a. *Overview of the Religious Exemption*

Section 501(c)(3) provides tax-exempt status to an organization organized and operated exclusively for a *religious* purpose.<sup>278</sup> Although it provides for such exemption, federal income tax law fails to define the terms “religious” or “religion” in its statutes or regulations, due primarily to First Amendment concerns.<sup>279</sup> Religious organizations are generally viewed as being broader than just “churches” or “traditional houses of worship,” and include book publishers, broadcasters, cemeteries, and other organizations.<sup>280</sup> To further complicate matters, exempt purposes listed in Section 501(c)(3) are not “mutually exclusive” in that a “separately incorporated parochial school may be both ‘religious’ and ‘educational,’ and many typical ‘charitable’ activities may be under the control or sponsorship of a particular religion or church.”<sup>281</sup> The IRS is acutely aware of the constitutional ramifications of attempting to define “religion” or “religious” narrowly, and, therefore, advises its revenue agents to interpret the terms broadly, “encompassing even those sects that do not believe in a Supreme Being.”<sup>282</sup> Accordingly, the IRS subscribes to this general rule: “in the absence of a clear showing that beliefs or doctrines under consideration are not sincerely held by those professing or claiming them as a religion, the Service cannot question the ‘religious’ nature of those beliefs.”<sup>283</sup> In fact, if a religious organization is denied exemption, it is typically on grounds other than meeting

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<sup>277</sup> See *supra* notes 13-25 and accompanying text.

<sup>278</sup> I.R.C. § 501(c)(3) (2006); see also Treas. Reg. § 1.501(c)(3)-1(d)(1)(i)(a) (as amended 1990).

<sup>279</sup> See HOPKINS, *supra* note 52, § 8.2, at 227.

<sup>280</sup> JAMES J. FISHMAN & STEPHEN SCHWARZ, NONPROFIT ORGANIZATIONS, CASES AND MATERIALS 444 (3d ed. 2006).

<sup>281</sup> *Id.* at 444-45.

<sup>282</sup> *Id.* at 445; see also, I.R.S. Gen. Couns. Mem. 36,993 (Feb. 3, 1977) (finding that a witches’ coven qualified as a religious organization and a church within the meaning of Section 501(c)(3)).

<sup>283</sup> I.R.S. Gen. Couns. Mem. 36,993 (Feb. 3, 1977); see also Holy Spirit Assoc. v. Tax Commission, 435 N.E.2d 662, 668 (1982) (“It is for the religious bodies themselves, rather than the courts or administrative agencies, to define, by their teachings and activities, what their religion is. The courts are obliged to accept such characterization of the activities of such bodies, . . . unless it is found to be insincere or sham.”).

some definition of religion or religious, such as the private inurement prohibition or the restrictions on lobbying and political campaign activity contained in Section 501(c)(3).<sup>284</sup>

Although the same Congressional and IRS trepidation is present in attempting to define a “church,”<sup>285</sup> some designation is necessary because of the unique treatment and protection that churches receive under the Internal Revenue Code.<sup>286</sup> In making this designation, the IRS follows a checklist comprised of fourteen criteria or characteristics to determine whether an organization constitutes a church.<sup>287</sup> Among such criteria are a distinct legal existence, a recognized creed and form of worship, a formal code of doctrine and discipline, a distinct religious history, and ordained ministers selected after prescribed studies.<sup>288</sup> Although the IRS cautions that such criteria are not exclusive and, ultimately, it is a facts-and-circumstances determination,<sup>289</sup> the criterion most consistently relied on by courts in determining the existence of a church is the presence or absence of an established and regular *congregation*.<sup>290</sup> The IRS provides in its continuing education materials that, “[i]n looking for a congregation, the central focus is whether the organization’s membership is a coherent group of individuals or families that join together to accomplish religious purposes or shared beliefs. The size of the congregation is less important than its dynamic.”<sup>291</sup>

Although nearly all religious organizations are eligible for tax-exempt status under Section 501(c)(3), only “churches, their integrated auxiliaries and conventions or associations of churches” are presumed not to be private foundations,<sup>292</sup> and thus, excepted from the notice

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<sup>284</sup> See, e.g., *Christian Echoes*, 470 F.2d at 849 (exempt status revoked because organization no longer met the operational test and violated the lobbying and political campaign restrictions contained in Section 501(c)(3)); *Branch Ministries*, 211 F.3d at 137 (church violated the political campaign prohibition). Cf. *U.S. v. Kuch*, 288 F.Supp. 439, 444 (D.D.C. 1968) (court determined that the church was not a religion because the record presented no “solid evidence of a belief in a supreme being, a religious discipline, a ritual, or tenets to guide one’s daily existence.”).

<sup>285</sup> See *HOPKINS*, *supra* note 52, § 8.3, at 237.

<sup>286</sup> See *infra* notes 293-295 and accompanying text.

<sup>287</sup> See Robert Louthian & Thomas Miller, *Defining “Church” – the Concept of a Congregation*, MATERIALS FOR IRS EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION TECHNICAL INSTRUCTION PROGRAM FOR FY 1994, at 2, available at <http://www.irs.ustreas.gov/charities/article/0,,id=113084.00.html> (last visited Sep. 7, 2006). The fourteen points are: (i) distinct legal existence; (ii) recognized creed and form of worship; (iii) a definite and distinct ecclesiastical government; (iv) a formal code of doctrine and discipline; (v) a distinct religious history; (vi) a membership not associated with any other church or denomination; (vii) an organization of ordained ministers; (viii) ordained ministers selected after completing prescribed studies; (ix) a literature of its own; (x) established places of worship; (xi) regular congregations; (xii) regular religious services; (xiii) Sunday schools for religious instruction of the young; and (xiv) schools for the preparation of its ministers. *Id.* This fourteen-point test was adopted subsequently by federal courts in *American Guidance Foundation Inc. v. U.S.*, 490 F. Supp. 304, 306 n.2 (D.D.C. 1980), *aff’d without opinion* (D.C. Cir. 1981).

<sup>288</sup> *Louthian & Miller*, *supra* note 287, at 2; see also Rev. Rul. 59-129, 1959-1 C.B. 58.

<sup>289</sup> Internal Revenue Manual – Administration § 321.3.

<sup>290</sup> *Louthian & Miller*, *supra* note 287, at 3, citing *American Guidance Foundation*, 490 F. Supp. at 306 (“[a]t a minimum, a church includes a body of believers or communicants that assembles regularly in order to worship.”).

<sup>291</sup> *Louthian & Miller*, *supra* note 287, at 8.

<sup>292</sup> An organization that meets the requirements of I.R.C. § 501(c)(3) (2006) is either classified as a (i) “public charity” under one of the four provisions or “support tests” of I.R.C. § 509(a) (2006) (such provisions based primarily on an organization’s sources of financial support), or (ii) a “private foundation.” An organization is considered a private foundation if it does *not* meet the requirements of any of the I.R.C. § 509(a) support tests. A private foundation typically receives contributions from only a few individuals or entities, whereas a public charity

requirements of Section 508 (i.e., a church does not need to file an application to be recognized as exempt under Section 501(c)(3)).<sup>293</sup> Churches are also relieved from filing annual information returns with the IRS.<sup>294</sup> In addition, the Internal Revenue Code confers upon churches special procedural safeguards with respect to IRS examinations or audits.<sup>295</sup> Churches are also exempted from certain rules governing qualified retirement plans, and social security, self-employment, and withholding taxes.<sup>296</sup>

A particular church's activities typically comprise more than just making religious services and worship available to its congregants. Many churches conduct activities such as operating a school, seminary, or social service agency (e.g., day care), or conducting women's or children's groups without forming a separate legal entity for such activities.<sup>297</sup> Until such time that an activity is incorporated or otherwise made part of a separate legal entity, it is considered a component of the church, as a legal entity, and covered by the church's exemption.<sup>298</sup> Once a new legal entity is formed to conduct such an activity, the reasons for which are typically liability or administrative related, the entity needs to obtain its own tax-exempt status.<sup>299</sup> This is typically accomplished through the activity's relationship to the church, which the Internal Revenue Code classifies as an "integrated auxiliary."<sup>300</sup> An "integrated auxiliary" is defined by regulation as a separate entity that is a charitable organization (e.g., a school, mission society, or youth group), a public charity (as opposed to a private foundation),<sup>301</sup> internally supported,<sup>302</sup> and affiliated with a church or a convention or association of churches.<sup>303</sup> An organization meets the "affiliated" requirement if it is covered by a group exemption letter issued to a church or a convention or association of churches,<sup>304</sup> is operated, supervised or controlled by such church, or pertinent facts and circumstances establish such an affiliation.<sup>305</sup> Under prior regulatory law, an

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typically receives its income from a broader segment of the general public in the form of gifts, contributions, or receipts from performance of services. Furthermore, private foundations are subject to additional excise taxes under I.R.C. §§ 4941-4945 (2006).

<sup>293</sup> I.R.C. § 508(c)(1)(A) (2006); *see also* Treas. Reg. § 1.508-1(a)(3)(i)(a) (as amended in 1995).

<sup>294</sup> I.R.C. § 6033(a)(2)(A)(i) (2006).

<sup>295</sup> I.R.C. § 7611 (2006).

<sup>296</sup> NICHOLAS P. CAFARDI & JACLYN FABEAN CHERRY, UNDERSTANDING NONPROFIT AND TAX EXEMPT ORGANIZATIONS § 8.03[C], 112 (2006), *citing* I.R.C. §§ 410(c)(1)(B), 411(e)(1)(B), 412(h)(4), 414(e), 1402(e), 3121(b)(8), and 3401(a)(9) (2006).

<sup>297</sup> *Id.*, § 8.06, at 114.

<sup>298</sup> *Id.*

<sup>299</sup> *Id.*

<sup>300</sup> *Id.*; *see supra* note 293 and accompanying text.

<sup>301</sup> *See supra* note 292.

<sup>302</sup> With respect to the "internal support" requirement, an organization qualifies as an integrated auxiliary if it either: "(1) offers admissions, goods, services or facilities for sale, other than on an incidental basis, to the general public and not more than 50 percent of its support comes from a combination of government sources, contributions from the general public, and receipts other than those from an unrelated business; or (2) does not offer admissions, goods, services, or facilities for sale, other than on an incidental basis, to the general public." FISHMAN & SCHWARZ, *supra* note 280, at 444, *citing* Treas. Reg. § 1.6033-2(h)(4) (as amended in 1995).

<sup>303</sup> Treas. Reg. § 1.6033-2(h)(1) (as amended in 1995).

<sup>304</sup> A group exemption letter or "group ruling" requires the church's central organization to report annually to the IRS the entities and affiliates covered by its exemption and certify that each of them meet the requirements for exemption under Section 501(c)(3). *See* CAFARDI & CHERRY, *supra* note 296, § 8.05, at 113; Rev. Proc. 80-27, 1980-1 C.B. 677.

<sup>305</sup> HOPKINS, *supra* note 52, § 8.5, at 243, *citing* Treas. Reg. § 1.6033-2(h)(2) (as amended in 1995). Treas. Reg. § 1.6033-2(h)(3) (as amended in 1995) provides a list of factors used to determine whether a an organization is

organization that qualified as an integrated auxiliary had to engage in an activity that was “exclusively religious.”<sup>306</sup> Such standard was not met if the organization’s activity “was of a nature other than religious that would serve as a basis for tax exemption” (e.g., educational or scientific activity).<sup>307</sup> However, the Eighth Circuit held that this requirement was not consistent with Congressional intent, thereby concluding that a social service agency could constitute an integrated auxiliary of a church.<sup>308</sup>

*b. Exception for a “Church”*

The intent of the proposal set forth in this Article is to except churches from the proposed nondiscrimination requirement. The primary reason for this exception is that the application of such a requirement would likely violate the First Amendment’s free exercise clause in that it could be interpreted as attempting to regulate religious belief.<sup>309</sup> Furthermore, it is not the intent of this Article’s proposal to control what members of churches believe or with whom they share such beliefs. Consequently, an exception to the nondiscrimination requirement for churches within Section 501(c)(3) would be needed.<sup>310</sup> However, because the federal income tax law definition of a church also encompasses integrated auxiliaries, who by definition can include church-affiliated schools, universities, social service agencies, etc., the definition of a church for purposes of the notice and annual reporting provisions of the Internal Revenue Code needs to be tailored to exclude such separate, affiliated entities. Furthermore, to address situations where a school, university or social service agency is conducted within the same legal entity as the congregational church, the statutory use of “church” in Sections 508 and 6033 should be defined to reflect the fourteen-point test promulgated by the IRS and adopted by the courts, with specific emphasis on the criterion of an established and dynamic congregation.<sup>311</sup> This Article’s proposal can only effectively combat the kind of ongoing discrimination illustrated in Part I by limiting the definition of a church to an organization contemplated by the fourteen-point test. Such a limited definition will likely garner criticism by those who believe there are already too many

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affiliated, which includes, but is not limited to: (i) the organization’s charter or bylaws reveal that it shares common religious doctrines or practices with a church, (ii) such church or convention or association of churches has the power to appoint, control or remove at least one of the organization’s officers or directors, (iii) its name indicates an institutional relationship, and (iv) upon dissolution, its assets are to be distributed to such church or convention or association of churches. *Id.*

<sup>306</sup> HOPKINS, *supra* note 52, § 8.5, at 244.

<sup>307</sup> *Id.*

<sup>308</sup> *Id.*, citing *Lutheran Social Services of Minn. v. U.S.*, 758 F.2d 1283, 1291 (8<sup>th</sup> Cir. 1985).

<sup>309</sup> The First Amendment provides that “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; . . .” U.S. CONST. amend. 1. *See also* HOPKINS, *supra* note 52, § 8.1, at 220, citing *Sherbert v. Verner*, 374 U.S. 398, 402 (1963) (“Government may neither compel affirmation of a repugnant belief, nor penalize or discriminate against individuals or groups because they religious views abhorrent to the authorities.”).

<sup>310</sup> To illustrate, Section 501(c)(3) could be further amended to include the following subparagraph:

(B) In the case of a church, as defined in section 508(c)(1)(A), subparagraph (A) shall not apply to the extent that the application of such subparagraph would not be consistent with the church’s established tenets or creed.

In addition, the exception should be similarly extended to religious orders and similar exclusively religious” organizations exempt under Section 501(c)(3). Religious orders are not defined in the Internal Revenue Code or applicable regulations. HOPKINS, *supra* note 52, § 8.6, at 245. However, the IRS has issued guidelines for determining whether an organization qualifies as such. *See* Rev. Proc. 91-20, 1991-1 C.B. 524.

<sup>311</sup> *See supra* notes 287-291 and accompanying text.

limitations on churches in the Internal Revenue Code.<sup>312</sup> However, a limited definition of a church for purposes of Sections 508 and 6033 does not preclude a broader definition of church for other purposes within the Internal Revenue Code, as is currently done, for instance, in the FICA tax provisions.<sup>313</sup>

The Supreme Court, in upholding the imposition of a racial nondiscrimination policy in *Bob Jones University*, appeared to similarly appreciate the difference between a church and a “religious” school by stating that “[w]e deal here only with religious *schools* – *not with churches or other purely religious institutions*; here, the governmental interest is in denying public support to racial discrimination in education.”<sup>314</sup> In addition, the Supreme Court rejected the university’s claim that the denial of its tax exemption violates the Establishment Clause because it favors religions that do not advocate racial discrimination.<sup>315</sup> It provided the following response:

[A] regulation does not violate the Establishment Clause merely because it ‘happens to coincide or harmonize with the tenets of some or all religions.’ The IRS policy at issue here is founded on a ‘neutral, secular basis,’ and does not violate the Establishment Clause. . . . In addition, as the Court of Appeals noted, ‘the uniform application of the rule to all religiously operated schools *avoids* the necessity for a potentially entangling inquiry into whether a racially restrictive practice is the result of sincere religious belief.’<sup>316</sup>

It is certainly arguable that the Supreme Court’s reasoning can be employed to ensure that a nondiscrimination requirement within Section 501(c)(3) is applied to all charitable organizations, other than churches or “other purely religious institutions,” based on a governmental interest to deny public support to charitable organizations that discriminate. By limiting the definition of a church as stated above, a nondiscrimination requirement within Section 501(c)(3) can truly accomplish its primary purpose – ensure that the stream of tax-deductible dollars received by charitable organizations are not used to discriminate against any member of society.

An alternative solution may be to not alter the current definition and treatment of churches and church-affiliated entities at all. According to a 1975 revenue ruling (issued after the IRS announced that it would no longer grant or maintain exemptions to schools with racially discriminatory policies),<sup>317</sup> the public policy doctrine could be utilized to deny or revoke exempt

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<sup>312</sup> See, e.g., Michael Hatfield, *Ignore the Rumors – Campaigning from the Pulpit is Okay: Thinking Past the Symbolism of Section 501(c)(3)*, 20 NOTRE DAME J.L. ETHICS & PUB. POL’Y 125 (2006); Christine R. Moore, *Religious Tax Exemption and the “Charitable Scrutiny” Test*, 15 REGENT U.L. REV. 295 (2003). Cf. Vaughn E. James, *Reaping Where They Have Not Sowed: Have American Churches Failed to Satisfy the Requirements for the Religious Tax Exemption?*, 43 CATH. LAW. 29, 74 (2004); Ann M. Murphy, *Campaign Signs and the Collection Plate – Never the Twain Shall Meet?*, 1 PITT. TAX REV. 35 (2004).

<sup>313</sup> See I.R.C. § 3121(w)(3) (2006). Any amendment to the language of I.R.C. §§ 508 and 6033 (2006) may also need to be similarly made to other Internal Revenue Code sections that adopt the “integrated auxiliaries” or “integrated auxiliary” language, as in I.R.C. §§ 501(h)(5)(B) and 6043(b)(1) (2006). Cf. Charles M. Whelan, *“Church” in the Internal Revenue Code: The Definitional Problems*, 45 FORDHAM L. REV. 885 (1977).

<sup>314</sup> *Bob Jones Univ.*, 461 U.S. at 604 n.29 (emphasis added).

<sup>315</sup> *Id.* at 604 n.30.

<sup>316</sup> *Id.* (citations omitted).

<sup>317</sup> See *supra* notes 87-88 and accompanying text.

status to a church or a separate affiliated entity that operated and controlled a school with a racially discriminatory admissions policy.<sup>318</sup> In the ruling, the IRS presented several scenarios including a school (“X”) with a racially discriminatory admissions policy that was incorporated as a separate entity, but affiliated with and controlled by a church, and a school with the same policy operated directly within the church entity (“Y”).<sup>319</sup> In the first scenario, the IRS held that X was not operated exclusively for charitable purposes and therefore did not qualify for exempt status under Section 501(c)(3), but this had no effect on the church’s exemption.<sup>320</sup> In the second scenario, the IRS concluded that there should be no disparate result just because the school was operated within the church entity (Y). Accordingly, it found that Y was not exempt under Section 501(c)(3).<sup>321</sup> In a third scenario, the IRS similarly concluded that exempt status could not be conferred to a church that operated two schools (one that was separately incorporated and one that was operated within the same entity as the church), and asserted that it was required by its religious tenets to maintain a racially discriminatory policy. The IRS relied on a line of Supreme Court cases that conclude that although the First Amendment’s Free Exercise Clause bars government interference into religious beliefs and opinions, it does not necessarily “affect the legal consequences otherwise attending a given practice or action that is not inherently religious.”<sup>322</sup> Based on this reasoning, similar conclusions could be reached with respect to tax-exempt status if the proposed nondiscrimination requirement was applied to the above factual scenarios. However, to date, the IRS conclusions set forth in the revenue ruling have not been validated by a federal court.

#### 4. *Other Potential Difficulties and Criticisms*

Another potential difficulty or criticism with respect to the proposal set forth herein is how it will apply to same-gender or same-religion organizations, such as a all-girls Catholic high school or an organization directing its relief and educational programs at poverty-stricken Kenyans immigrating to the United States. Will such organizations be denied tax-exempt status

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<sup>318</sup> Rev. Rul. 75-231, 1975-1 C.B. 158.

<sup>319</sup> *Id.*

<sup>320</sup> *Id.*

<sup>321</sup> *Id.* The IRS based its conclusion on the Supreme Court’s decision in *Norwood v. Harrison*, 413 U.S. 455 (1973), in which the Court held that a state may not provide free textbooks to a private school if it would have a “significant tendency to facilitate, reinforce, and support private discrimination.” The Supreme Court made no exception in *Norwood* for the schools that were not separate legal organizations, but directly operated by churches receiving free textbooks. The IRS concluded that, [i]t follows that the legal organization operating Y [in the second scenario] is frustrating Federal public policy by having a racially or ethnically discriminatory policy as to students.” *See also*, Gen. Couns. Mem. 39,754 (Sep. 19, 1988) (IRS Chief Counsel concluded, in accordance with Rev. Rul. 75-231, that a church’s “failure to operate a school in a bona fide nondiscriminatory manner precludes the church from qualifying as an organization that is operated exclusively for charitable purposes, and thus also precludes the church from qualifying for exemption from federal income tax by virtue of being described in section 501(c)(3).”).

<sup>322</sup> Rev. Rul. 75-231, *citing* *Reynolds v. U.S.*, 98 U.S. 145, 166-167 (1878), and *Mitchell v. Pilgrim Holiness Church Corporation*, 210 F. 2d 879 (7th Cir. 1954), *cert. denied*, 347 U.S. 1013 (1954). In the ruling, the IRS explained “[t]he important distinction between religious belief, on the one hand, and the legal consequences that may validly be attached to action induced by religious belief, on the other, is well illustrated by one recent line of cases interpreting the Federal drug laws. The courts have repeatedly refused to engraft a religious exception on any criminal statute outlawing the transportation of heroin, marijuana, and peyote into the U.S., notwithstanding an apparent judicial recognition that a given accused might sincerely believe the use of such drugs has a proper place in certain religious ceremonies which are prescribed in both the Koran and the Bible.” *See U.S. v. Spears*, 443 F. 2d 895 (5th Cir. 1971).

under an amended Section 501(c)(3) because they discriminate on the basis of gender or national origin? Similar dilemmas immediately surfaced in the years surrounding the *Bob Jones University* decision.<sup>323</sup> In response, the IRS was reluctant to extent the public policy doctrine to such situations,<sup>324</sup> in part, because the doctrine fails to designate a clear source of public policy, as discussed in Part II of this Article.<sup>325</sup> Perhaps the IRS did not see such instances of discrimination as being invidious or harmful, and thus outside the intended purposes and goals of the public policy doctrine.

Accordingly, the best solution may lie with the definition of discrimination under the statute; specifically, whether it is defined as policies or practices that are wrongful, harmful, or invidious in some way. The proposed amendment to Section 501(c)(3) should contain a legislative grant to the IRS, along with some clearly-defined parameters, to promulgate regulations that set forth instances that do or do not constitute discrimination under the legislative purposes of the statute. For instance, gender-based discrimination could be deemed not to exist in same-sex schools due to proven pedagogical benefits and a lack of concerted effort to specifically exclude the other gender. In addition, racial or national origin discrimination could be deemed to not exist with respect to an organization whose mission has an established record of combating poverty in an area of a city that happens to be comprised mostly of African-American citizens or a particular immigrant population. Again, the lack of any evidence establishing a concerted effort to exclude persons of other races or national origins may be decisive. Ultimately, whether or not a particular policy, action, or course of actions constitutes discrimination will be a facts-and-circumstances determination, borrowing standards and burdens of proof from established federal civil rights laws and other nondiscrimination statutes.<sup>326</sup>

This point may be best illustrated by two General Counsel Memorandum (“GCM”) – one issued before and the other immediately after the Supreme Court’s decision in *Bob Jones University*. In GCM 37462,<sup>327</sup> the IRS concluded that a scholarship trust that restricted eligible beneficiaries to Caucasian students furthers racial discrimination in education contrary to established federal public policy. Notwithstanding, the IRS determined that it was doubtful that administering such a trust would adversely impact the school’s exemption because it was de minimus in relation to the school’s aggregate scholarship program.<sup>328</sup> However, in GCM 39082,<sup>329</sup> the IRS revoked the “per se rule” in GCM 37462, concluding that scholarship trusts that restrict eligibility to Caucasian students should be examined on a case-by-case basis to determine whether racial discrimination is advanced. The IRS explained that, for instance, a private trust that grants scholarships only to Caucasian students to enroll at a “predominantly

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<sup>323</sup> FISHMAN & SCHWARZ, *supra* note 280, at 424.

<sup>324</sup> See Rev. Rul. 77-272, 1972-2 C.B. 191 (IRS held that an organization that provided job training exclusively for Native Americans did not violate the public policy doctrine because it was formed at the request of the Bureau of Indian Affairs and accomplished goals set forth in the Adult Vocational Training Act); Priv. Ltr. Rul. 7744007 (IRS ruled that a scholarship fund limiting grants to male graduates at a co-ed high school did not violate the public policy doctrine because the doctrine did not extent to gender-based discrimination);

<sup>325</sup> See *supra* notes 115-118 and accompanying text.

<sup>326</sup> Such as disparate treatment and disparate impact

<sup>327</sup> I.R.S. Gen. Couns. Mem. 37,462 (Mar. 17, 1978).

<sup>328</sup> *Id.*

<sup>329</sup> I.R.S. Gen. Couns. Mem. 39,082 (Dec. 1, 1983).

minority school could be said actually to discourage racial discrimination in education.”<sup>330</sup> The IRS further concluded that the “well-established policy of promoting private educational trusts should, on balance, prevail even where the benefits of the trust are limited to members of a particular race.”<sup>331</sup> In the GCM, the IRS found it persuasive that the school charged with administering the trust adopted and maintained a racial nondiscrimination policy and the trust accounted for a small share of the total financial assistance available to students.

This Article’s proposal may also be criticized as unnecessary in light of the number of state and local nondiscrimination laws.<sup>332</sup> However, such laws apply in varying degrees and in limited situations, such as only in government employment or public housing, and may not apply directly to charitable organizations. In addition, such laws are constantly subject to challenge by lawsuits and legislative repeal and, therefore, cannot ensure the same comprehensive application to all charitable organizations that can be achieved through an amendment to Section 501(c)(3).<sup>333</sup> Notwithstanding their importance and effectiveness in combating all kinds of discrimination, state and local nondiscrimination laws do not directly or effectively assist in achieving one of the primary purposes of this Article’s proposal – that the stream of tax-deductible dollars received by charitable organizations are not used to maintain a discriminatory policy or otherwise effect discrimination against any member of society.

## V. CONCLUSION

In Part I of this Article, a simple but important question was posed – should a charitable organization continue to enjoy the benefits of tax-exempt status if it engages in discrimination? After illustrating the apparently common practice of discrimination by charitable organizations and the failure of existing law to combat it, this Article answers that question with a resounding “No!” Fundamental to this Article’s proposal is the notion that discrimination by a charitable organization is intrinsically incompatible with that organization’s charitable purpose and mission. In filling the current void in federal income tax with respect to such discrimination, this Article’s proposal attempts to transform Section 501(c)(3) into the gold standard for all tax-exempt organizations, ensuring that their beneficiaries are as diverse as the taxpaying public from whom they draw their support.

By not relying on an ill-defined public policy doctrine or federal civil rights laws that are questionably applicable, a nondiscrimination requirement within Section 501(c)(3) offers a more comprehensive solution to the problem of discriminatory policies and practices of charitable organizations. It sends a strong message to potential and existing charitable organizations that

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<sup>330</sup> *Id.*

<sup>331</sup> *Id.*

<sup>332</sup> For a list of states, cities and counties with civil rights ordinances, policies or proclamations prohibiting discrimination based on sexual orientation, see Lambda Legal Defense and Education Fund, Summary of States, Cities and Counties Which Prohibit Discrimination Based on Sexual Orientation, available at <http://www.lambdalegal.org/cgi-bin/iowa/news/fact.html?record=217> (last visited Sep. 7, 2006).

<sup>333</sup> See, e.g., Jonathan Saltzman, *Romney eyes bill exempting religious groups on bias laws*, BOSTON GLOBE, Mar. 11, 2006; Christopher Heredia, *Salvation Army says no benefits for partners, National panel overturns regional OK*, SAN. FRAN. CHRONICLE, Nov. 14, 2001, at A-22; Dana Milbank, *Charity Cites Bush Help in Fight Against Hiring Gays*, WASH. POST, July 10, 2001, at A01.

discrimination is fundamentally inconsistent with tax-exempt status under Section 501(c)(3) and more in concert with society's notion of what constitutes a charity. As the Supreme Court stated in *Bob Jones University*, a charitable organization must "be in harmony with the public interest" and its purpose "must not be so at odds with the common community conscience as to undermine any public benefit that might otherwise be conferred."<sup>334</sup> Furthermore, a nondiscrimination requirement ensures that the stream of tax-deductible dollars (i.e., generated by the Section 170 charitable contributions deduction) received by charitable organizations is not used to discriminate against any member or segment of society.

The proposal is not totally free from difficulties and challenges. However, by permitting organizations that wish to discriminate to qualify for exempt status under Section 501(c)(4) as a social welfare organization, a nondiscrimination requirement within Section 501(c)(3) should withstand any constitutionally-based challenges (i.e., alleged First Amendment violations) or criticisms that it effectively squelches pluralism. To ensure that such requirement combats discrimination comprehensively, genuine consideration needs to be given to redefining the term "church" for purposes of the notice and annual reporting provisions under Sections 508 and 6033, respectively. The proposal specifically excepts churches from the nondiscrimination requirement due primarily to First Amendment free exercise concerns. By tailoring the definition to the fourteen-point test articulated by the IRS and adopted by courts, with a specific emphasis on the criterion of an established and dynamic congregation, church-affiliated schools, universities, social service agencies, and other organizations that currently constitute "integrated auxiliaries" of churches under the Internal Revenue Code will not be shielded from the proposed nondiscrimination requirement. Additional consideration will also need to be given to the intended meaning of discrimination with respect to same-gender, same-national-origin, or similarly focused organizations that otherwise operate exclusively for exempt purposes under Section 501(c)(3).

To conclude, the immortal words of President John F. Kennedy, in his message to Congress calling for the enactment of Title VI, are particularly pertinent to the proposal herein:

Simple justice requires that public funds, to which all taxpayers of all races [colors, and national origins] contribute, not be spent in any fashion which encourages, entrenches, subsidizes, or results in racial [color or national origin] discrimination.<sup>335</sup>

The inclusion of an expansive nondiscrimination requirement within Section 501(c)(3) is a necessary step in ensuring that charitable organizations do not use public funds to encourage, entrench or subsidize discrimination of any kind against any member or segment of society.

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<sup>334</sup> See *supra* note 230 and accompanying text.

<sup>335</sup> See <http://www.usdoj.gov/crt/cor/coord/titlevi.htm> (last visited Sep. 7, 2006).