
The Parsonage Exemption

Adam Chodorow*

The parsonage exemption allows “ministers of the gospel” to exclude the value of housing benefits from income, whether received in-kind or as a cash allowance. Critics argue that the provision violates the First Amendment’s Establishment Clause, while supporters contend that it does not single religion out for a cognizable benefit. Alternately, supporters claim that it is a permissible accommodation for religion under the First Amendment’s Free Exercise Clause. This Article fills an important gap in the debate by offering a nuanced explanation of how the parsonage exemption and other housing provisions function within the tax code. Placing the exemption in its proper context makes clear that the parsonage exemption: (1) operates as a unique subsidy for religious actors; (2) involves significantly more church-state entanglement than would its elimination; (3) violates core tax principles of horizontal and vertical equity; and (4) differs significantly from other exemptions for religious actors.

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* Copyright © 2018 Adam Chodorow. Professor of Law and Willard H. Pedrick Distinguished Research Scholar at the Sandra Day O'Connor College of Law at Arizona State University. I would like to thank Ellen Aprill, Jon Forman, Troy Rule, Michael Helfand, Erin Scharff, Sam Brunson, James Weinstein, Stuart Benjamin, Karen Brashaw, Jessica Berch, and Robert Baty for their assistance and comments on earlier drafts.

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INTRODUCTION

The parsonage exemption, allows “ministers of the gospel” to exclude the value of housing benefits from income, whether provided in-kind or paid as a cash allowance.¹ This is no small matter. According to the Treasury Department, the exemption will cost approximately \$9.3 billion in forgone taxes over the next ten years,² reflecting approximately \$37 billion in untaxed income.³ To date, the constitutional challenges mounted against the parsonage exemption have foundered on standing.⁴ However, challengers may have finally cleared this hurdle,⁵ and we may finally be set to get to the merits.

Unsurprisingly, litigants and scholars have focused primarily on the Supreme Court’s confused First Amendment jurisprudence. However, the parsonage exemption is part of the Tax Code,⁶ and, regardless of the constitutional test chosen, any attempt to evaluate the exemption depends in large part on understanding the role it and other housing provisions play within that Code. This Article fills an important gap in the debate over the parsonage exemption by placing it in its appropriate context and examining it from that perspective.

In 2002, Erwin Chemerinsky surveyed the different tests the Supreme Court had articulated for determining whether laws violate

¹ Some commentators distinguish between the parsonage exemption (referring to in-kind housing) and the housing allowance (referring to cash allowances). I refer to both provisions as the parsonage exemption and distinguish between them as necessary.

² OFFICE OF TAX ANALYSIS, U.S. DEP’T OF THE TREASURY, TAX EXPENDITURES: FISCAL YEAR 2017, at 23 (Nov. 11, 2015) [hereinafter TAX EXPENDITURES], <https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2017.pdf>.

³ This assumes an average marginal rate of 25%. In fact, if such income were taxed and the parties wanted to ensure that ministers received \$37 billion in after-tax income, they would have to gross up the income to account for taxes, leading to even greater tax savings. For instance, ministers would need to be paid \$49.3 billion to receive \$37 billion on an after-tax basis, reflecting a tax savings of \$12.3 billion.

⁴ It is difficult for taxpayers to challenge tax provisions that provide benefits to others, such as the parsonage exemption, because they typically cannot show individual harm. Instead, courts have required taxpayers to request the benefit, even if they clearly do not qualify, and then challenge the denial. *See, e.g., Freedom From Religion Found., Inc. v. Lew*, 773 F.3d 815, 820-21 (7th Cir. 2014) (denying plaintiffs standing because they had not asked for the benefit prior to submitting the challenge, and thus had not been denied).

⁵ *See* Complaint at 2, *Gaylor v. Lew*, No. 16-CV-215 (W.D. Wis. Apr. 6, 2016) (describing plaintiffs’ claim that jurisdiction is proper because they were denied refunds of taxes paid on their housing allowance).

⁶ All references to the Tax Code, the Code, or Sections refer to the Internal Revenue Code of 1986, as amended, unless otherwise indicated.

the First Amendment and concluded that the parsonage exemption's cash allowance provision failed them all.⁷ Supporters have raised a number of arguments in response. Initially, they claim that the exemption does not pose Establishment Clause issues. For instance, citing other housing provisions in the Code, some argue that the parsonage exemption does not single out religion for a benefit because it is part of a broad policy that happens to include churches, much as Code § 501(c)(3) constitutionally exempts charitable, educational, and religious organizations from income tax.⁸ Others argue that, unlike direct support, exemptions cannot be considered a subsidy for purposes of the First Amendment.⁹

Alternately, supporters concede that the exemption raises Establishment Clause concerns but argue that the parsonage exemption is nonetheless constitutionally permitted under the Free Exercise Clause as an accommodation for religion. Some argue that it is necessary to avoid church-state entanglement.¹⁰ Others claim that it is necessary to ensure that ministers are treated the same as laypeople

⁷ Erwin Chemerinsky, *The Parsonage Exemption Violates the Establishment Clause and Should Be Declared Unconstitutional*, 24 WHITTIER L. REV. 707, 735 (2003). Professor Chemerinsky was not asked to and did not evaluate the in-kind provision.

⁸ See, e.g., Brief in Support of Defendant's Motion for Summary Judgment at 7-8, *Gaylor v. Lew*, No. 3:16-CV-00215 (W.D. Wis. Apr. 4, 2016) (asserting that the secular purpose of § 107(2) is to eliminate discrimination between religious and secular employees, and among religious employees); Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment at 20, *Gaylor v. Lew*, No. 3:16-CV-00215 (W.D. Wis. Apr. 4, 2016) (arguing that § 107(2) is part of a broad secular scheme); Justin Butterfield, Hiram Sasser & Reed Smith, *The Parsonage Exemption Deserves Broad Protection*, 16 TEX. REV. L. & POL. 251, 261-64 (2012) (addressing Chemerinsky's arguments and comparing the parsonage exception directly to 501(c)(3) organizations).

⁹ See, e.g., Brief in Support of Defendant's Motion for Summary Judgment, *supra* note 8, at 21-23 (arguing that a tax exclusion, unlike a subsidy, "leaves religion alone" and thus does not violate the First Amendment); Martha M. Legg, *Excluding Parsonages from Taxation: Declaring a Victor in the Duel Between Caesar and the First Amendment*, 10 GEO. J.L. & POL'Y 269, 283-86 (2012) (arguing that not all exemptions serve to function as subsidies, the parsonage exemption included).

¹⁰ See, e.g., Brief in Support of Defendant's Motion for Summary Judgment, *supra* note 8, at 25-33 (arguing that the parsonage exemption does not create excessive entanglement between the government and religion); Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment, *supra* note 8, at 36-43 (arguing that the government frequently creates provisions to avoid church-state entanglement); Edward A. Zelinsky, *Do Religious Tax Exemptions Entangle in Violation of the Establishment Clause? The Constitutionality of the Parsonage Allowance Exclusion and the Religious Exemptions of the Individual Health Care Mandate and the FICA and Self-Employment Taxes*, 33 CARDOZO L. REV. 1633, 1635 (2012) (rejecting claim that § 107 impermissibly entangles church and state).

and that all religions and ministers are treated equally, regardless of the form housing support takes.¹¹ Finally, some have argued that the parsonage exemption is similar to other exemptions for religious actors found in the Code and elsewhere, including the exemptions from payroll taxes and under the Affordable Care Act. They argue that these other provisions either demonstrate that the parsonage exemption is appropriate or that these other accommodations would be threatened were the exemption found to be unconstitutional.¹²

As demonstrated below, placing the exemption in its proper tax context reveals that it: (1) operates as a unique subsidy to religion; (2) leads to significant church-state entanglement; (3) violates the core tax values of horizontal and vertical equity by ignoring important differences in church practices; and (4) differs from other exemptions for religious actors found in the Code and elsewhere, such that they neither provide it cover nor would be at risk were the parsonage exemption deemed unconstitutional.

The notion that the parsonage exemption is part of a broad, neutral housing policy scattered throughout the Tax Code is easily refuted. Supporters cite no other example of a broad policy contained in myriad sections. Nor do the legislative histories of the different housing provisions support this claim. Moreover, such claims overlook important differences in the purpose and scope of these different sections. For instance, § 119 applies only where housing is: (1) in-kind, (2) on-site, (3) required, and (4) for the benefit of the employer and reflects a normative judgment about what properly constitutes income.¹³ Examples of those who qualify under § 119 include hospital workers,¹⁴ hotel managers,¹⁵ and seamen,¹⁶ all of

¹¹ See, e.g., Brief in Support of Defendant's Motion for Summary Judgment, *supra* note 8, at 10-16 (arguing that the purpose of the statute is to promote nondiscrimination between ministers of different religions and between lay people and ministers); Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment, *supra* note 8, at 43-47 (stating that the parsonage exception serves to reduce discrimination); Stuart J. Lark & Erich T. Kennedy, *Once and Future Challenges to the Minister's Housing Allowance*, 14 TAX'N EXEMPTS 185, 190 (2003) (summarizing argument that the parsonage exception promotes equal treatment).

¹² Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment, *supra* note 8, at 48-49 (arguing that many areas of the tax code would be affected should the parsonage exemption be struck down); Zelinsky, *supra* note 10, at 1667-76 (emphasizing the broad implications of striking down the parsonage exemption).

¹³ See I.R.C. § 119 (2018).

¹⁴ O.D. 915, 1921-4 C.B. 85, 1921 WL 50340 ("Where the employees of a hospital are subject to immediate service on demand at any time during the twenty-four hours of the day and on that account are required to accept quarters and meals at the

whom *must* be on-site overnight to perform their jobs. In such limited circumstances, housing is not compensatory and therefore should properly be excluded from income.¹⁷

In contrast, § 911 permits those who have established a tax home overseas to exclude foreign-earned income, including some housing allowances.¹⁸ This provision can be understood either as a normative tax rule designed to eliminate double taxation for those subject to foreign taxes or as a targeted subsidy to encourage international trade. Sections 134 and 912 permit military personnel, generally, and federal government employees living abroad to exclude cash housing allowances.¹⁹ These provisions should be understood as part of the government's employment contract with its workers. Rather than tax such amounts and gross up salaries to account for the additional taxes, the government simply excludes the allowances from income.

The claim that exemptions differ from direct subsidies for Establishment Clause purposes simply ignores economic reality. While the Supreme Court has at times suggested that tax exemptions, deductions, and credits differ from direct support,²⁰ in *Texas Monthly, Inc. v. Bullock*,²¹ it held that targeted tax exemptions to religious actors could indeed violate the Establishment Clause. Ignoring the significant economic benefits that flow to ministers in the form of tax exemptions for some, but not all, of their income would permit Congress to subvert the First Amendment.

hospital, the value of such quarters and meals may be considered as being furnished for the convenience of the hospital and does not represent additional compensation to the employees.”).

¹⁵ *Benaglia v. Comm’r*, 36 B.T.A. 838, 839-40 (1937) (stating Petitioner hotel manager’s “residence at the hotel was not by way of compensation for his services, not for his personal convenience, comfort or pleasure, but solely because he could not otherwise perform the services required of him”).

¹⁶ O.D. 265, 1919-1 C.B. 71 (stating seamen’s lodging and food costs do not need to be included in stated income).

¹⁷ As discussed more fully below in section III.A, Section 119 also reflects an administrative decision to adopt narrow bright-line rules to avoid disputes with taxpayers over whether housing is compensatory in nature.

¹⁸ See I.R.C. § 911 (2018).

¹⁹ See I.R.C. § 134 (2018); I.R.C. § 912 (2018).

²⁰ See, e.g., *Ariz. Christian Sch. Tuition Org. v. Winn*, 563 U.S. 125, 130 (2011) (holding that plaintiffs did not have standing to challenge tax credits that could go, among other places, to religious schools); *Walz v. Tax Comm’r of N.Y.C.*, 397 U.S. 664, 667 (1970) (holding that appellant’s argument that a subsidy and tax credit were substantially the same was meritless).

²¹ *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 5 (1989).

Arguments that the parsonage exemption is an appropriate accommodation under the Free Exercise Clause fair no better. For instance, contrary to supporters' claims, eliminating the parsonage exemption would actually reduce church-state entanglement because § 107 necessarily embroils the government in significant doctrinal and organizational questions and requires significant government oversight. The government must determine whether a religion is legitimate, who qualifies as a minister, what activities are sacerdotal in nature, how much sacerdotal activity qualifies a minister for the exemption, whether a minister has actually engaged in such activities, whether certain entities are "integral agencies" of religious organizations, and, when a minister works for a secular organization, whether a church has made a good faith assignment.²²

In contrast, subjecting ministers to § 119 would significantly reduce church-state interactions. The in-kind requirement would eliminate 87% of ministers because they receive cash allowances.²³ Such ministers would simply have to pay income taxes on all their income. They already report the value of tax-free housing for payroll tax purposes, significantly undercutting any entanglement claims.²⁴ For the remaining 13%, the analysis would focus first on whether the housing was on-site and second on whether they had to live on-site to do their jobs. These enquiries might touch on religious practice, but they would be far less intrusive than the inquiry under § 107.

While the goal of treating all churches and ministers the same seems appealing and uncontroversial, doing so without regard to meaningful differences violates the core tax concepts of horizontal and vertical equity, which hold that those who are similarly situated should be taxed the same, while those who are differently situated should be taxed differently.²⁵ Ministers who must live on-site to perform their job duties are not receiving housing as compensation and are therefore situated differently from those who receive off-site housing or housing allowances as compensation. Those differences should have real-world

²² See *infra* Section I.B.

²³ See Sarah Eekhoff Zylstra, *Are Pastors' Homes that Different?*, CHRISTIANITY TODAY (June 24, 2014), <http://www.christianitytoday.com/ct/2014/june/are-pastors-homes-that-different.html>.

²⁴ I.R.C. § 1402(a)(8) (2018); IRS, TAX GUIDE FOR CHURCHES AND RELIGIOUS ORGANIZATIONS 23 (Aug. 2015) [hereinafter TAX GUIDE], <https://www.irs.gov/pub/irs-pdf/p1828.pdf>. See *infra* Section IV.C, for a discussion of payroll taxes and how they apply to ministers.

²⁵ See, e.g., David Elkins, *Horizontal Equity as a Principle of Tax Theory*, 24 YALE L. & POL'Y REV. 43, 44-45 (2006) (stating that those who are similarly, not identically, situated, should be taxed the same).

tax consequences. Nor should it matter, assuming *arguendo* that all ministerial housing is compensatory, that some churches can provide tax-free housing while others cannot. No one argues that all ministers should receive tax-free income because some churches offer tax-deferred retirement compensation or tax-free health insurance, while others do not. It is not the government's job to support poorer congregations.

Finally, exemptions from payroll taxes and the Affordable Care Act are designed to ensure that religious actors not be forced to violate their religious beliefs. The exemption for ministerial housing rests on entirely different grounds. Thus, the existence of these other exemptions offers no support for the parsonage exemption. Nor would eliminating the parsonage exemption affect their viability.

Part I sets forth the legislative history of the parsonage exemption and how it has been applied. Part II briefly describes the Supreme Court's First Amendment jurisprudence, as well as the specific arguments made in support of the parsonage exemption. Part III addresses the Establishment Clause arguments. Part IV addresses the Free Exercise arguments. The final Part concludes.

I. THE PARSONAGE EXEMPTION

When Congress enacted the modern income tax in 1913, it did not address whether taxpayers should include the value of employer-provided housing in income. The Treasury Department considered this question early on in a number of different contexts, generally concluding that housing could be excluded when it was provided to employees so that they could perform their jobs. For instance, in 1919, the IRS ruled that food and lodging supplied to seamen could be excluded from income.²⁶ In 1920, the IRS came to the same conclusion for those working in camps.²⁷ In 1921, the IRS held that hospital workers who were subject to call twenty-four hours per day and required to accept meals and lodging at the hospital could exclude the value of such meals and lodging from income.²⁸ The Treasury Department first considered this question for ministers in 1921 and held that ministers *should* include the value of any housing they

²⁶ O.D. 265, 1919-1 C.B. 71.

²⁷ T.D. 2992, 1920-2 C.B. 72.

²⁸ O.D. 915, 1921-4 C.B. 85, 1921 WL 50340. In contrast, those who were on duty for shorter periods and who could elect to obtain food and lodging elsewhere were required to include the value of such food and lodging in income. *Id.*

received in income.²⁹ Congress quickly overturned this decision by adding the predecessor to § 107 to the Tax Code.³⁰ What follows is a discussion of the legislative history of the parsonage exemption and how the IRS has applied it.

A. *Legislative History*

As originally enacted, the statute excluded from income “[t]he rental value of a dwelling house and appurtenances thereof furnished to a minister of the gospel as part of his compensation.”³¹ Unfortunately, the legislative history is silent regarding the reason Congress reversed the administrative decision.³² This provision only applied to in-kind housing and typically applied to ministers who lived on-site and acted as caretakers of their churches. While it appeared to put ministers on the same footing as other employees entitled to receive tax-free housing, it explicitly allowed them to receive tax-free housing even when it was intended as compensation, a benefit unavailable to other employees. Moreover, limiting the benefit to in-kind housing meant that certain denominations with a tradition of building parsonages, such as Catholics, were able to offer tax-free housing, while others that did not build parsonages, including most protestant denominations, could not.

In 1954, Congress overhauled the Tax Code and, among other things, codified the rules for tax-free housing outside the ministerial context.³³ As described more fully below in section III.A, the new § 119 mandated that the housing be: (1) in-kind, (2) on-site, (3) required by the employer, and (4) for the employer’s convenience.³⁴ Congress left the broader in-kind housing provision of § 107’s predecessor unchanged. Thus, ministers could continue to receive tax-free housing even if they lived off-site or if the housing were explicitly intended as compensation. In addition, Congress permitted ministers

²⁹ O.D. 862, 1921-4 C.B. 85.

³⁰ Revenue Act of 1921, Pub. L. No. 67-98, § 213(b)(11), 42 Stat. 227, 239 (1921).

³¹ This provision was later codified as § 22(b)(6) of the Internal Revenue Code of 1939. Revenue Act of 1939, Pub. L. No. 76-1, 53 Stat. 510 (1939).

³² See, e.g., *Income Tax: Internal Revenue Hearings on the Proposed Revenue Act of 1921 Before the S. Comm. on Fin., 67th Cong., 497-577 (1921)*; S. Rep. No. 67-257 (1921); H.R. Rep. No. 67-350 (1921).

³³ See H.R. Rep. 83-1337, at 4042 (1954) (indicating the rules were amended to require that meals be provided on-site and that it be a job requirement, restrictions which were missing in the pre-1954 rulings).

³⁴ See Act of Aug. 16, 1954, ch. 736, Pub. L. No. 591-736, 68A Stat. 32, 32.

to receive tax-free cash housing allowances, again without any requirement that the housing be for the employer's convenience.³⁵

Proponents of the parsonage exemption contend that the cash-allowance exemption is part of a broad, neutral policy covering housing, that the special rules for ministers simply reflect the unique circumstances of working as a minister, or that the changes were designed to put ministers on par with secular employees and to ensure that all ministers could receive the same benefits, regardless of differences.³⁶ However, the new and more lenient rules for ministers were part of Cold War efforts to promote religion. Congress added "under God" to the Pledge of Allegiance in 1954 as a way to differentiate the United States from communists in Russia and China.³⁷ In 1956, Congress declared "In God We Trust" to be the official motto of the United States, and the phrase began appearing on paper money in 1957.³⁸

The legislative history outlines four key motivations for the changes to § 107. The first was to support ministers in their fight against communism.³⁹ The second was to subsidize ministers' low salaries.⁴⁰

³⁵ *Id.*

³⁶ See Brief in Support of Defendant's Motion for Summary Judgment, *supra* note 8, at 7-8; Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment, *supra* note 8, at 20; Butterfield, *supra* note 8, at 461-64; Lark, *supra* note 11, at 191.

³⁷ *The Pledge of Allegiance*, UShistory.org, <http://www.ushistory.org/documents/pledge.htm> (last visited Jan. 18, 2017).

³⁸ The motto first appeared on coins during the Civil War. See *History of "In God We Trust,"* U.S. DEP'T TREASURY, <https://www.treasury.gov/about/education/Pages/in-god-we-trust.aspx>.

³⁹ Congressman Peter Mack (Dem. Illinois) sponsored the bill and testified as follows in its support:

Certainly, in these times when we are being threatened by a godless and antireligious world movement, we should correct this discrimination against certain ministers of the gospel who are carrying on such a courageous fight against this foe.

General Revenue Revision: Hearings Before the H. Comm. on Ways & Means, 83d Cong., 1st Sess., Pt. 3, 1576 (1953) [hereinafter *Hearings Before the H. Comm. On Ways & Means*] (statement of Peter Mack, Rep. D-Illinois).

⁴⁰ Congressman Mack argued:

Of our clergymen, 55 percent are receiving less than \$2,500 per year. This is some \$256 less than the \$2,668 annual median income for our labor force. It is well to keep in mind that many of these clergymen support families like the rest of us, and that many of these clergymen still receive low incomes based on the 1940 cost of living but must pay 1953 rents for a dwelling house.

The third was to address perceived discrimination against denominations that did not build parsonages and therefore could not provide tax-free housing.⁴¹ Finally, some argued that the provision was necessary to create equity between rich and poor churches.⁴² No mention at all is made of a broad, neutral housing policy, differences between ministers and lay employees that might warrant more lenient rules, or the need to put ministers on the same footing as laypeople.

In 1984, in preparation for what ultimately became the Tax Reform Act of 1986, the Treasury Department proposed eliminating the exemption along with a host of other tax preferences.⁴³ However, Congress ultimately retained the exemption.

In 2002, litigation arose as to whether ministers could exclude unlimited amounts of cash compensation allocated to and actually spent on housing⁴⁴ or whether the amount excludible should be limited to the rental value of the housing. The Tax Court sided with the minister, and the IRS appealed the decision to the Ninth Circuit, which, *sua sponte*, invited Erwin Chemerinsky to file a brief on § 107(2)'s constitutionality.⁴⁵ In response to an outcry from religious organizations, the government quickly moved to protect the exemption. Congress amended the statute explicitly to limit the allowance to the fair rental value of the home and other associated expenses,⁴⁶ and the Justice Department settled the case and sought to

Id. at 1575.

⁴¹ The House report noted that it was unfair that some ministers got tax-free housing, while others received larger salaries to cover housing costs and had to pay tax on those amounts:

Under present law, the rental value of a home furnished a minister of the gospel as part of his salary is not included in his gross income. This is unfair to those ministers who are not furnished a parsonage, but who receive larger salaries (which are taxable) to compensate them for expenses they incur in supplying their own home.

Your committee has removed the discrimination in the existing law by providing that the present exclusion is to apply to rental allowances paid to ministers to the extent used by them to rent or provide a home.

H.R. Rep. No. 83-1337, at 15 (1954), as reprinted in 1954 U.S.C.C.A.N. 4035, 4040.

⁴² See, e.g., *Hearings Before the H. Comm. On Ways & Means*, *supra* note 39, at 1574.

⁴³ U.S. DEP'T OF THE TREASURY, 1 TAX REFORM FOR FAIRNESS, SIMPLICITY, AND ECONOMIC GROWTH: THE TREASURY DEP'T REPORT TO THE PRESIDENT 73 (1984).

⁴⁴ See *Warren v. Comm'r*, 114 T.C. 343, 343 (2000). This might occur when ministers owned their own homes.

⁴⁵ *Warren v. Comm'r*, 302 F.3d 1012, 1014 (9th Cir. 2002).

⁴⁶ See *Chemerinsky*, *supra* note 7, at 708-09; see also *Clergy Housing Allowance*

dismiss the appeal. The Ninth Circuit acquiesced, over Professor Chemerinsky's objections,⁴⁷ and invited him to file a stand-alone action.⁴⁸ Unfortunately for those who wished to see this issue resolved on the merits, he did not take up that invitation.

The parsonage exemption provides additional benefits to ministers who own their own homes. First, unlike renters, they will end up with an asset partially paid for with tax-free money. Second, not only may they exclude housing allowances, but they may also deduct mortgage interest and property tax expenses associated with their homes.⁴⁹ Typically, deductions are used to determine net income. However, where income is excluded from the tax base, permitting associated deductions can lead to taxpayers being better off than if they had not received the income in the first place.⁵⁰ Thus, Congress typically disallows deductions associated with tax-exempt income.⁵¹ In Revenue

Clarification Act of 2002, Pub. L. No. 107-181, § 2(a), 116 Stat. 583, 583 (2002). Section 107 currently provides in full:

In the case of a minister of the gospel, gross income does not include—

- (1) the rental value of a home furnished to him as part of his compensation; or
- (2) the rental allowance paid to him as part of his compensation, to the extent used by him to rent or provide a home and to the extent such allowance does not exceed the fair rental value of the home, including furnishings and appurtenances such as a garage, plus the cost of utilities.

I.R.C. § 107 (2018).

Congress described the purpose of the act as designed to (1) encourage home ownership; (2) “accommodate clergy in denominations that require as part of their ministry that they locate to specific communities for such periods of time as designated by their denomination, and whose denominations may provide housing or housing allowances”; (3) “minimize government intrusion into internal church operations and the relationship between a church and its clergy”; (4) “accommodate . . . churches through tax policies that strive to be neutral with respect to such differences”; (5) avoid “intrusive inquiries by the government into . . . activities that are inherently religious”; and (6) clarify the extent to which a parsonage allowance is excluded from gross income. H.R. 4156, 107th Cong. § 2 (2002) (as introduced on Apr. 10, 2002).

⁴⁷ *Warren*, 302 F.3d at 1015.

⁴⁸ *Id.*

⁴⁹ See I.R.C. §§ 64, 265(a)(6) (2018).

⁵⁰ A taxpayer who receives \$100 of income and then incurs a deductible \$100 expense has no net change in wealth and no tax liability. It is as if she never received the \$100. If the \$100 is excluded from income and the expenditure remains deductible, she can reduce her taxes by her marginal rate, despite being cash-flow neutral, and is actually better off than had she not earned the \$100.

⁵¹ See, e.g., I.R.C. § 265(a)(1).

Ruling 1962-212, the IRS applied this principle to ministers.⁵² However, in 1986, in response to complaints from ministers, Congress enacted § 265(a)(6), which permits ministers who live in their own homes and receive tax-exempt housing allowances to deduct interest and property tax payments as well.⁵³

Finally, the income and payroll tax treatments for housing benefits provided to clergy differ. Payroll taxes, which include Social Security (also referred to as Federal Insurance Contributions Act or “FICA”) and Medicare, are levied on wage income.⁵⁴ Even though the value of housing benefits provided to clergy, whether in-kind or as cash allowances, is excluded for income tax purposes, it is included for payroll and self-employment tax purposes, at least until clergy retire.⁵⁵

B. Application

To evaluate § 107’s constitutionality, one must look not only to its statutory language, but also to how it has been interpreted and implemented. For instance, as an initial matter, the statute is unconstitutional on its face because it applies only to “ministers of the gospel,” which would include only Christians. However, the IRS has construed the term to include ordained rabbis, imams, and others, including Buddhists, thus avoiding that constitutional issue.⁵⁶ The IRS

⁵² Rev. Rul. 62-212, 1962-2 C.B. 41.

⁵³ Kamron Keele, *A Plea for the Repeal of Section 107: No More Tax-Free Mansions for Dubious “Minsters of the Gospel,”* 56 TAX L. 73, 91 (2002). Section 265(a)(6) also applies to those who receive tax-exempt military housing allowances.

⁵⁴ See I.R.C. § 3121.

⁵⁵ I.R.C. § 1402(a)(8) (2018); TAX GUIDE, *supra* note 24, at 23. See *infra* Section IV.C, for a discussion of payroll taxes and how they apply to ministers.

⁵⁶ See *Salkov v. Comm’r*, 46 T.C. 190, 194 (1966) (noting that Congress did not intend to exclude non-Christian faiths or persons who are equivalent to “ministers”). For ease of reference, I will continue to use the term “minister.”

As discussed below in section II.A, interpreting the provision to cover all religious leaders does not avoid constitutional concerns because it still favors religion over non-religion. Ellen Aprill has suggested that one could protect the exemption by broadening it to include those working at non-profit organizations who are expected to meet with members, patients, or clients at all times. Ellen P. Aprill, *Parsonage and Tax Policy: Rethinking the Exclusion*, 96 TAX NOTES 1243, 1245 (2002). One commentator has suggested that the IRS can do this administratively, see Meredith Satz, *Re-Interpreting the Parsonage Exclusion: Constitutional Challenges and the Agency Response in the Wake of Freedom From Religion Foundation, Inc. v. Lew*, 67 ADMIN. L. REV. 751, 754-65 (2015), but that would likely stretch the term “minister of the gospel” beyond its breaking point.

has also declined to rule *ex ante* whether individuals qualify as “minister[s] of the gospel” for federal tax purposes.⁵⁷

Tying the benefit to ordination can raise difficult questions. For one, one must determine whether the religion is legitimate. While this is easy for more established religions, it becomes more difficult with new and unusual religions.⁵⁸ Next, it may be difficult to know who is properly ordained. While many sects have well-established ordination procedures, in certain Christian traditions, one can self-identify as a minister without any formal training or ordination process. Indeed, mail order “ordinations” are readily available.⁵⁹ In addition, some religions have different types of religious leaders, and the IRS must determine which are entitled to the exemption.⁶⁰ Tying the benefit to ordination can also have gender consequences. Many religions, including Orthodox Judaism and Christianity, Catholicism, and Islam, do not ordain women. Thus, women in these religious communities cannot receive this benefit.⁶¹

Second, the statute’s plain language does not limit the exemption to those working as ministers. Thus, a minister who works as a plumber, whether for a church or Roto-Rooter, would arguably be eligible to

⁵⁷ Rev. Proc. 2016-3, 2016-1 I.R.B. 126.

⁵⁸ See, e.g., Bobby Henderson, *Success (and Trouble) for Arizona Pastafarian’s ID Photo*, CHURCH OF THE FLYING SPAGHETTI MONSTER (June 2, 2017), <https://www.venganza.org/2017/06/arizona-id> (describing one “Pastafarian’s” success in convincing the Arizona Department of Motor Vehicles to allow him to wear a colander on his head for his driver’s license picture on religious grounds); Don Lattin, *Rock Religion? A Religious Cult That Sprang from the Extreme Fringe of the Grateful Dead’s Following Is Drawing Critics Who Say Devotees Are Brainwashed*, SUN SENTINEL, Jan. 18, 1992, http://articles.sun-sentinel.com/1992-01-18/features/9201030888_1_dennis-mcnally-jerry-garcia-sect.

⁵⁹ See, e.g., *Become an Ordained Minister*, UNIVERSAL LIFE CHURCH, <https://www.themonastery.org/landing/get-ordained?gclid=CMnpj4XEmNQCFVOUfgodqNYDzQ> (last visited Sept. 18, 2017).

⁶⁰ See, e.g., *Salkov v. Comm’r*, 46 T.C. 190, 199 (1966) (asserting a Jewish cantor commissioned by recognized national body and installed by local congregation with power to perform certain religious functions is qualified under § 107 even though he could not perform all functions of ordained rabbi); *Silverman v. Comm’r*, 32 A.F.T.R.2d 73-5379 1, 5 (8th Cir. 1973) (asserting the same conclusion, with extensive discussion of Judaism’s “dual ministry”).

⁶¹ For instance, women who teach sacred texts at orthodox Jewish religious schools perform the same jobs as rabbis; however, they have generally been excluded from § 107 because they are not ordained. See Michael J. Brodye, *Orthodox Yeshivas, Female Instructors, and the Parsonage Exemption*, 18 TAX’N EXEMPTS 44, 48 (2006); Jacob Lewin, *Orthodox Jewish Women and Eligibility for the Parsonage Exemption*, 17 CARDOZO J.L. & GENDER 139, 163-69 (2010) (arguing that such women should come within § 107).

exclude any housing allowance he received. However, the Treasury regulations specify that housing allowances must be in connection with services ordinarily provided by a minister.⁶² This also raises a host of difficult questions.

Ministers who work for church organizations serve in a number of roles beyond leading a congregation, and the IRS must decide what counts as ministerial for tax purposes. For instance, in Revenue Ruling 57-129, the IRS held that ministers involved in managing the organization would be considered ministers for tax purposes, while ministers acting as stenographers, mail clerks, and janitors would not.⁶³ The ruling did not address how much ministerial work was sufficient to qualify for the exemption.

When ministers work for non-church organizations, they must demonstrate that their church has made a bona fide assignment to their employer to serve church purposes, in addition to showing that their work is ministerial in nature.⁶⁴ However, the IRS has held that some organizations, such as parochial schools and religious colleges, are “integral agencies” of a church, such that ministers who work for those entities are eligible for exemption, even absent an assignment.⁶⁵ The IRS has taken a broad view of ministerial duties in this context, permitting administrators, counselors, and teachers at such institutions to qualify.⁶⁶

Extending the benefit to “integral agencies” and taking a broad view of what constitutes ministerial work has led to some anomalous results. For instance, ministers working as teachers and administrators can receive tax-free housing that is unavailable to non-minister co-workers performing the same jobs.⁶⁷ Some denominations, such as the

⁶² Treas. Reg. § 1.107-1(a) (as amended in 1963). The regulations incorporate the test set forth in Treas. Reg. § 1.1402(c)-5 (as amended in 1968) for determining whether duties qualify as those typically performed by a minister. Section 1402 provides definitions for purposes of self-employment taxes. For a review of IRS attempts to determine what activities count as ministerial and the difficult doctrinal issues that arise, see generally Roger H. Taft, *Tax Benefits for the Clergy: The Unconstitutionality of Section 107*, 62 GEO. L.J. 1261 (1974).

⁶³ This ruling focused on the exemption for ministers for social security taxes, but the reasoning applies equally to income from the parsonage exemption.

⁶⁴ See *Boyer v. Comm’r*, 69 T.C. 521, 532 (1977); Treas. Reg. § 1.1402(c)-5(c)(ii)(2); I.R.S. Priv. Ltr. Rul. 9720022 (Feb. 11, 1997).

⁶⁵ Treas. Reg. § 1.1402(c)-5(b)(2)(iv).

⁶⁶ See, e.g., Rev. Rul. 70-549, 1970-2 C.B. 16; Rev. Rul. 62-171, 1962-2 C.B. 39; I.R.S. Priv. Ltr. Rul. 139444-09 (June 11, 2010); I.R.S. Priv. Ltr. Rul. 2000-02-040 (Jan. 14, 2000); I.R.S. Tech. Adv. Mem. 91-44-047 (Nov. 1, 1991); I.R.S. Priv. Ltr. Rul. 91-26-048 (Apr. 2, 1991); I.R.S. Tech. Adv. Mem. 90-33-002 (Aug. 17, 1990).

⁶⁷ See Joel Newman, *On Section 107’s Worst Feature: The Teacher-Precacher*, 61 TAX

Churches of Christ,⁶⁸ designate *all* adherents as ministers, thus opening up the exemption far beyond what most people likely imagine. According to a church elder, “[e]very believer, and the Churches of Christ would emphasize baptized believer, is a minister.”⁶⁹ To qualify as a minister, all one must do is obtain a letter from the church, and apparently almost 100% of applications are approved.⁷⁰ Thus a large percentage of the employees at colleges affiliated with the Churches of Christ are entitled to tax-free housing.

For instance, in Revenue Ruling 70-549, the IRS determined that Abilene Christian College (now University) was an integral part of the Churches of Christ and that therefore all church members working there as teachers were entitled to the parsonage exemption.⁷¹ In *Reed v. Commissioner*,⁷² the Tax Court considered whether teachers and administrators at Lubbock Christian College (also affiliated with the Churches of Christ) could exempt the fair market rental value of their homes, even though their out of pocket costs were lower. Most worked as teachers in subjects such as English, History, Psychology, Music, and Physical Education. One served as the Director of Business Services and another as the Director of College Relations and Alumni.⁷³ Each employee lived off-campus and either rented or owned his own home.⁷⁴ The court simply assumed that these employees were entitled to the parsonage exemption, ultimately limiting the deduction to out-of-pocket expenses.

Pepperdine University is also affiliated with the Churches of Christ. As reported in the Pepperdine Graphic, the student newspaper, one of

NOTES 1505, 1507 (1993) (noting that the extension provides significant tax benefits to ordained teachers, even though they are doing the exact same jobs as non-ordained teachers).

⁶⁸ People use the terms “Church of Christ,” “church of Christ,” and “churches of Christ.” The use of lower case is meant to indicate that it is not a denomination in the traditional sense. The use of the plural is meant to indicate the independent nature of each congregation and the ways in which they sometimes work together. I have elected to use “Churches of Christ.”

⁶⁹ Joann Groff & Sarah Carrillo, *What Is a Minister?*, PEPP. U. GRAPHIC, Oct. 30, 2003, <http://pepperdine-graphic.com/what-is-a-minister>.

⁷⁰ *Id.*

⁷¹ See Rev. Rul. 70-549, 1970-2 C.B. 16.

⁷² See *Reed v. Comm’r*, 82 T.C. 208, 210 (1984) (stating the cases were consolidated for trial).

⁷³ This information was not contained in the decision but was available from Robert Baty, a former IRS employee, who was personally familiar with the case. Telephone Interview with Robert Baty, Retired IRS Appeals Officer, IRS (July 15, 2016).

⁷⁴ *Reed*, 82 T.C. at 210.

the shocking discoveries when Pepperdine released its Form 990 in 2003 was the number of professors and administrators who were classified as ministers and who took advantage of the parsonage exemption.⁷⁵ But perhaps the most jaw dropping of these examples can be found in *Jobe v. Commissioner*.⁷⁶ The IRS challenged the ability of the basketball coach working at Oklahoma Christian College (“OCC”) to claim the parsonage exemption.⁷⁷ The IRS initially refused to recognize Coach Jobe as a minister and rejected his effort to exclude his \$6,600 housing allowance from income.⁷⁸ However, the IRS dismissed the case before trial, thus permitting Coach Jobe to exclude his housing allowance.⁷⁹

Allowing these schools to offer professors, administrators, and even basketball coaches tax-free housing gives them a significant advantage when competing with other universities, even other religiously-affiliated universities, for new hires. One of the justifications for allowing tax-free cash allowances was to equalize the treatment of all religions, despite differences in religious doctrine and practice.⁸⁰ These examples reveal that religious doctrine and practice continue to yield disparate tax treatment for similarly situated institutions.

Third, unlike with other housing benefits, ministers may receive tax-free cash housing allowances as part of their retirement pay.⁸¹ As a result, the benefit can continue long after ministers have stopped working, undermining any claim that the housing is for the convenience of the employer, that is, necessary so that the employee can do her job, as is the case with the generally applicable housing rule found in § 119.

Fourth, although the 2002 amendment limited the amount excludible to the lesser of the rental value of the housing or out-of-pocket expenses,⁸² it can still provide significant benefits to individual ministers. For instance, Joel Osteen lives in a \$10.5 million home⁸³ and is entitled to exclude the fair rental value of that home so long as

⁷⁵ See Groff & Carrillo, *supra* note 69.

⁷⁶ No. 33686-83 (T.C. Mar. 21, 1985).

⁷⁷ See Petition at 2, 11, *Jobe*, No. 33686-83 (Mar. 21, 1985).

⁷⁸ See *id.*

⁷⁹ See *id.* at 2.

⁸⁰ See *Hearings Before the H. Comm. On Ways & Means, supra* note 39, at 1574-76.

⁸¹ See TAX GUIDE, *supra* note 24, at 23.

⁸² See Clergy Housing Allowance Clarification Act, 26 U.S.C. § 107 (2002); *Reed v. Comm’r*, 82 T.C. 208, 211 (1984).

⁸³ Shana Raley-Lusk, *Joel Osteen Fun Facts: 10 Things You Might Not Know About Evangelical Leader Joel Osteen*, NEWSMAX (May 8, 2015, 4:56 PM), <http://www.newsmax.com/FastFeatures/joel-osteen-fun-facts/2015/05/08/id/643575>.

he spends that money on the home and his church allocates that amount to housing.

Finally, the parsonage exemption is expensive in the absolute. The Treasury Department's most recent tax expenditure budget estimated that it will cost approximately \$9.3 billion over the next ten years.⁸⁴ Assuming a 25% marginal tax rate, this suggests that ministers will receive \$37 billion in tax-free housing and housing allowances over this period under terms not available to others.⁸⁵ According to a recent report, approximately 87% of all ministers receive a cash allowance, meaning that a relatively small percentage might be eligible for exemption under the generally applicable rule of § 119.⁸⁶

While some of the recent changes to the rule have curtailed some of the abuses, concerns still abound. In 2007, Senator Grassley (Rep. Iowa), the then-ranking member of the Senate Finance Committee, undertook an investigation of a number of churches and their practices.⁸⁷ More recently, John Oliver devoted an episode of *Last Week Tonight with John Oliver* to televangelists, revealing that the exemption and its abuses continue to be controversial.⁸⁸

II. THE CONSTITUTIONAL QUESTION

Those seeking to challenge the parsonage exemption on constitutional grounds face two hurdles.⁸⁹ First, the Supreme Court has made it difficult to establish standing for those seeking to

⁸⁴ See TAX EXPENDITURES, *supra* note 2.

⁸⁵ \$49.3 billion, if we hold ministerial compensation constant. See *supra* note 3.

⁸⁶ See Zylstra, *supra* note 23.

⁸⁷ See Letter from Senator Charles Grassley to Randy & Paula White, Without Walls Int'l Church, Paula White Ministries (Nov. 5, 2007) [hereinafter Grassley Letter], <https://www.finance.senate.gov/imo/media/doc/prg110607a.pdf>; Kathy Lohr, *Senator Probes Megachurches' Finances*, NPR (Dec. 4, 2007), <http://www.npr.org/templates/story/story.php?storyId=16860611>.

⁸⁸ See HBO, *Last Week Tonight with John Oliver: Televangelists*, YOUTUBE (Aug. 16, 2015), <https://www.youtube.com/watch?v=7y1xJAVZxXg> (discussing the parsonage exemption at the 9:50 mark).

⁸⁹ The Tax Anti-Injunction Act could pose an additional hurdle. To protect the tax collection process, the Act precludes taxpayers from seeking an injunction in most cases, forcing them instead to challenge provisions through the tax collection process. I.R.C. § 7421 (2018). Courts have held that it does not bar taxpayer lawsuits in this context. See, e.g., *Am. Atheists, Inc. v. Shulman*, 21 F. Supp. 3d 856, 868 (E.D. Ky. 2014). In any event, the path the courts have set for establishing standing — that plaintiffs must seek the tax benefit and be denied — ensures that they must go through that process, obviating the need for a stand-alone injunction.

challenge tax provisions. After a number of false starts,⁹⁰ litigants appear to have finally figured out a way to overcome the standing hurdles, at least with regard to § 107(2).⁹¹ Second, those challenging the parsonage exemption must establish that it violates the First Amendment. The standing issues are beyond the scope of this Article. Instead, this Part sets forth the Supreme Court's relevant First Amendment jurisprudence and the specific arguments parsonage exemption supporters have raised in its defense.

A. *First Amendment Jurisprudence*

The First Amendment contains both an Establishment Clause and a Free Exercise Clause, collectively referred to as the "Religion Clauses." The Establishment Clause limits the government's ability to support religious organizations or practices, while the Free Exercise Clause limits the government's ability to interfere with them. The Supreme Court's jurisprudence on these clauses is a confusing mess, in part because the Establishment and Free Exercise Clauses are often in tension with one another, and in part because of the myriad ways in which First Amendment issues arise.

As Chief Justice Burger noted, "the Court's opinions reflect the limitations inherent in formulating general principles on a case-by-case basis."⁹² The "considerable internal inconsistencies," he noted, "derives from what, in retrospect, may have been too sweeping utterances on aspects of these clauses that seemed clear in relation to the particular case but have limited meaning as general principles."⁹³ To complicate matters, each individual justice appears to have his or her own take on the First Amendment's Establishment and Free Exercise Clauses and their requirements. As a result, many of the cases involve pluralities, with multiple concurring and dissenting opinions, making it quite difficult to determine which approach should be considered controlling precedent.

Plumbing the depths of this jurisprudence is beyond the scope of this Article, but some understanding of the basic concerns with which the Court struggles helps frame the issues here. In *Lemon v. Kurtzman*,

⁹⁰ See, e.g., *Freedom From Religion Found., Inc. v. Lew*, 773 F.3d 815, 825 (7th Cir. 2014); *Am. Atheists, Inc.*, 21 F. Supp. 3d at 872.

⁹¹ Two officers of the Freedom From Religion Foundation received cash allowances for housing, paid tax on such allowances and filed suit for a refund. The IRS has denied the refund, leading to a refund action in federal district court. See *Freedom From Religion Found., Inc.*, 773 F.3d at 819.

⁹² *Walz v. Tax Comm'n of N.Y.C.*, 397 U.S. 664, 668 (1970).

⁹³ *Id.*

the Supreme Court set forth a three-prong test for deciding whether a statute violates the First Amendment.⁹⁴ To pass muster, a statute: (1) must have a secular purpose, (2) must have a primary effect that neither hinders nor advances religion, and (3) may not engender excessive entanglement of government in religious affairs. However, the court has often abandoned that test.⁹⁵ It has identified other factors that bear on a statute's constitutionality, including historical practice,⁹⁶ the appearance of endorsement,⁹⁷ and the potential for religious divisiveness.⁹⁸

Insofar as the parsonage exemption involves tax exemption, it may help to explore in detail *Walz v. Tax Commissioner of New York City*⁹⁹ and *Texas Monthly, Inc. v. Bullock*,¹⁰⁰ the two leading cases in this area. *Walz* involved a challenge to New York's property tax exemption for charitable, educational, and religious organizations. *Texas Monthly* involved a challenge to Texas's decision to exempt religious publications from the state sales tax. Both resulted in multiple opinions, reflecting different views of the First Amendment.

Chief Justice Burger wrote for the Court in *Walz*, holding that the property tax exemption for religious organizations did not violate the Constitution. The Chief Justice began by noting the tension between

⁹⁴ *Lemon v. Kurtzman*, 403 U.S. 602, 612-13 (1971).

⁹⁵ See, e.g., *Lamb's Chapel v. Center Moriches Union Free Sch. Dist.*, 508 U.S. 384, 397 (1993) ("As to the Court's invocation of the *Lemon* test: Like some ghoul in a late-night horror movie that repeatedly sits up in its grave and shuffles abroad, after being repeatedly killed and buried, *Lemon* stalks our Establishment Clause jurisprudence once again, frightening the little children and school attorneys of Center Moriches Union Free School District.").

⁹⁶ See, e.g., *Marsh v. Chambers*, 463 U.S. 783, 792 (1983) (upholding prayer before public meetings in part because of historical precedent).

⁹⁷ See, e.g., *Cty. of Allegheny v. ACLU*, 492 U.S. 573, 632-37 (1989) (O'Connor, J., concurring). O'Connor suggests that the question of endorsement should be evaluated using an "objective observer, acquainted with the text, legislative history, and implementation of the statute." *Wallace v. Jaffree*, 472 U.S. 38, 76 (1985) (O'Connor, J., concurring). Justice Stevens disagrees, see *Capitol Square Review & Advisory Bd. v. Pinette*, 515 U.S. 753, 800 n.5 (1995) (Stevens, J., dissenting), and the circuits have split. See, e.g., *Brooks v. Oak Ridge*, 222 F.3d 259, 266 (6th Cir. 2000) (adopting O'Connor's knowledgeable reasonable observer standard); *ACLU v. Schundler*, 104 F.3d 1435, 1448 (3d Cir. 1997) (adopting Justice Stevens's reasonable observer standard). If the Court undertakes an endorsement analysis and adopts Justice O'Connor's approach to the reasonable observer, the legislative history and discussion below of how the parsonage exemption fits within the Tax Code are clearly relevant.

⁹⁸ See, e.g., *Lemon*, 403 U.S. at 623.

⁹⁹ *Walz v. Tax Comm'n of N.Y.C.*, 397 U.S. 664 (1970).

¹⁰⁰ 489 U.S. 1 (1989).

the two Religion Clauses and observing that there is “play in the joints,” where the government is free to act.¹⁰¹ He further remarked that “[n]o perfect or absolute separation is really possible.”¹⁰² On the question of historical practice, he noted “no one acquires a vested or protected right in violation of the Constitution by long use, even when that span of time covers our entire national existence and indeed predates it,”¹⁰³ making clear at the same time that historical practice is not something lightly set aside.¹⁰⁴ He also posited that exemptions differ from direct subsidies because they do not involve forced extractions and transfers from the treasury.¹⁰⁵

Chief Justice Burger found that the legislative purpose of the statute at issue was neither to advance nor inhibit religion, based in large part on the fact that churches were included in a broad range of similar organizations eligible for tax exemption, all of which fostered “moral or mental improvement.”¹⁰⁶ In addition, he noted that imposing the property tax on churches would increase interactions between church and state because the state would need to value property and potentially impose tax liens and foreclose on churches if taxes went unpaid.¹⁰⁷ This could lead to significant confrontations between churches and the state.

Justice Brennan concurred, but focused primarily on the history of the property tax exemption, its purpose, and how it has operated.¹⁰⁸ Among other things, he agreed with Chief Justice Burger’s view of the difference between tax exemptions and direct subsidies.¹⁰⁹ Justice Harlan concurred, noting that his main concerns were “neutrality” and “voluntarism.”¹¹⁰ Justice Douglas dissented on the theory that the statute aided the religious as against non-believers, thus advancing religion over non-religion.¹¹¹

Texas Monthly generated four opinions and no majority in holding the sales tax exemption at issue unconstitutional. Justice Brennan,

¹⁰¹ *Walz*, 397 U.S. at 669.

¹⁰² *Id.* at 670.

¹⁰³ *Id.* at 678.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.* at 675.

¹⁰⁶ *Id.* at 672. The Court expressly did not justify the exemption based on “good works” done by particular churches. *Id.* at 674.

¹⁰⁷ *Id.* at 674.

¹⁰⁸ *Id.* at 680.

¹⁰⁹ *See id.* at 690-93.

¹¹⁰ *Id.* at 694.

¹¹¹ *Id.* at 700.

joined by Justices Marshall and Stevens, announced the judgment of the Court and began by reiterating that: (1) the Establishment Clause prohibits legislation that endorses one or another set of religious beliefs or religion generally, (2) laws must have a secular purpose, and (3) laws may not have a principle or primary effect that advances or inhibits religion.¹¹²

Justice Brennan observed that the cases that permitted benefits to flow to religious organizations, such as *Walz*, did so typically in contexts where religious organizations were but one of a broad class of similar recipients.¹¹³ He found that the sales tax exemption at issue violated the Establishment Clause because it was targeted solely at religious publications. Justice Brennan rejected Chief Justice Burger's statement in *Walz* (and in his own concurrence in that case) that tax exemptions should not be considered subsidies, stating that "every tax exemption constitutes a subsidy that affects nonqualifying taxpayers, forcing them to become 'indirect and vicarious "donors."'"¹¹⁴ He continued by noting that "when government directs a subsidy exclusively to religious organizations that is not required by the Free Exercise Clause and that either burdens non-beneficiaries markedly or cannot reasonably be seen as removing a significant state-imposed deterrent to the free exercise of religion," it impermissibly benefits religion and conveys a message of endorsement.¹¹⁵

Justice White concurred with the judgment, basing his decision on the First Amendment's Free Press Clause. He found the statute unconstitutional because it discriminated based on content.¹¹⁶

Justice Scalia, joined by Justices Rehnquist and Kennedy, issued one of his trademark dissents. Whereas Justice Brennan had focused primarily on the Establishment Clause, Justice Scalia focused primarily on the Free Exercise Clause. He contended that the exemption for religious periodicals did not establish religion.¹¹⁷ Instead, he believed the exemption was a permissible, but not required, accommodation for religion because it limited the interactions between the state and

¹¹² *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 8-9 (1989).

¹¹³ *Id.* at 11.

¹¹⁴ *Id.* at 14 (citations omitted).

¹¹⁵ *Id.* at 15. Justice Brennan did not indicate the necessary breadth for an exemption to be seen as generally applicable.

¹¹⁶ *Id.* at 25-26.

¹¹⁷ *See id.* at 29-45.

religious organizations.¹¹⁸ In his view, *Walz* was dispositive and should have governed.¹¹⁹

Justice Blackmun, joined by Justice O'Connor, was uncomfortable with both Justice Brennan's opinion and Justice Scalia's dissent because he viewed them as subordinating one Religion Clause to the other.¹²⁰ He acknowledged that a broader exemption could satisfy both clauses, but he did not specify how broad an exemption would have to be to pass muster.¹²¹ That said, in his view, a narrowly drawn exemption, applicable only to religious periodicals, clearly violated the First Amendment.¹²²

B. Arguments Supporting the Parsonage Exemption

Supporters of the parsonage exemption make two types of arguments that can be traced back to *Walz* and *Texas Monthly*. The first seeks to establish that the parsonage exemption does not, in fact, single religion out for a special subsidy in violation of the Establishment Clause. Some have argued that the exemption should be read in context with other housing provisions found in the Code and that, when read in this context, the exemption should be understood to be part of a broad, neutral housing policy that happens to include ministers, similar to the property tax exemption the Court considered and approved in *Walz*.¹²³ Indeed, some argue that the exemption is necessary to put ministers on the same footing as laypersons.¹²⁴ Alternately, they argue that tax exemptions differ from direct spending and should not be considered support for Establishment Clause purposes, even if they do single out religious organizations and actors.¹²⁵

¹¹⁸ See *id.* at 30-31, 39, 41-42, 45.

¹¹⁹ See *id.* at 33-40, 42-44.

¹²⁰ See *id.* at 27-28.

¹²¹ See *id.* at 28.

¹²² See *id.*

¹²³ See sources cited *supra* note 8.

¹²⁴ See sources cited *supra* note 11.

¹²⁵ See sources cited *supra* note 9. Professor Zelinsky also contends that the parsonage exemption is normative, and not a subsidy, because it is meant to accommodate religion in conformance with the Free Exercise Clause. See Zelinsky, *supra* note 10, at 1644. As demonstrated below in section III.A, "normative" for tax purposes refers to the extent to which the rule conforms to an ideal income definition. Deviations to accommodate religion are by definition not normative. In any event, creating a special rule for religion acts like a subsidy, even if one was not intended. In this case, the legislative history reveals that one was.

The second type of argument concedes that the exemption may single religion out for a benefit but asserts that it is nonetheless permissible under the Free Exercise Clause to avoid or, at the very least lessen, church-state entanglement. For instance, some supporters argue that the exemption is constitutionally permitted as an accommodation to religion because it reduces entanglement relative to applying the rule found in § 119.¹²⁶ Others argue that § 119 discriminates among different religions, and § 107 is necessary to ensure that all religions are treated equally, despite differences in their resources and practices.¹²⁷ Finally, some supporters point to other exemptions found in the Tax Code and elsewhere for religious actors as evidence that this exception for religious actors is permitted.¹²⁸ Framed negatively, they argue that finding the parsonage exemption unconstitutional would put these other exemptions at risk.¹²⁹

Regardless of the First Amendment test the Supreme Court ultimately applies, a detailed and nuanced understanding of tax policy and how the parsonage exemption and other housing provisions function within the Code is necessary to evaluate these arguments. We turn next to a careful analysis of those arguments from a tax perspective.

III. SECTION 107 RAISES ESTABLISHMENT CLAUSE CONCERNS

This Part considers the claim that the parsonage exemption does not violate the First Amendment's Establishment Clause. Section A

¹²⁶ See generally sources cited *supra* note 10. Zelinsky defends § 107(2) as constitutional, but he argues that it is bad public policy. See Zelinsky, *supra* note 10, at 1665.

¹²⁷ See Butterfield et al., *supra* note 8, at 261; sources cited *supra* note 11. One commentator has suggested that Code § 107(1) is permissible because it avoids entanglement with church-owned property, while Code § 107(2) is unconstitutional because it does not involve church-owned property. Thomas E. O'Neill, *Constitutional Challenge to Section 107 of the Internal Revenue Code*, 57 NOTRE DAME L. REV. 853, 860-67 (1982).

¹²⁸ See Zelinsky, *supra* note 10, at 135-41.

¹²⁹ Supporters also make a historical argument, noting that property tax exemptions for churches pre-date the United States. See Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment, *supra* note 8, at 2-3, 22-27. While true, we are talking here about income taxes, not property taxes. Income taxes are imposed on ministers, not churches, and they have been from the very beginning. See Revenue Act of 1913, Pub. L. No. 63-16, § 2, 38 Stat. 114, 167. While in-kind housing has been exempted since 1921, the broader exemption for cash allowances dates to 1954. See Act of Aug. 16, 1954, ch. 736, Pub. L. No. 591-736, 68A Stat. 32, 32. Efforts to justify a relatively new income tax exemption for ministers by reference to an older property tax exemption for churches are strained.

addresses the claim that the exemption is part of a broad, neutral housing policy that naturally includes ministers. Section B addresses the claim that tax exemptions should not be considered subsidies for Establishment Clause purposes.

A. *Section 107 Is Not Part of a Broad, Neutral Housing Policy that Naturally Includes Ministers*

Although § 107 indisputably singles out religious actors for a tax benefit, supporters have argued that it does not violate the Establishment Clause because it is part of a web of similar provisions that, taken as a whole, constitute a broadly applicable, neutral housing policy.¹³⁰ In their view, the exemption is no different from that at issue in *Walz*, which excused a variety of institutions, including churches, from the state property tax, or § 501(c)(3), which exempts educational institutions, charities, and churches from income tax. Indeed, some have argued that § 107(2) (allowing tax-free cash allowances) is necessary to ensure that ministers are not discriminated against relative to non-minister employees.¹³¹ To the extent that the rules for ministers are more lenient than those generally applicable, they argue that the special circumstances of ministerial employment warrant such treatment.¹³²

These arguments are problematic for a number of reasons. For instance, both § 501(c)(3) and the property tax exemption at issue in *Walz* were contained in a single provision and provided identical benefits to similar organizations. Parsonage exemption proponents do not cite to any other example of purportedly broad, neutral policy contained in a variety of different provisions scattered throughout the Code, let alone one a court has found to justify special benefits for religious actors. Nor do the legislative histories of these different provisions suggest in any way that Congress was thinking broadly of housing policy or had the other housing provisions in mind when it expanded the benefits for ministers in 1954, while at the same time tightening up the generally applicable rules. Indeed, the legislative history reveals the opposite; Congress was laser-focused on providing

¹³⁰ See sources cited *supra* note 8; see also Peter J. Reilly, *In Defense of Special Tax Treatment for Clergy*, FORBES (Sept. 6, 2012, 6:44 AM), <http://www.forbes.com/sites/peterjreilly/2012/09/06/in-defense-of-special-tax-treatment-for-clergy/#6d4530d672b4> (discussing how § 107 is constitutional if analyzed to be a part of the employer assisted housing tax exemption).

¹³¹ See sources cited *supra* note 11.

¹³² See Intervenor Defendants' Brief in Support of Their Motion for Summary Judgment, *supra* note 8, at 30-36.

special benefits to ministers, and ministers alone.¹³³ The record is devoid of any discussion of how ministers are either similar to or different from other employees who receive housing benefits, warranting special treatment. In sum, these arguments are nothing more than an ex post, ahistorical effort to create constitutional cover for the parsonage exemption.

However, one need not even look to the legislative history to debunk these claims. Rather, viewing the different housing provision through a tax lens reveals that they serve very different functions and therefore are not part of a broad, neutral housing policy. This section begins with a discussion of the basic structure of the Tax Code and the treatment of fringe benefits generally before turning to the different housing provisions.

1. The Basic Structure and Nature of the Tax Code

A close look at the Tax Code reveals three basic kinds of rules. The first is normative, designed to measure income so that the appropriate amount of tax can be collected.¹³⁴ The second is administrative, required to make the Tax Code capable of enforcement¹³⁵ or to protect some element of the Code, such as progressivity.¹³⁶ The third, often referred to as “tax expenditures,” promotes some non-tax policy, such as home ownership¹³⁷ or health insurance,¹³⁸ or supporting the poor.¹³⁹

At times, it is difficult to classify a provision. For instance, it is not clear whether the decision not to tax imputed income, such as the value of owner-occupied housing, reflects a belief that such value is

¹³³ See *supra* Section I.B.

¹³⁴ See, e.g., I.R.C. §§ 162, 1001, 1011, 1012, and 1016 (2018). These rules, which allow business deductions and track and account for basis on sale or disposition of an asset, are necessary to determine the amount of gain or loss taxpayers experience. See *id.*

¹³⁵ See, e.g., I.R.C. § 102(c). The use of bright-line rules often reflects the need to make the rules administrable. See *id.* For instance, § 102(a) excludes gifts from income. *Id.* Section 102(c) excludes all employer-provided gifts from the general rule, thereby avoiding difficult litigation over whether transfers from employers to employees should be treated as excludible gifts or taxable compensation. *Id.*

¹³⁶ See, e.g., I.R.C. § 1015(a) (2018). For instance, the shifting basis rules found in § 1015 are necessary to prevent taxpayers from shifting losses to others in higher tax brackets. See *id.*

¹³⁷ See, e.g., I.R.C. § 36 (2018) (first time homebuyer credit); I.R.C. § 121 (2018) (exclusion of sale proceeds on home); I.R.C. § 163(h)(3) (2018) (mortgage interest deduction).

¹³⁸ See, e.g., I.R.C. §§ 105-106 (2018) (exclusion of employer-provided healthcare).

¹³⁹ See I.R.C. § 32(l) (2018) (Earned Income Tax Credit).

not income or the understanding that valuation and liquidity concerns make taxing such income infeasible.¹⁴⁰ The answer to this question depends in large part upon the income definition one believes the Tax Code is designed to implement. Before turning to the Tax Code's housing provisions, I begin with a brief discussion of tax theory and policy and the treatment of fringe benefits, generally, to illustrate how tax theorists approach these kinds of questions.

2. Fringe Benefits, Generally

Code § 61(a)(1) includes “[c]ompensation for services, including fees, commissions, fringe benefits, and similar items” in income. Fringe benefits are typically non-wage, in-kind compensation, and they are included in income as a normative matter because they represent an accession to wealth.¹⁴¹ Nonetheless, the Code excludes a number of fringe benefits from income. In some cases, they are excluded to promote some social policy. In others, administrative concerns dominate. Finally, in some cases, the benefit provided is meant to advance the employer's interests and not as compensation, even though some benefit may accrue to the employee. Where non-compensatory purposes dominate, Congress and the courts exclude the benefits on both normative and administrative grounds.

a. Subsidies

The exemption for qualified transportation fringe benefits found in Code § 132(a)(5) provides a good example of a rule designed to

¹⁴⁰ Another example can be seen in the debate over whether the exclusion for gifts and the deduction for charitable giving are normative, administrative, or subsidies. Compare William D. Andrews, *Personal Deductions in an Ideal Income Tax*, 86 HARV. L. REV. 309, 313 (1972) (arguing that the charitable contribution deduction is appropriate under a pure income tax), and Douglas A. Kahn & Jeffery H. Kahn, “Gifts, Gifts, and Gifts” — *The Income Tax Definition and Treatment of Private and Charitable “Gifts” and a Principled Policy Justification for the Exclusion of Gifts from Income*, 78 NOTRE DAME L. REV. 441, 461 (2003) (arguing that the exemption for gifts is appropriate under basic tax theory), with Mark G. Kelman, *Personal Deductions Revisited: Why They Fit Poorly in an “Ideal” Income Tax and Why They Fit Worse in a Far from Ideal World*, 31 STAN. L. REV. 831, 834-35 (1979), and Marjorie E. Kornhauser, *The Constitutional Meaning of Income and the Income Taxation of Gifts*, 25 CONN. L. REV. 1, 29-30 (1992) (arguing that gifts should be included in income).

¹⁴¹ Some have suggested that income should include only cash transactions. See Andrews, *supra* note 140, at 318. Some have suggested that income should include only cash transactions. *Id.* Under this view, the decision to include fringe benefits in income would be administrative in nature, designed to prevent people from avoiding taxes by arranging to be paid in-kind. *Id.*

advance a non-tax objective. Tax law typically treats commuting expenses as personal and therefore not deductible.¹⁴² If an employer directly pays for an employee's non-deductible expense, such amounts are typically included in income. Nonetheless, Congress has determined that driving alone entails negative externalities that taxpayers typically do not take into account. Accordingly, it has decided to subsidize joint commuting, mass transit, and even bicycling to work.¹⁴³ Section 132(f) does so by permitting taxpayers to exclude from income employer-provided transportation via commuter highway vehicles, transit passes, qualified parking, and qualified bicycle-commuting reimbursement.

b. Rules of Administrative Convenience

The exemption for *de minimis* fringe benefits found in § 132(a)(4) provides a good example of tax rules based on administrative convenience. Section 132(e) defines *de minimis* fringe benefits as “any property or service the value of which is . . . so small as to make accounting for it unreasonable or administratively impractical.”¹⁴⁴ Examples include use of the office copy machine, occasional holiday or birthday gifts of property, occasional cocktail parties, flowers, fruit, donuts, and soft drinks.¹⁴⁵ Except for very limited circumstances, cash and cash equivalents may not be excluded as *de minimis*.¹⁴⁶ Provisions like this clearly deviate from the accepted income definition, though they cannot be said to operate as subsidies. Instead, they reflect a judgment that the burdens of tracking such income and collecting taxes on it are just not worth it.

c. Normative Rules

Finally, a number of exemptions are normative, that is, they are deemed necessary to measure income accurately. The exemption for “working condition” fringe benefits found in § 132(a)(3) falls into this category. Section 132(d) defines working condition fringes as benefits, the cost of which the taxpayer could have deducted had she incurred the expense directly. Expenses are deductible if they are ordinary and

¹⁴² See I.R.C. § 262(a) (2018); Rev. Rul. 99-7, 1999-1 C.B. 361.

¹⁴³ For a discussion of externalities and the market failure theory of tax subsidies, see Adam Chodorow, *Charity with Chinese Characteristics*, 30 UCLA PAC. BASIN L.J. 1, 23-27 (2012).

¹⁴⁴ I.R.C. § 132(e) (2018).

¹⁴⁵ Treas. Reg. § 1.132-6(e) (as amended in 1992).

¹⁴⁶ See Treas. Reg. § 1.132-6(c).

necessary for the production of income, whether in a trade or business or a profit seeking activity.¹⁴⁷ The reason for the exclusion is that the employee would have no income if she were to incur the deductible expense and then get an offsetting reimbursement. Accordingly, it makes little sense to tax the employee if the employer simply provides the benefit or covers the expense directly.¹⁴⁸ Hence the exclusion.

Another way to frame the question is to ask whether the good or service is compensatory in nature. Items provided to an employee so that she can do her job are intended to benefit the employer and not as compensation. Tying the exemption to the employee's ability to deduct the expense if incurred directly ensures that the benefit is work related and not compensatory. Such benefits are not income, and including them in the tax base would overstate an employee's compensation.

Tax theorists typically determine whether a tax provision is normative by reference to the Code's underlying income definition. The Code is silent on this matter, and scholars have advanced a number of different possibilities.¹⁴⁹ That said, the Haig-Simons-Schanz income definition dominates. Under this approach, income can be thought of as the sum of consumption plus change in wealth over an accounting period.¹⁵⁰ Take someone who earns \$100. She can consume it (spend it) or save it. If we add together the amounts consumed and saved, we should be able to derive her income. For instance, if someone were to spend \$10 at the movies and put \$90 in the bank, she will have consumed \$10, her wealth will have increased by \$90, and we can infer that she had \$100 of income.

The key to this approach is to determine what constitutes consumption. Personal spending, such as going to the movies, is considered consumption, while spending to generate income is not. Thus, assume that she starts with \$100 in her bank account and spends \$10 to go to the movies. She also spends \$15 in a business venture that yields \$50 of cash. We would determine her income using the Haig-Simons-Schanz approach as follows. She has \$10 of consumption, reflecting only the money spent on the movie. Her

¹⁴⁷ See I.R.C. §§ 162, 212 (2018).

¹⁴⁸ Under the statute, the employee should deduct the expense and include the reimbursement in income. See, e.g., I.R.C. § 62(a)(2)(A) (2018). The regulations permit employees simply to exclude the reimbursement if they do not deduct the expense, but one gets the same result. See Treas. Reg. § 1.62-2 (as amended in 2003).

¹⁴⁹ See, e.g., Andrews, *supra* note 140.

¹⁵⁰ See Deborah A. Geier, *The Myth of the Matching Principle as a Tax Value*, 15 AM. J. TAX POL'Y 17, 42 (1998). Some substitute "savings" for "change in wealth." *Id.*

wealth started at \$100, was reduced by \$10 for the movie, reduced by another \$15 for the business spending, and then increased by \$50. The final balance in her account would be \$125, for a net increase of \$25. Her income over this period would thus be \$35.

This approach can easily be mapped onto the real-world income tax. Gross income includes all revenues, with no deductions (§ 61). An act of consumption is a personal expense for which no deduction is allowed (§ 262). In contrast, business expenditures are not consumption and therefore may be deducted from gross income (§§ 162 and 212). Applying this approach to the example above, the taxpayer has \$50 of gross income. Of the \$25 she spent, \$15 was spent to generate income and may be deducted. The other \$10 is a personal expense and may not be deducted, leaving her with \$35 of income, the same answer as above.

This analysis can be used to explain the differing tax treatment of various fringe benefits. First imagine someone who earns \$10 and spends it at the theater. Using the Haig-Simons-Schanz income definition, she has \$10 of income, determined as \$10 of consumption and no change in wealth. Using the real-world tax regime, she has \$10 of gross income and no deductions. What happens if her employer reimburses her for the theater ticket? Under the Haig-Simons-Schanz approach, we can see that she has \$10 of consumption and an increase in wealth of \$10, for a total of \$20. In the real-world tax system, we get the same result by including the reimbursement in income. She will report \$20 of income, consisting of the \$10 she earned, denying her a deduction for the personal expense, and including the \$10 reimbursement.

Assume next that instead of spending the \$10 she earned at the theater, she spent the money for a business purpose. Using the Haig-Simons-Schanz approach she has no change of wealth and no consumption, and thus reports no income. Under the real-world approach, she would report \$10 of gross income and a \$10 deduction, yielding the same result. But what if she were reimbursed? Under the Haig-Simons-Schanz approach, she would report \$10 of income because she would have a \$10 increase in wealth. Under the real-world approach, she would include the \$10 she earned, deduct the \$10 expenditure, and then include the \$10 reimbursement in income, for a total of \$10 of income.

Finally, to tie this back into the discussion of fringe benefits, what happens if the employer provides the benefit directly to the employee instead of having the employee incur the expense and get reimbursed? If the item reflects personal consumption, such as the movie ticket in

the example above, the benefit must be included in income.¹⁵¹ This puts the taxpayer in the same position she would have been in had she purchased the ticket and been reimbursed. In contrast, if the item is not considered consumption, the benefit may be provided tax-free. Again, the employee ends up in the same position she would have been in had she incurred the expense directly and been reimbursed.

This framework will help us assess the various housing provisions found in the Tax Code and evaluate the claim that the parsonage exemption is part of a broad policy that is neutral towards religion, similar to the property tax exemptions at issue in *Walz* or § 501(c)(3).

3. Specific Housing Provisions

As a preliminary matter, housing, like commuting, is considered a personal expense, or consumption, for which no deduction is typically allowed.¹⁵² If provided by an employer as a fringe benefit, whether in-kind or as a cash allowance, its value must be included in income absent special provisions expressly excluding such amounts.¹⁵³ The Code contains five provisions that permit housing to be provided tax-free. I start with the generally applicable in-kind housing provision found in § 119 and then turn to the targeted provisions that allow for tax-free housing allowances, including §§ 911 (expatriates), 134 (military personnel), and 912 (government employees living abroad). I conclude with a discussion of § 107 and illustrate how it differs from these other provisions in fundamental ways that undermine the claim of a broad, neutral policy to allow tax-free housing.

a. In-Kind Housing — Code Section 119

The question of whether to include employer-provided housing in income arose shortly after Congress adopted the income tax. As noted above, the IRS issued a number of rulings in the early part of the twentieth century permitting seamen, hotel managers, and hospital

¹⁵¹ For purposes of this discussion, I am ignoring § 132(e), which allows certain *de minimis* benefits like theater tickets to be provided tax-free for administrative reasons. See I.R.C. § 132(e) (2018).

¹⁵² See I.R.C. § 262(a) (2018).

¹⁵³ See I.R.C. § 162(a)(2) (2018); *United States v. Correll*, 389 U.S. 299, 304-06 (1967). The tax treatment of permanent housing (nondeductible) differs from that of temporary housing while traveling away from home on business (deductible). See I.R.C. § 152(a)(2) (2018); *Correll*, 389 U.S. at 304-06. Addressing temporary housing is beyond the scope of this Article.

workers, among others, to exclude such housing from income.¹⁵⁴ In one case, involving government employees working for Indian Services, the IRS held that the tax consequences would depend on how the government accounted for the housing, that is, whether the employer deemed it to be compensatory.¹⁵⁵

Over time, these rulings found their way into the regulations,¹⁵⁶ where the inquiry focused on whether the lodging was compensatory or for the convenience of the employer — that is, provided so that the employee could do her job. Thus, from the very beginning, or at the very least soon thereafter, the rules for ministers differed from those for laypeople. Section 107 explicitly permitted compensatory housing to be excluded. The regulations did not cover what to do when both elements were present.¹⁵⁷ Eventually, the Treasury Department issued a notice stating that one should look first to see whether compensation was intended.¹⁵⁸ If so, then the benefits were taxable. If not, then one must determine whether they were provided for the benefit of the employer. If not, then the benefits were taxable. Thus, only if the housing were non-compensatory and for the convenience of the employer could the taxpayer exclude the value of such housing from income.

This approach led to significant litigation because it was often difficult to determine whether housing, especially off-site housing, was intended as compensation or was really for the convenience of the employer. Employers and employees both preferred the latter, and they could always cobble together some argument as to why the housing was for the employer's convenience.¹⁵⁹

¹⁵⁴ O.D. 265, 1 C.B. 71 (1919); T.D. 2992, 1920-2 C.B. 76; O.D. 915, 4 C.B. 85-86 (1921).

¹⁵⁵ 4 C.B. 85 (1921), 1921 WL 50800. If the Department of the Interior treated it as compensation, then the taxpayer had to include the value of the housing in income. If it did not, then the taxpayer could exclude it. *Id.*

¹⁵⁶ See, e.g., Treas. Reg. 118, § 39.22(a)-3 (1951). For a discussion of the history of § 119, see generally *Taxation — Exclusion Under Section 119 Granted Although Employee Was Charged for Value of Quarters Supplied*, 33 ST. JOHN'S L. REV. 408 (1959) (discussing *Boykin v. Comm'r*, 260 F.2d 249 (8th Cir. 1958)).

¹⁵⁷ See Revenue Act of 1921, Pub. L. No. 67-98, § 213(b)(11), 42 Stat. 227, 239 (1921).

¹⁵⁸ See Mimeograph 6472, 1950-1 C.B. 15.

¹⁵⁹ In many regards, this was similar to the problems the IRS faced with employer gifts to employees. Both the employer and employee had incentives to characterize compensation as excludible gifts, and they controlled the facts. To avoid fights, Congress enacted I.R.C. § 102(c), which provided that transfers from employers to employees could not be excluded as gifts. See I.R.C. § 102(c) (2018).

In 1954, the same year that Congress liberalized the rules regarding ministers, Congress codified the housing rules by adding § 119 to the Tax Code. The new provision limited the exclusion to situations where the housing was: (1) in-kind, (2) on-site, (3) required by the employer, and (4) for the employer's convenience.¹⁶⁰ It eliminated the formal inquiry into whether the benefit was intended to be compensatory, though that question is clearly implicit in the section's requirements, relying on bright-line rules rather than a more difficult inquiry into intent.

The early rulings along with the regulations and finally § 119 contain a common thread. The value of housing is excluded from income in cases where living at the jobsite is necessary to perform the job. Seamen cannot work on a boat and live elsewhere. Hospital workers on call cannot stay across town. Those working in a remote camp cannot live elsewhere. Hotel managers need to be on-site to handle any overnight emergencies. In these cases, accepting the housing is clearly for the convenience of the employer and necessary for the employee to do the job. Other examples might include lighthouse keepers, resident assistants, and dorm parents. While such employees might enjoy the housing and benefit financially from not having to maintain a separate home, they cannot perform their jobs unless they live on-site.

Tax theorists would frame this as an inquiry into whether employer-provided housing should be considered consumption. If it is consumption, it should be included in income. However, if it is not, it should be excluded. Henry Simons, of Haig-Simons-Schanz fame, addressed the problem by reference to a hypothetical flügeladjutant, an aide-de-camp, first discussed by Friedrich Kleinwächter.¹⁶¹ In contrast to a normal army officer, the flügeladjutant receives not only salary, but also housing in the palace.¹⁶² He must also attend opera and hunts with the prince as part of his job.¹⁶³ Simons further posits that he does not like opera or hunting.¹⁶⁴ Were the flügeladjutant to pay for these activities outside the work context, they would clearly be considered consumption. However, attending the opera and participating in hunts are part of his job. The analysis described above

¹⁶⁰ See I.R.C. § 119 (2018).

¹⁶¹ See HENRY CALVERT SIMONS, *PERSONAL INCOME TAXATION: THE DEFINITION OF INCOME AS A PROBLEM OF FISCAL POLICY* 53 (1938).

¹⁶² *Id.*

¹⁶³ *Id.*

¹⁶⁴ *Id.*

does not address what to do when a fringe benefit has this dual characteristic.

Not taxing the flügeladjutant raises equity concerns, but taxing him seems equally problematic. The answer cannot depend upon whether the flügeladjutant enjoys the opera or hunting or would have gone on his own. That is simply not administrable. Simons does not resolve the problem, except to suggest that it may be appropriate to exclude these kinds of dual-purpose benefits, either because they should not be considered consumption or because it is administratively too difficult to measure the consumptive elements.¹⁶⁵

The courts addressed a similar issue in *United States v. Gotcher*, which involved a taxpayer who was flown to Germany to inspect a Volkswagen plant as part of his job.¹⁶⁶ The IRS argued that the value of the flight was income to Mr. Gotcher, but the Court of Appeal held that it was motivated by Volkswagen's business purposes. Even though Mr. Gotcher benefitted from a trip that he might otherwise have taken, the court held that its value should not be included in his income. Instead it was provided as part of, and necessary to do, his job and therefore was properly excluded from income.

Housing presents an even more difficult question than other forced consumption, like travel, because employer-provided housing almost always displaces consumption, while other forced consumption may not.¹⁶⁷ The flügeladjutant might not go to the opera or hunting absent the job. The taxpayer in *Gotcher* might not have taken the trip to Germany. However, both would almost certainly have incurred housing expenses. Thus, a case could be made that all housing, regardless of whether it is work related, should be taxed. However, Congress has taken a different path and permitted it to be excluded under very limited circumstances.

One thing that distinguishes work-related benefits, including those in the examples above, from consumption is that they are forced. As Professor Ellen Aprill notes, there is a difference between consumption, which should be included in income, and "forced

¹⁶⁵ See *id.*

¹⁶⁶ *United States v. Gotcher*, 401 F.2d 118, 119-20 (5th Cir. 1968).

¹⁶⁷ The same can be said for meals. People will eat regardless of whether they have business, and all meals could therefore be considered a personal expense. The courts have at times considered whether the duplication of expenses should be necessary before deductions or exemptions are allowed. See, e.g., *Rosenspan v. United States*, 438 F.2d 905, 912 (2d Cir. 1971). This requirement could help justify deductions for travel while temporarily away from home, but such a rule has not been adopted. See John A. Lynch, Jr., *Travel Expense Deductions Under I.R.C. § 162(a)(2) — What Part of "Home" Don't You Understand*, 57 BAYLOR L. REV. 705, 707 (2005).

consumption,” which should not.¹⁶⁸ Forced consumption is not really consumption. The difficulty is that taxpayers and employers have every incentive to characterize consumption as forced, and it can be hard to figure out the truth. As a result, tax authorities have had to create administrative rules to address these questions.

For instance, many would not buy business suits but for work, and an argument could be made that such consumption is forced. The IRS has addressed the question of work clothing by holding that such expenditures are deductible only if no one would wear such clothing outside the work setting.¹⁶⁹ While many people would never wear business suits outside of work, others certainly do, for weddings and other formal occasions. Thus, business suits are not deductible (or excludible if employer-provided), regardless of what any one individual might do. In contrast, a McDonald’s uniform would be deductible if purchased directly and excludible if employer-provided.

The need for clear rules is even more urgent for housing, given the significant sums at stake and the fact that all employees need housing of one kind or another. It would be quite easy to manufacture a reason why someone needed to live near work, converting consumption into purported forced consumption. Thus, Congress imposed stringent requirements in § 119. To be excluded from income, housing must be: (1) in-kind, (2) on-site, (3) required by the employer, and (4) for the employer’s convenience.¹⁷⁰ Each of these elements is designed to ensure that housing is not intended as compensation but rather is required for the employee to do her job. Bright-line rules are often under and over inclusive, but they are relatively easy to administer. In this case, it will also be rarely met.¹⁷¹ In this regard, it differs

¹⁶⁸ See Aprill, *supra* note 56. Medical expenses are an example of forced consumption, and some have argued that they should be deductible in full as a result. See Andrews, *supra* note 140, at 317. Under current law, taxpayers may deduct medical expenses only to the extent they exceed 10% of Adjusted Gross Income. See I.R.C. § 213 (2018); see also Daniel Shaviro, *The Man Who Lost Too Much: Zarin v. Commissioner and the Measurement of Taxable Income*, 45 TAX L. REV. 215, 236-39 (1990) (arguing that Mr. Zarin’s compulsive gambling should be viewed as forced consumption and therefore not included in the tax base).

¹⁶⁹ See, e.g., Rev. Rul. 70-474, 1970-2 C.B. 35; Rev. Rul. 70-475, 1970-2 C.B. 35; Rev. Rul. 70-476, 1970-2 C.B. 35.

¹⁷⁰ See I.R.C. § 119 (2018).

¹⁷¹ Another example of an administrative rule can be found in § 119(d), which applies to housing provided by educational institutions. See I.R.C. § 119(d) (2018). The IRS determined that such housing did not typically meet the requirements of § 119(a), leading to numerous disputes about the value provided. Section 119 sets the maximum value provided at 5% of the appraised value or, if no appraisal exists, the fair market rental value of the housing. See *id.* Any rent paid would reduce the amount

significantly from the parsonage exemption, which permits housing to be provided tax-free to a minister “as part of his compensation,”¹⁷² that is, without any analysis as to whether it is work-related.

b. Provisions Allowing Tax-Free Cash Allowances

When an employer provides a cash allowance, it becomes far more difficult to claim that the benefit is being provided so that the employee can do her job. Nonetheless, in some limited circumstances, Congress permits cash allowances for housing to go untaxed. As illustrated below, such allowances serve different purposes and cannot properly be characterized as part of a broad, neutral policy, justifying tax-free allowances for ministers.

(1) Housing Provisions for Expatriates

Section 911 permits those who live overseas and have established a tax home there to exclude up to about \$100,000 of foreign-earned income from U.S. taxation, as well as certain housing benefits.¹⁷³ Receipt of these amounts clearly reflects an accession to wealth. However, as reflected in the legislative history, these amounts are excluded from income to allow those living abroad to avoid double taxation and the administrative burden of filing U.S. tax returns while living abroad.¹⁷⁴

One of the core concerns of the international tax regime is to ensure that those who reside in one country and earn income in another are not subject to double taxation.¹⁷⁵ This can be accomplished in a

subject to tax. See JOINT COMM. ON TAXATION, 99TH CONG., GENERAL EXPLANATION OF THE TAX REFORM ACT OF 1986, at 824-25 (Comm. Print 1987), <https://www.jct.gov/publications.html?func=startdown&rid=2355>.

¹⁷² I.R.C. § 107 (2018).

¹⁷³ *Foreign Earned Income Requirements*, I.R.S., <https://www.irs.gov/individuals/international-taxpayers/foreign-earned-income-exclusion-requirements> (last updated Apr. 8, 2016). The amount excludible is adjusted for inflation each year.

¹⁷⁴ These amounts are distinguishable from tax-free reimbursement for housing costs incurred while travelling away from home on business. See I.R.C. § 162(a)(3) (2018). To qualify for this exclusion, one must establish a home overseas and therefore cannot be said to be away from home.

¹⁷⁵ See *US Federal Tax Liability: Expat Tax USA*, EXPAT INFO DESK, <https://www.expatinfodesk.com/expat-guide/nationality-specific-information/americans/us-tax-liability> (last visited Sept. 19, 2017). The concern with double taxation is not always consistent. *Income Tax in the USA*, IMMIHELP, <https://www.immihelp.com/newcomer/income-tax-usa.html> (last visited Sept. 19, 2017) (noting that the federal government and most states tax income). However, states have largely worked out a system of apportionment and credits to ensure that different states do not tax the same income. Is

variety of ways. For instance, one could cede taxing authority to the source country, that is, where the income is earned (called territorial taxation), or to the country where the taxpayer resides (called residence taxation). The United States has opted for the latter and taken it one step further. Not only do we tax residents, but we also tax U.S. citizens living abroad on their worldwide income.¹⁷⁶ This creates the situation where both the United States and foreign countries attempt to tax the income of U.S. nationals living abroad.

To avoid situations where the United States and another country attempt to tax the same income, the United States has entered into a series of Double Tax Conventions that allocate taxing authority between the signatories.¹⁷⁷ However, countries can take unilateral steps to avoid double taxation. For instance, they can allow taxpayers to credit foreign taxes paid against their domestic tax obligations, as seen in the U.S.'s foreign tax credit regime.¹⁷⁸ They can also exempt foreign-earned income from domestic taxation. This is precisely what § 911 does.¹⁷⁹

Congress enacted the predecessor to § 911 in 1926, permitting individual citizens who were “bona fide non resident[s] of the United States for more than six months during the taxable year” to exclude all their foreign-earned income from U.S. taxation.¹⁸⁰ The stated justification was to increase our foreign trade by removing disadvantages faced by Americans working abroad.¹⁸¹ In particular,

Your Business Paying Taxes to the Correct Jurisdiction? Sourcing Can be Complicated, RSM, <http://rsmus.com/what-we-do/services/tax/state-and-local-tax/topics/apportionment.html> (last visited Sept. 19, 2017).

¹⁷⁶ This practice is quite rare and has been the subject of significant debate. See, e.g., Michael S. Kirsch, *Taxing Citizens in a Global Economy*, 82 N.Y.U. L. REV. 443, 512-13 (2007) (noting that any income earned while abroad is still subject to U.S. taxation); Bernard Schneider, *The End of Taxation Without End: A New Tax Regime for U.S. Expatriates*, 32 VA. L. REV. 1, 40-41 (2012) (noting foreign-earned assets exceeding a certain amount must be attached to U.S. tax returns).

¹⁷⁷ See, e.g., U.S. DEP'T OF THE TREASURY, UNITED STATES MODEL INCOME TAX CONVENTION (2016), <https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/Treaty-US%20Model-2016.pdf>.

¹⁷⁸ See, e.g., I.R.C. §§ 901-904 (2018).

¹⁷⁹ For an early history of § 911, see Note, *Section 911 of the Internal Revenue Code and the Foreign-Based Partner*, 74 YALE L.J. 956, 956-57 (1965).

¹⁸⁰ Revenue Act of 1926, ch. 27, §§ 209, 213(b)(14), 44 Stat. 9, 20, 26. Congress has amended the statute over the years to limit the exclusion and ensure that people are truly living overseas. See, e.g., Revenue Act of 1942, Pub. L. No. 77-753, § 160, 56 Stat. 798, 860; Revenue Act of 1951, Pub. L. No. 82-183, § 603, 65 Stat. 452, 562 (loosening the rules up somewhat); S. REP. NO. 77-1631, at 116 (1942) (extending the time one must spend abroad).

¹⁸¹ See S. REP. NO. 82-781, at 52-53 (1951), as reprinted in 1951 U.S.C.C.A.N. 1968,

foreigners living abroad only faced residence-based taxation, while U.S. citizens faced both foreign and U.S. taxes. In addition, living abroad was seen to be a hardship worthy of special tax breaks.¹⁸² While the Treasury Department lists the exclusion as a tax expenditure and there certainly are elements of subsidy,¹⁸³ the decision to exempt this income can also be viewed as a normative rule designed to ensure that foreign-earned income is taxed once.¹⁸⁴

In 1981, long after Congress amended the parsonage exemption to allow for tax-free cash allowances, Congress amended § 911 to exclude certain housing allowances from income as well.¹⁸⁵ As before, Congress suggested that doing so would promote foreign trade and that excluding housing allowances would ease the burden of living abroad.¹⁸⁶ However, it also effectively avoided a double taxation of such amounts. Regardless of whether the exemption is viewed as a subsidy or normative, it post-dates the housing allowance and its beneficiaries and justification differ significantly from the parsonage exemption's, significantly undercutting the notion that it is part of a broad, neutral policy.

(2) Government Employee Housing Provisions

Two additional provisions allow taxpayers to receive tax-free housing allowances. Section 134 does so for military employees; § 912 does so for government employees living abroad. These provisions predate the housing allowance for ministers, but they, too, cannot be viewed as part of a broad housing policy. Instead, they are terms of employment, quite distinct from the other housing provisions found in the Code.

2023-24; Note, *supra* note 179.

¹⁸² See Note, *supra* note 179.

¹⁸³ See TAX EXPENDITURES, *supra* note 2, at 29 (discussing exemption of foreign-earned incomes).

¹⁸⁴ The same analysis applies to the current debate about whether to abandon worldwide taxation in favor of a territorial system. While the switch to territorial taxation is promoted as a way to even the playing field for American companies and to increase their competitiveness, it is not generally seen as a subsidy to business, but rather as a way to implement a normative international tax regime.

¹⁸⁵ I.R.C. § 911(c) (2018); Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, §§ 102, 111, 95 Stat. 172, 186, 190. The limit is generally 30% of the income deduction, though it may vary. *Foreign Housing Exclusion or Deduction*, IRS, <https://www.irs.gov/individuals/international-taxpayers/foreign-housing-exclusion-or-deduction> (last updated Aug. 27, 2017).

¹⁸⁶ S. REP. NO. 97-144, at 36 (1981); H.R. REP. NO. 97-201, at 10-11 (1981).

Section 134 is best understood as part of a web of tax provisions that favor active military and veterans. For instance, § 112 excludes combat zone pay from income.¹⁸⁷ The Worker, Homeownership, and Business Assistance Act of 2009 contains specific provisions that permit former and current members of the military and other government employees additional time to take advantage of the First-Time Homebuyer tax credit and waive some of the recapture provisions.¹⁸⁸ Section 134 was added to the Code in 1986 and codifies the exemptions for any benefits that were excludible from income on September 9, 1986.¹⁸⁹

Tax-free housing allowances for military have a long history. In 1925, the Court of Claims held that allowances provided to military personnel for housing and sustenance were tax-free because they were more in the nature of reimbursement than salary.¹⁹⁰ Our understanding of income has evolved since then, such that reimbursement for non-deductible expenses would no longer be exempt from tax absent a specific statutory exception, but the exemption for housing allowances for military has survived.¹⁹¹

Clearly, military need to live on or near a base to do their jobs, and they must move wherever the government sends them. Those who must live on-site are engaged in forced consumption, and their housing would be excludible under § 119. Where insufficient on-site housing exists, military personnel must find their own housing nearby, and the military compensates them for the expense tax-free, thus equalizing the treatment of those who live on- and off-base.

On the surface, this looks like the 1954 decision to treat ministers who must find their own housing the same as those who must live in church-owned property. However, the courts have already addressed taxpayer efforts to analogize from the exclusion for military allowances to other taxpayers. For instance, in *Magness v. Commissioner*, state policemen sought to exclude their meal allowances from income under § 119 by reference to a purportedly

¹⁸⁷ I.R.C. § 112 (2018); I.R.C. § 134 (2018).

¹⁸⁸ *First-Time Homebuyer Credit: Members of the Military and Certain Other Federal Employees*, IRS, <https://www.irs.gov/newsroom/first-time-homebuyer-credit-members-of-the-military-and-certain-other-federal-employees> (last visited Jan. 22, 2017).

¹⁸⁹ I.R.C. § 134(b)(1)(B) (2018).

¹⁹⁰ *Jones v. United States*, 60 Ct. Cl. 552, 574 (1925).

¹⁹¹ See, e.g., I.R.S. Priv. Ltr. Rul. 5612265140A (Dec. 26, 1956) (affirming the exemption for military personnel and refusing to extend it to civilian contractors); Rev. Rul. 60-66, 1960-1 C.B. 21, 1960 WL 13009.

similar exclusion for military families. In rejecting the claim, the court stated:

Further, the *Jones* case presented the peculiar situation wherein the United States, with one hand, as an employer, gives money to its employees, and with the other hand, as a tax collector, takes it back; whereas a state is in the same position as any other employer so far as the federal income tax obligations of its employees are concerned.¹⁹²

In other words, tax benefits afforded federal government employees are different from provisions applicable to others because of the employment relationship.

The predecessor to § 912 was added to the Code in 1943¹⁹³ and is part of the international tax regime, like § 911. It applies to certain federal government employees working abroad and permits them to exclude certain housing allowances from income. The legislative history notes that these employees were forced to move overseas, much like military personnel were forced to live on or near military bases, and that their efforts were critical to the war effort.¹⁹⁴ The high cost of living damaged morale and effectiveness. The State Department did not have the funds to increase their salaries, and Congress decided to exempt living allowances from income as a means of increasing those employees' take home salaries.¹⁹⁵ The link between tax benefit and compensation could not be clearer.

¹⁹² *Magness v. Comm'r*, 247 F.2d 740, 744 (5th Cir. 1957).

¹⁹³ Revenue Act of 1943, Pub. L. No. 78-235, § 125(a), 58 Stat. 21, 21, 46 (1944) (expanding the exemption in the Foreign Service Act of 1946, Pub. L. No. 79-724, § 1051, 60 Stat. 999, 999, 1032).

¹⁹⁴ S. REP. NO. 78-627, at 24 (1944).

¹⁹⁵ The Senate report on this amendment reads in pertinent part as follows:

The Secretary of State has reported that at posts in the countries now associated with us in common war against the enemy and in those neutral states of supreme importance to us where the Foreign Service is performing a vitally important part in the Nation's war effort, the cost of living continues to mount higher and higher and the financial difficulties of our officers and employees grow progressively worse, threatening the efficiency and morale of this important group of personnel. The Department has neither the authority nor the funds to compensate such personnel for the extra burden which falls upon them by reason of the tax levied on cost of living allowances. The situation is acute and as the allowances are to meet official needs as distinguished from personal requirements, the exclusion of such allowances from tax consideration for this class of personnel is in the public interest.

c. *Code Section 107*

Section 107 has two distinct provisions, one permitting tax-free employer-provided housing and the other permitting tax-free cash allowances. Current efforts to challenge the parsonage exemption focus on the cash allowance because of standing issues. Nonetheless, future litigants may well establish standing to challenge in-kind housing. Accordingly, I discuss both.

(1) Section 107(1) — In-Kind Housing

As noted above, Congress tightened up the generally applicable rules governing tax-free housing in 1954 by adding § 119 to the Code. At the same time, Congress left § 107(1) unchanged. Section 119 is a normative rule that limits the exemption to forced consumption, while § 107(1) functions as a subsidy for ministers, at least to the extent that it is broader than § 119, because it exempts compensatory housing from income.

Nothing in § 107(1) conditions the provision of housing on the ability to do one's job. Indeed, the statute explicitly states that the housing may be provided as "compensation." Moreover, ministers may receive tax-free housing as part of their retirement packages,¹⁹⁶ completely undermining the notion that the housing is connected in any way to current job performance. In the parlance of Haig-Simons-Schanz, housing provided under § 107(1) can reflect pure consumption, which should be taxed, as opposed to forced consumption, which should not.

Some have argued that relaxing the rules for ministers in § 107(1) relative to § 119 should be viewed as a concession to the unique nature of working as a minister, whether because they often have people over to the house, are on call 24/7, or benefit from living in the community where they work.¹⁹⁷ In other words, they claim that ministerial housing really is work related and therefore properly excluded. However, nothing in § 107(1) requires ministers to use their houses for work, be available 24/7, or live in the community. Indeed, the statute explicitly states that they can receive their housing as compensation. Nor does anything in the legislative record support this claim.

S. REP. NO. 78-627, at 24 (1944).

¹⁹⁶ See TAX GUIDE, *supra* note 24, at 23.

¹⁹⁷ See Intervenor Defendants' Brief in Favor of Summary Judgment, *supra* note 8, at 30-33, 43-47.

Moreover, claims that ministers are categorically different from other employees such that they deserve less stringent rules cannot withstand scrutiny. If nothing else, ministers can work as teachers, administrators, and even basketball coaches, alongside laypeople performing the exact same jobs. If we allow such ministers to receive tax-free in-kind housing, while denying the same to laypeople, we are doing so because of their status as ministers and not because their jobs differ materially from other employees.

But what about those who lead congregations? Perhaps they differ from other employees and thus are entitled to looser rules. While some ministers may use their houses for prayer meetings and counseling, many do not. Moreover, many lay employees also work out of their homes. For instance, secular counselors and tutors regularly meet with clients at home. Corporate CEOs and law professors often have people over for a variety of work purposes. These employees are not permitted to receive off-site, tax-free housing. Rather, if they dedicate a portion of their homes to business use, they may be able to deduct the expenses associated with those dedicated portions.¹⁹⁸

Similarly, not all ministers are constantly on call. And even for those who are, it is not clear how often they are called upon in the middle of the night. Other professions are similar. For instance, medical personnel take call on a regular basis, but no one suggests that they should be able to receive off-site, tax-free housing, even if they must live near the hospital. Police and other emergency responders are also often subject to emergency calls, but they do not get tax-free housing. Moreover, the question is not whether someone might be on call, but rather whether it is necessary to live in specific housing for someone to do her job. Section 119 ensures that is the case. Section 107(1) does not.

Finally, the claim that churches benefit if ministers live in the same community in which they work is not sufficient to warrant tax-free housing. Many ministers do not live in the communities in which they work.¹⁹⁹ Moreover, many other types of businesses benefit if their employees live in the communities in which they work.²⁰⁰ Efforts to

¹⁹⁸ See generally *Business Use of Your Home*, IRS (2016), <https://www.irs.gov/pub/irs-pdf/p587.pdf>.

¹⁹⁹ See RICARDO MILLER, SR., *THE TRAVELING MINISTER'S HANDBOOK: KEYS TO DEVELOPING A SUCCESSFUL ITINERANT MINISTRY* (2011).

²⁰⁰ See William Craig, *5 Benefits of Hiring Locally*, FORBES (Sept. 13, 2016), <https://www.forbes.com/sites/williamcraig/2016/09/13/5-benefits-of-hiring-locally/#5bce8a564c1b>. For instance, real estate agents who live in the community are more likely to generate leads than those who live elsewhere. Jay Thompson, *10 Ways to*

characterize consumption as forced by first claiming that benefits accrue to the employer when employees live nearby and then by “requiring” employees to live nearby are precisely why Congress tightened up the rules in § 119. While ministers may be sympathetic and some benefits may flow to them from living nearby, they are not categorically different from other types of employees. Creating a special rule for ministers simply privileges them and undermines the notion of a broad, neutral housing policy that includes ministers.²⁰¹

Exemption proponents have raised a host of other arguments, including that: (1) every minister living on-site could satisfy the convenience of the employer requirement found in § 119,²⁰² (2) it is sometimes difficult to determine whether ministers are employees or self-employed,²⁰³ and (3) permitting in-kind housing to be tax-free avoids difficult valuation questions and liquidity problems.²⁰⁴

First, if every minister who lives on-site can satisfy the convenience of the employer rule in § 119, there is no need for a special rule for ministers. This argument only highlights the fact that § 107(1) expands the benefit beyond what is allowed for the general public, by expressly allowing compensatory housing and eliminating all requirements designed to ensure that the housing be inextricably linked to the employee’s ability to do her job.

Second, determining the employment status of ministers is not difficult. To avoid any issues, churches could explicitly hire their ministers. If employing ministers is anathema, tax authorities could deem them to be employees for purposes of § 119. Indeed, the exact opposite presumption is made for purposes of social security, where ministers are deemed to be self-employed and therefore subject to self-employment tax,²⁰⁵ regardless of their state law employment status.

Generate Real Estate Buyer Leads, ZILLOW (Mar. 9, 2015), <https://www.zillow.com/agent-resources/trends-and-data/tips-and-advice/generate-real-estate-buyer-leads>.

²⁰¹ In some cases, off-site property in which a minister was required to reside could be considered its own premises because significant church business is routinely conducted there. If the ministers were required to live on such premises and, living there, as opposed to simply working there, were necessary for the minister to do her job, then the minister could qualify under § 119.

²⁰² Dean T. Barham, *The Parsonage Exclusion Under the Endorsement Test: Last Gasp or Second Wind*, 13 VA. TAX. REV. 397, 418-20 (1993).

²⁰³ *Id.* at 419.

²⁰⁴ Zelinsky, *supra* note 10, at 104.

²⁰⁵ See *Publication 517 (2015), Social Security and Other Information for Members of the Clergy and Religious Workers*, IRS, <https://www.irs.gov/publications/p517/index.html> (last visited Jan. 22, 2017).

Finally, determining the value of in-kind housing is not difficult. Were a plumber to be compensated by being allowed to stay at a church-owned cabin, the same issues would arise. No one argues that such compensation should be tax-free. More important, ministers must already include the value of employer-provided housing for payroll tax purposes. Including the value of such housing for income tax purposes would not be difficult or administratively burdensome.²⁰⁶

(2) Section 107(2) — Cash Allowances

The argument that allowing ministers to receive tax-free cash allowances is part of a broad, neutral policy is even weaker than it is for in-kind housing. The only cash allowances allowed in 1954 were those for government employees, and, as explained above, those provisions should be viewed as part of the employment contract between the government and its employees. The exemption for expatriates came much later. The legislative history regarding this provision reveals that it was designed specifically to subsidize churches and ministers and to allow all ministers to get the same benefit, regardless of the form their housing took.²⁰⁷ Nothing in § 107(2) attempts to tie the housing to job performance. Most ministers can choose to live wherever they like. Housing allowances for ministers are no different from those received by corporate executives who move for work. They represent consumption, pure and simple, and they should be subjected to tax, just like the rest of a minister's compensation.

The legislative history for the 2002 amendment to § 107 attempts, after the fact, to paint the consumption as forced by noting that some churches assign ministers to specific posts, similar to the military and Foreign Service workers.²⁰⁸ As a factual matter, this is true for only a small number of hierarchical denominations. Most ministers interview for jobs and move if necessary, just like the rest of us. However, even

²⁰⁶ See *Warren v. Comm'r*, 302 F.3d 1012, 1013-14 (9th Cir. 2002).

²⁰⁷ One commentator has argued that the parsonage exemption has a secular purpose because it is designed to promote the wellbeing of society. Barham, *supra* note 202, at 410-12. Absent the tax, churches and ministers will have more money to do good deeds. *Id.* However, unlike § 501(c)(3), which covers all similarly situated non-profit organizations, § 107 is directed solely to religious actors, which is why it is constitutionally suspect. *Id.*

²⁰⁸ See Chemerinsky, *supra* note 7, at 708-09; see also Clergy Housing Allowance Clarification Act of 2002, Pub. L. No. 107-181, § 2(a), 116 Stat. 583, 583. In this regard, they are purportedly similar to the government workers covered by § 912. See S. REP. NO. 78-627, at 24; *supra* note 194 and accompanying text.

if all ministers were subject to assignment by their employers, it would be an odd and wildly under inclusive class of taxpayers eligible for this benefit, including only ministers, the military, and foreign service officers. Moreover, this claim appears nowhere in the earlier discussions of the exemption. Courts are typically loath to allow subsequent Congresses to provide evidence of an earlier Congress's intent.²⁰⁹

4. Conclusion

Supporters of the parsonage exemption claim that it does not pose Establishment Clause issues because it is part of a broad neutral policy that happens to include ministers, much like § 501(c)(3) covers charities, educational institutions, and churches. They further argue that the need for a special rule for ministers arises from the unique nature of ministerial duties. They cite no other example of a broad policy contained in myriad statutes. Nor do they cite to the legislative history, which undermines these claims. Comparing § 501(c)(3) to the various housing provisions found in the Code undercuts these claims as well. Section 501(c)(3) provides identical benefits to a class of organizations that provide public goods. Religious organizations fit naturally within that group. In contrast, §§ 107, 119, 911, 134 and 912 differ significantly from one another. They do not benefit a class of similarly situated taxpayers or offer the same benefits. They are also offered for different reasons. The notion that, when taken together, they constitute a broad, neutral policy is simply not supportable.

Another way to evaluate this claim is to consider what a real broad-based and coherent housing exemption might look like. For instance, to overcome the parsonage exemption's constitutional infirmities, Ellen Aprill proposed amending the parsonage exemption to allow tax-free housing for *all* who work at non-profit organizations and who are expected to meet with members, patients, or clients at all times, that is, on an emergency basis.²¹⁰ This would extend the benefit to all who were similarly situated, as does § 501(c)(3). Aprill claims that it would also tie the provision of tax-free housing to a business purpose, bringing it closer to the rationale that underlies the generally applicable § 119. As Aprill explains, "by requiring a purpose integrally related to the proper performance of the employee's duties — the so-

²⁰⁹ See, e.g., *Sullivan v. Finkelstein*, 496 U.S. 617, 628 n.8 (1990).

²¹⁰ Aprill, *supra* note 56, at 1243. The proposal covers in-kind housing and would permit a limited cash allowance that would phase out as salary increases. *Id.*

called ‘noncompensatory purpose,’ the emergency limitation gives a policy basis for the exclusion.”²¹¹

It is not clear that this proposal effectively ties the provision of housing to a business need. No connection exists between the obligation to see parishioners or clients and housing.²¹² Counselors must live somewhere and such housing does not become forced by simply asserting a connection with work.²¹³ Nonetheless, Aprill’s proposal can be seen as a subsidy that extends the same benefit to similarly situated taxpayers, thus making it look like § 501(c)(3) and bringing it within the holding of *Walz*. Comparing Aprill’s proposed rule to the parsonage exemption makes clear that the parsonage exemption is not part of a broad, neutral policy.

B. *The Parsonage Exemption Functions as a Subsidy*

Citing *Walz*, supporters further assert that the exemption does not raise Establishment Clause concerns even if it singles out religion because exemptions reflect the government’s decision to leave religion alone, not subsidize it.²¹⁴ In *Walz*, Chief Justice Burger stated that tax exemptions were different from direct subsidies because no money is extracted from taxpayers and transferred from the public treasury to churches.²¹⁵ More recently in *Arizona Christian School Tuition Organization v. Winn*, a narrow majority held that tax credits differed from direct spending for standing purposes in Establishment Clause cases.²¹⁶ However, in *Texas Monthly*, the Supreme Court found that a targeted tax exemption could indeed violate the Establishment Clause. As Justice Brennan noted, exempting something from taxation provides a benefit no less than sending a check.²¹⁷ Any other holding elevates form over substance and permits the government to subvert the First Amendment.

²¹¹ *Id.* at 1245.

²¹² This is to say nothing of the difficult task of determining who is truly on call or how often the obligation is invoked. The requirement that one live on-site acts as a filter of sorts.

²¹³ If being on call rendered off-site housing “forced,” doctors and emergency responders should get tax-free housing because they are often on call.

²¹⁴ See Legg, *supra* note 9, at 285.

²¹⁵ *Walz v. Tax Comm’r of N.Y.C.*, 397 U.S. 664, 690 (1970).

²¹⁶ *Ariz. Christian Sch. Tuition Org. v. Winn*, 563 U.S. 125, 126 (2011). The Winn Court only addressed standing and not whether credits should count as spending for merits purposes. *Id.*

²¹⁷ *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 14 (1989) (noting that a targeted exemption was equivalent to a direct subsidy).

Tax theorists have long understood that targeted tax breaks are equivalent to direct government spending. Stanley Surrey first championed this insight in the 1960s and 1970s,²¹⁸ and it has come to dominate tax policy thinking. The Congressional Research Service and the Treasury Department now produce annual “tax expenditure” reports showing how much spending Congress has buried in the Tax Code. The key to this analysis is to establish a normative baseline against which deviations can be measured. As described above in section III.A, “normative” in this context means necessary to measure income accurately, and therefore it necessarily incorporates an underlying theory of income. Provisions designed to promote specific activities, such as home ownership, are not normative and thus represent spending.²¹⁹

For instance, imagine that the tax rate is 50%, and the government decides to promote homeownership by providing homeowners \$100. It could send each homeowner a check for \$100, which would clearly be understood to be a subsidy. However, it could accomplish the same goal by hiding this spending in the Tax Code. For example, it could permit a \$200-dollar deduction, say of home mortgage interest, which would produce \$100 in tax savings. Or it could provide \$100 of tax credits. Finally, it could exempt \$200 of income from tax, which would produce the same result. Regardless of the form chosen, each homeowner will be \$100 richer, while the government will be \$100 poorer.

The government already acknowledges that the parsonage exemption is a subsidy for religious actors. In 2006, the Congressional Research Service classified § 107 as a tax expenditure, noting that “[t]he provision is inconsistent with economic principles of horizontal and vertical equity.”²²⁰ Moreover, “[m]inisters with higher incomes receive a greater tax subsidy than lower-income ministers because of their higher marginal tax rates.”²²¹ The Treasury Department stated in

²¹⁸ See, e.g., STANLEY SURREY, *PATHWAYS TO TAX REFORM, THE CONCEPT OF TAX EXPENDITURES*, at vii (1973).

²¹⁹ See, e.g., Leonard E. Burman, *Is the Tax Expenditure Concept Still Relevant?*, 56 NAT'L TAX J. 613, 613 (2003), http://webarchive.urban.org/UploadedPDF/410813_NTA_Tax_Expenditure.pdf. The concept of tax expenditures is not without its critics. In particular, one must determine the appropriate baseline, and the Tax Code does not formally establish one. *Id.* at 16.

²²⁰ STAFF OF S. COMM. ON THE BUDGET, 109TH CONG., *REP. ON TAX EXPENDITURES: COMPENDIUM OF BACKGROUND MATERIAL ON INDIVIDUAL PROVISIONS 352* (Comm. Print 2006), <https://www.gpo.gov/fdsys/pkg/CPRT-109SPRT31188/html/CPRT-109SPRT31188.htm>.

²²¹ *Id.*

its 2017 Tax Expenditure Budget that “[d]edicated payments and in-kind benefits represent accretions to wealth that do not differ materially from cash wages.”²²² It estimated that the exemption cost \$9.3 billion in forgone revenues over a ten-year period.²²³

Some have argued that courts should not treat targeted tax breaks the same as indirect spending for Establishment Clause purposes because to do so would “constitutionalize” economic theory.²²⁴ However, failure to do so requires a willful disregard of economic reality. It also ignores Congressional practice. For instance, in 2009, the IRS issued two notices, the first of which explained how to apply for \$250 million in tax credits for delivering a coal gasification plant,²²⁵ the second announcing \$1.25 billion in tax credits for certain advanced coal facilities.²²⁶ Congress is clearly buying energy infrastructure with tax credits instead of cash, and it would be foolish for the Supreme Court to hold otherwise.

If the Court were to ignore spending through the Tax Code for Establishment Clause purposes, Congress could subsidize religion with impunity. For instance, it would offer hundreds of millions of refundable tax credits to the Church of Unlimited Devotion or the Pastafarians²²⁷ without raising First Amendment concerns. Or it could exempt all Christians and Jews from income tax, while imposing those taxes on all others. Any approach that countenances such actions under the First Amendment is deeply flawed.

Justice Brennan’s position in *Texas Monthly* reflects the more sophisticated understanding that exemption is economically equivalent to imposing a tax and then returning the money.²²⁸ Indeed, the Court has routinely looked to economic reality in tax cases. For instance, it

²²² See TAX EXPENDITURES, *supra* note 2, at 12.

²²³ *Id.* at 23. The Joint Committee on Taxation also included the parsonage exemption in its compendium of tax expenditures, estimating a \$4 billion cost over the next five years. *Id.* at 23.

²²⁴ See, e.g., Linda Sugin, *Tax Expenditure Analysis and Constitutional Decisions*, 50 HASTINGS L.J. 407, 418 (1999); Edward A. Zelinsky, *Winn and the Inadvisability of Constitutionalizing Tax Expenditure Analysis*, 121 YALE L.J. ONLINE 25 (2011), <http://yalelawjournal.org/forum/winn-and-the-inadvisability-of-constitutionalizing-tax-expenditure-analysis>.

²²⁵ I.R.S. Notice 2009-23, 2009-1 C.B. 802. For an in-depth discussion of how Congress spends through the Tax Code and the difficulties such spending creates, see Edward D. Kleinbard, *The Congress Within the Congress: How Tax Expenditures Distort Our Budget and Political Processes*, 30 N. OHIO U. L. REV. 1, 1, 3-4, 7 (2010).

²²⁶ I.R.S. Notice 2009-24, 2009-1 C.B. 817.

²²⁷ See Rev. Rul. 62-212, 1962-2 C.B. 41; Keele, *supra* note 53, at 94.

²²⁸ *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 14 (1989).

has reconstructed cash flows to determine the true economic impact of transfers.²²⁹ It has also developed the economic substance doctrine to deny tax benefits where transactions technically comply with the laws but lack economic substance.²³⁰ In other words, in tax matters, the Supreme Court routinely looks to the economic substance of an action, as opposed to its form. It is not clear why the Court should ignore economic reality in this context. Indeed, the Bible itself admonishes that those who know the right thing to do should do it.²³¹

Finally, we turn to the claim that exemptions differ from credits and deductions because exemption reflects the government's decision to leave religion alone.²³² While this argument might make sense in some contexts, it makes little sense here. Churches must already report the incomes of their employees, including ministers, to the government, and ministers must pay taxes on their non-housing income. And they already pay payroll taxes on their housing benefits. Excluding a portion of ministerial income from the income tax does not amount to leaving ministers and churches alone. Instead, in this context, exemption simply provides ministers a special benefit unavailable to others.²³³

IV. EXEMPTING MINISTERIAL HOUSING FROM THE INCOME TAX IS NOT AN APPROPRIATE ACCOMMODATION UNDER THE FREE EXERCISE CLAUSE

Assuming, *arguendo*, that the parsonage exemption raises Establishment Clause concerns, supporters argue that it is nonetheless permissible under the Free Exercise Clause as an accommodation for

²²⁹ See, e.g., *Old Colony Tr. Co. v. Comm'r*, 279 U.S. 716, 729 (1929) (holding that a payment from an employer directly to the IRS on behalf of an employee should be understood to consist first of a transfer to the employee and then to the IRS).

²³⁰ See, e.g., *Gregory v. Helvering*, 293 U.S. 465, 470 (1935). This doctrine is now codified in I.R.C. § 7701(o) (2018).

²³¹ *James* 4:17 (English Standard Version) (“So whoever knows the right thing to do and fails to do it, for him it is sin.”). Socrates is also reputed to have said “to know the good is to do it.” This quote does not appear in Plato, but the idea appears at various places in the dialogues. See, e.g., PLATO, *GORGIAS* 509e (380 BC) (“[N]o one does wrong of his own wish, but that all who do wrong do it against their will.”).

²³² Douglas Laycock, *Towards a General Theory of the Religion Clauses: The Case of Church Labor Relations and the Right to Church Autonomy*, 81 COLUM. L. REV. 1373, 1416 (1981).

²³³ One commentator has argued that tax exemption cannot be a subsidy for non-income producing entities, like churches, because it affords them little benefit. See Legg, *supra* note 9, at 285. However, the exemption here applies to ministers, not to the churches themselves. Exempting a portion of ministerial income from taxes lowers costs for churches and thereby offers significant benefits.

religion. Some claim that it is necessary to avoid church-state entanglement. Others argue that the cash allowance provision is necessary to put ministers on equal footing with other ministers, thus avoiding discrimination among religions with different housing practices. Still others argue by analogy, pointing to other accommodations found in the Tax Code and elsewhere to argue that the parsonage exemption is permissible. In this Part, I consider these claims with reference to both the analytic tools tax theorists use and the way the parsonage exemption has been implemented.

A. *Section 107 Leads to More Church-State Entanglement, Not Less*

A number of commentators suggest that exempting ministerial housing from the income tax is necessary, or at the very least permissible, under the First Amendment's Free Exercise Clause to avoid church-state entanglement.²³⁴ To the extent that some interaction between church and state is inevitable, some argue that the courts should defer to Congress in deciding the nature and amount of such interactions.²³⁵ As described more fully below, this argument has it exactly backward. Subjecting ministers to the generally applicable rule of § 119 would entail far less entanglement than currently arises under § 107. In addition, deferring to Congress in such a clear-cut case as this would be an abdication of the Courts' responsibility to protect important constitutional rights and enforce limitations on government power.

Just what the Supreme Court means by entanglement is not entirely clear.²³⁶ Like the general test, the appropriate definition appears to depend on the context. *Walz* dealt with a tax exemption for religious actors and is therefore likely to provide the best guidance here. The concern in *Walz* was that the government might have to impose liens or levies on churches or even foreclose on them if they failed to pay property taxes.²³⁷ Supporters of the parsonage exemption appear to be making similar claims here, arguing that subjecting ministers to tax on their housing — as opposed to their regular salary — would subject

²³⁴ See, e.g., Butterfield et al., *supra* note 8; Zelinsky, *supra* note 10, at 1657-59, 1677.

²³⁵ See, e.g., Zelinsky, *supra* note 10, at 1669, 1677 (stating that it is constitutional to “permit (but not require) Congress to pick” between trade-offs of enforcement and eligibility entanglements).

²³⁶ For a detailed discussion of the entanglement prong, see Stephen M. Feldman, *Divided We Fall: Religion, Politics, and the Lemon Entanglement Prong*, 7 FIRST AMEND. L. REV. 253, 257-58 (2009).

²³⁷ *Walz v. Tax Comm'n of N.Y.C.*, 397 U.S. 664, 674 (1970).

them and their churches “to the inherently intrusive relationship between the tax collector and the taxpayer.”²³⁸ They also argue that the government would have to evaluate religious doctrine were it to apply § 119 to ministers.²³⁹

However, applying § 119 to ministers would not lead to the type of entanglement the Court was concerned about in *Walz*. Declaring the parsonage exemption unconstitutional simply requires churches to report *all* the compensation they pay to ministers. Churches must currently report the value of ministerial housing for payroll tax purposes. It is not at all clear why making churches report all compensation for both payroll *and* income tax purposes would be more entangling.

Another way to approach this question is to consider whether applying § 119 to ministers would create greater entanglement than § 107.²⁴⁰ If not, § 107 can hardly be said to be an accommodation designed to reduce entanglement. Supporters argue that § 107 reduces entanglement, but even a cursory review of how it operates demonstrates the opposite to be true.

As described above in subpart I.B, § 107 requires the government to inquire into a number of religious doctrines and practices. For instance, the government must decide what qualifies as a legitimate religion. While this is easy for established religions, it is more difficult for new ones, like the Pastafarians or the Church of Unlimited Devotion, with less mainstream beliefs. Most religions have at their core non-verifiable beliefs that seem fantastical to non-believers. Is it simply the sincerity of believers that matters, and, if so, how does one determine sincerity? Or are some beliefs simply beyond the pale? Determining which beliefs or purported beliefs should count as a religion for tax purposes is clearly entangling.

The government must also determine who qualifies as a minister. For established churches with clear ordination rules, this is straightforward. But what about churches with no clear ordination process or independent ministers with no established church behind

²³⁸ Zelinsky, *supra* note 10, at 1635.

²³⁹ See Butterfield et al., *supra* note 8, at 263-68.

²⁴⁰ See Zelinsky, *supra* note 10, at 1636; see also 4 RELIGIOUS ORGANIZATIONS AND THE LAW § 34:20 (citing Barham, *supra* note 207, at 414). Professor Zelinsky argues that the complaints about entanglement with regard to § 107 are more properly seen as complaints about the regulations. Zelinsky, *supra* note 10, at 1657. However, the source of the entanglement is irrelevant. The statute is not self-executing, and the regulations simply attempt to address the entanglement issues the statute necessarily creates.

them. How is the government to decide whether taxpayers qualify as ministers in those cases? And what about churches with different levels of ordination? The government has had to delve into Jewish religious doctrine and practices to determine whether cantors, in addition to rabbis, should qualify for the exemption. They do.²⁴¹ The only way to answer these questions is to delve into religious beliefs and practices.

For ministers who work outside a church, the government must decide whether the organization is an “integral agency” of the church²⁴² and, if not, whether the church made a bona fide assignment to its religious purposes.²⁴³ Regardless of where the minister works, the government must also determine whether ministers claiming the exemption are performing ministerial functions.²⁴⁴ Again, it is straightforward for those who lead congregations, but many ministers serve in other capacities, whether within a church or for affiliated entities or secular organizations. The IRS has already been called on to decide whether ministers working within church organizations as clerks and stenographers qualify as ministers for purposes of the exemption. They do not.²⁴⁵ However, the IRS has ruled that ministers working elsewhere as teachers, counselors, directors of business services and alumni relations, and as basketball coaches do qualify for the exemption.²⁴⁶

The IRS must also determine how much ministerial activity is necessary to qualify as a minister for § 107 purposes. Does an ordained minister working as a plumber count as a minister if she gives one sermon a year? How about ten sermons? What if she volunteers in a soup kitchen or counsels youth in an after school program? Does the amount of ministerial activity required vary based

²⁴¹ See, e.g., *Salkov v. Comm’r*, 46 T.C. 190 (1966) (determining that a Jewish cantor commissioned by recognized national body and installed by local congregation with power to perform certain religious functions qualified under § 107 even though he could not perform all functions of ordained rabbi); see also *Silverman v. Comm’r*, No. 72-1336, 1973 WL 2493, at *2 (8th Cir. 1973) (reaching the same conclusion, with extensive discussion of Judaism’s “dual ministry”).

²⁴² See Treas. Reg. § 1.1402(c)-5(b)(2).

²⁴³ See *Boyer v. Comm’r*, 69 T.C. 521, 532 (1977) (determining an assignment of a Methodist minister to teach at a state college was not bona fide for the purposes of § 107).

²⁴⁴ See sources cited *supra* note 62.

²⁴⁵ Rev. Rul. 57-129, 1957-1 C.B. 313 (stating that ministers involved in management are considered ministers; ministers acting as stenographers, mail clerks, and janitors are not).

²⁴⁶ See *Reed v. Comm’r*, 82 T.C. 208, 212-13 (1984).

on the nature of the activity? The regulations are silent on this question, and one can easily imagine churches and ministers altering their behavior to structure job duties so that ministers could qualify for the exemption.

After determining the quantum of ministerial work necessary, the government must also ensure that ministers actually perform that work. In sum, § 107 requires the government to investigate and oversee both churches and ministers,²⁴⁷ delving into both doctrine and actual practice.²⁴⁸ This is precisely the type of interference the Court was concerned with in *Walz*.

In contrast, if § 119 were to apply to ministers, tax authorities could avoid most of these inquiries. As a preliminary matter, 87% of ministers currently receive cash allowances and would not be eligible for the exemption.²⁴⁹ Thus, applying § 119 to ministers would immediately reduce the number of potentially eligible ministers, significantly reducing church-state interactions. Ministers who do not qualify for an exemption would simply include the full value of their compensation in income, as they already do for payroll tax purposes.

For those receiving in-kind housing, tax authorities would have to determine whether the minister were an employee and whether the housing were: (1) on-site, (2) required by the employer, and (3) for the employer's convenience. As noted above, whether a minister is an employee is easy to determine, and Congress could simply deem ministers to be employees for § 119 purposes, just as they deemed them not to be for payroll tax purposes.²⁵⁰ Whether the employer requires the minister to accept the housing as a condition of employment is a factual question solved by looking at the employment agreement or talking to the parties.

The only inquiries that would arguably be entangling would be whether the housing was on-site and whether it was really offered for the employer's convenience. It should be relatively easy to determine whether housing is on- or off-site. In some cases, off-site housing could be considered a work site in-and-of-itself. For instance, an off-site residence might host enough business activity to count as a premises. In those rare occasions, inquiries would focus on the work-

²⁴⁷ See Groff & Carrillo, *supra* note 69.

²⁴⁸ See, e.g., Grassley Letter, *supra* note 87 (requesting explicit information about the operation of Without Walls International Church in order to determine whether the ministers were actually performing ministerial work).

²⁴⁹ See Zylstra, *supra* note 23. Of the remaining 13%, it is not clear how many live on-site. But, certainly some number would be disqualified by that requirement.

²⁵⁰ See TAX EXPENDITURES, *supra* note 2, at 15-16.

functions performed at the residence and not on religious doctrine. This inquiry is similar to determining whether taxpayers may deduct business expenses associated with using a residence for business purposes.

Deciding whether housing is for the benefit of the employer depends on the minister's duties, just as with any lay employee. Does the minister act as a caretaker for the church? Must she be available on the premises overnight for church business? If not, then the housing is not for the employer's convenience. Recall that the goal is not to eliminate church-state interactions. That is not possible. The goal is to minimize such interactions. These inquiries are far less intrusive than those required under § 107.

Zelinsky argues that the "church-state entanglement inherent in taxing noncash income is particularly acute in light of the valuation and liquidity problems of taxing such income."²⁵¹ However, valuation issues are no different in the religious context from those that arise in a secular one.²⁵² Were churches to pay other employees in noncash income, they would have to report the value of such income to the IRS. More important, housing benefits are already included in the tax base for payroll tax purposes.²⁵³ The valuation and liquidity concerns that would support exempting the value of employer-provided housing from income tax would apply equally to the payroll tax, and yet no one has raised it.

Finally, picking up on *Walz*, Zelinsky notes that entanglement is unavoidable, arising either by applying the general tax law to ministers or policing the boundaries of an exemption specifically tailored for them.²⁵⁴ In light of this, he seems to suggest that courts should defer to Congress's judgment.²⁵⁵ While deference might make sense where the level of entanglement for each option was essentially the same, here the claim is that § 107 is an accommodation to avoid the entanglement of § 119. However, the facts clearly demonstrate that

²⁵¹ Zelinsky, *supra* note 10, at 1636.

²⁵² Professor Zelinsky notes that churches might need to withhold taxes associated with such housing. *See* Zelinsky, *supra* note 10, at 1658. But § 3401(a)(9) excuses churches from this obligation. I.R.C. § 3401(a)(9) (2018). Taxing all minister compensation, including employer-provided housing, would not change that.

²⁵³ I.R.C. § 1402(a)(2) (2018). Interestingly, when a church objects to paying social security taxes because it violates religious tenets, such objection does not apply to its employees. Rather, those employees become subject to self-employment tax (assuming that they do not have their own religious objections). *See* I.R.C. § 3121(b)(8)(B) & (w) (2018); Zelinsky, *supra* note 10, at 1641-51.

²⁵⁴ *See* Zelinsky, *supra* note 10, at 1635, 1640-45.

²⁵⁵ *See id.* at 1636.

§ 107 increases entanglement. The courts routinely decide when Congress has stepped over a constitutional line, and, simply because no option avoids contact altogether, deference would eliminate the court's role in interpreting the Constitution, protecting rights, and limiting government power.²⁵⁶

B. The Parsonage Exemption Violates Core Tax Concerns About Horizontal and Vertical Equity

The Supreme Court in *Lemon* identified another form of entanglement, one that arises from government acts that create divisiveness along religious lines.²⁵⁷ Supporters of the parsonage exemption claim that § 107(2) helps avoid such divisiveness by putting ministers on equal footing with other taxpayers who are eligible for tax-free housing allowances²⁵⁸ and ensuring that that all ministers (and by extension religious organizations) are treated equally,²⁵⁹ regardless of the form their housing takes. The claim is that affording tax-free housing to some but not others is unfair and that § 107(2) is an appropriate accommodation because it avoids political fragmentation and divisiveness along religious lines.

Fairness, or equity, is a core tax concern, and the tools tax theorists use to assess tax provisions can be quite helpful in assessing these claims. Horizontal equity requires that similarly situated people be taxed similarly. Vertical equity acts as a corollary and requires that differently situated persons be taxed differently.²⁶⁰ Treating differently situated people the same can be as problematic as treating similarly situated people differently. The key question is whether ministers who satisfy § 119 are similarly situated to those who satisfy only § 107(1)

²⁵⁶ Eliminating the parsonage exemption might cause some churches to consider building a parsonage to try to come within the general rules of § 119, and that could arguably be viewed as a form of entanglement. However, churches already must comply with a host of general laws that shape their behavior, including tax laws. In fact, incentives to alter behavior already exist under § 107 because churches may assign the bare minimum of ministerial duties to ordained employees to bring them within the exemption.

²⁵⁷ See *Lemon v. Kurtzman*, 403 U.S. 602, 662-64 (1971) (identifying education as another form of entanglement with repercussions affecting religion).

²⁵⁸ See sources cited *supra* note 11.

²⁵⁹ See *supra* note 41; see also 4 RELIGIOUS ORGANIZATIONS AND THE LAW § 34:21 (“Simply put, different churches should not be treated differently simply because one already owns a parsonage and the other does not.” (citing Lark & Kennedy, *supra* note 11, at 191)).

²⁶⁰ For a discussion of vertical and horizontal equity, see Elkins, *supra* note 25, at 47-51.

or 107(2). Depending on the answer, different tax treatment may be warranted. As discussed more fully below, § 107 violates the norms of both horizontal and vertical equity, clearly undermining claims that fairness concerns justify the exemption.

1. Section 107 Leads to Disparate Treatment of Ministers and Laypeople

The first claim is that allowing ministers to receive tax-free cash housing and housing allowances is necessary to put ministers on the same footing as laypersons,²⁶¹ that is, to avoid discrimination against ministers. As demonstrated above in Part III, § 107(1) is far broader than § 119, providing ministers with a much greater ability to receive tax-free in-kind housing than is available to laypersons. Thus, § 107(1) does far more than simply level the playing field between ministers and others who receive in-kind housing. Section 107(2) fares no better. The vast majority of employees must pay taxes on cash housing allowances.²⁶² Thus, § 107(2) puts ministers in a better position than most other employees.²⁶³ Extending tax-free cash allowances to ministers violates the core norm of horizontal equity because it leads to disparate treatment of similarly situated ministers and lay employees.

A simple example illustrates this point. Imagine two teachers at a religiously affiliated school who teach the same subject in the same grade. The first is a minister, while the second is not. Each receives \$50,000 in compensation and pays \$10,000 for housing. However, § 107(2) permits the school to designate \$10,000 as a housing allowance for the minister. Economically, each has received \$50,000 in compensation. Under the principle of horizontal equity, they should be taxed the same. Section 107(2) violates that principle by allowing the minister to exclude \$10,000 of her income and report

²⁶¹ See sources cited *supra* note 11.

²⁶² The few employees entitled to exclude cash allowances for housing from income include expatriates, military, and government officials living abroad. These employees either live abroad, work for the government, or both, and the justifications for their exemptions do not apply to ministers. In other words, these employees differ from ministers, warranting different tax treatment.

²⁶³ Allowing ministers tax-free housing allowances arguably levels the playing field with the small number of employees who qualify for tax-free housing allowances under §§ 911, 912, and 134. However, the cost of doing so is to tilt the playing field in favor of ministers with the vast majority of employees. Moreover, those eligible under §§ 911, 912, and 134 either work for the government, live overseas, or both. Ministers are differently situated, and it is not at all clear why they should be treated the same.

only \$40,000. This unfairness is precisely what the Congressional Research Service had in mind when it stated that “[t]he provision is inconsistent with economic principles of horizontal and vertical equity”²⁶⁴ and should therefore be classified as a tax expenditure.²⁶⁵

2. Allowing All Ministers to Receive Tax-Free Housing Overlooks Important Differences Between Them

The second claim is that § 107(2) is necessary to ensure that all ministers (and by extension religious organizations) are treated equally, regardless of whether they receive on-site or off-site housing or cash allowances.²⁶⁶ Supporters argue that to do otherwise might stoke political fragmentation and divisiveness along religious lines²⁶⁷ based on different religious practices or would privilege rich churches over poor ones. These arguments founder for a variety of reasons.

First, efforts to equalize the tax treatment of those who receive in-kind housing and those who receive cash allowances assume that ministers in both situations are similarly situated. However, significant differences exist between those who satisfy § 119 and those who do not yet nonetheless receive tax-free in-kind housing or cash allowances.²⁶⁸ As explained above in section III.A, those who satisfy § 119 must accept housing on-site so that they can perform their jobs. Such housing should be excluded from the tax base because it is (1) not considered consumption, (2) forced consumption, or (3) administratively too difficult to determine what portion constitutes consumption. In contrast, those who receive housing or a cash

²⁶⁴ STAFF OF S. COMM. ON THE BUDGET, 109TH CONG., REP. TAX EXPENDITURES: COMPENDIUM OF BACKGROUND MATERIAL ON INDIVIDUAL PROVISIONS 329 (Comm. Print 2006).

²⁶⁵ This example also undermines the claim that ministers are categorically different from other employees and therefore entitled to a separate rule with looser standards.

²⁶⁶ See sources cited *supra* note 11; see also 4 RELIGIOUS ORGANIZATIONS AND THE LAW § 34:21 (“Simply put, different churches should not be treated differently simply because one already owns a parsonage and the other does not.” (citing Lark & Kennedy, *supra* note 11, at 191)).

²⁶⁷ See *Lemon v. Kurtzman*, 403 U.S. 602, 623 (1971).

²⁶⁸ Those who receive cash allowances to pay the costs of homes they own are also different from those who rent. Those who use the allowances to pay off their mortgages own an asset at the end of their employment, while renters own nothing. This difference certainly matters in other tax contexts. For instance, alimony used to pay a recipient spouse’s rent or mortgage is tax deductible for the payor. However, if the recipient spouse lives in a house owned by the payor and pays him rent, the amounts are not deductible as alimony. 26 C.F.R. § 1.71-1T(b)(Q-6)-(A-6) (2017).

allowance as compensation are being paid in the form of housing and should pay tax on the value received.

Treating differently situated people the same violates vertical equity and can be as unfair as treating similarly situated people differently. The problem here is that those who get in-kind housing and fail to satisfy § 119 should not receive such housing tax-free. The solution is not to “level up” by allowing all ministerial housing, including housing allowances, to be tax-free. Doing so allows ministers to bootstrap up from a bad policy to a worse one. Instead, the appropriate response is to level down, that is, to tax the housing for all ministers who fail to qualify under § 119. Doing otherwise treats all ministers the same despite important differences in compensation.

Second, it is not the government’s job to equalize church resources or to support those churches with limited resources. Arguments to the contrary simply highlight the fact that the exemption is not normative, but rather operates as a subsidy, at least for those who are offered the exemption without qualifying under § 119.²⁶⁹

Even if the exemption under § 119 were not normative, it does not follow that rich and poor churches should be treated equally. The Tax Code is replete with provisions that only wealthy employers use. For instance, larger and wealthier organizations, including churches, are far more likely to be able to provide tax-free health insurance,²⁷⁰ tax-favored pensions, and other tax-preferred compensation, such as 401(k)s, than smaller, less wealthy organizations. No one claims that churches that cannot satisfy the requirement for these provisions should nonetheless be allowed to provide tax-free compensation to their employees. It is not at all clear why the ability of some churches to provide tax-free housing is any different.

Finally, the claim that § 107 is an appropriate accommodation because it permits all religious organizations to be treated the same,

²⁶⁹ Professor Zelinsky argues that § 107 is normative because it is purportedly designed to accommodate religion and avoid entanglement. See Zelinsky, *supra* note 10, at 1636, 1655-57; see also Edward A. Zelinsky, *Dr. Warren, the Parsonage Exclusion, and the First Amendment*, 95 TAX NOTES 115, 117 (2002). This argument has two problems. First, “normative” in the context of the Tax Code refers to provisions designed to implement the underlying income definition the Tax Code embodies, that is, those provisions necessary to measure income accurately. Second, even if the parsonage exemption is not intended as a subsidy for religion — a contention belied by the legislative history — it acts like one. As the Supreme Court has repeatedly noted, laws may not have a principle or primary effect that advances or inhibits religion. See, e.g., *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 8-9 (1989).

²⁷⁰ See I.R.C. §§ 105-106 (2018) (giving tax-exemption to money spent on health insurance, which would be more feasible for a wealthier organization).

regardless of differences in doctrinal beliefs and practices, is belied by the way that section operates. Some religions ordain only men, while others treat all believers as ordained. Some sponsor schools that qualify as “integral agencies,” while others do not. These differences in religious beliefs and practices allow some churches to extend tax-free housing only to men, while others can extend them to all believers, so long as they are performing ministerial functions, which the IRS has construed to include basketball coaches, teachers, and administrators.²⁷¹ If we were to take seriously the notion that differences in doctrine and practice should not matter, the only practical way to do so would be to tax all housing offered to ministers, even if it satisfies § 119.

C. The Parsonage Exemption Differs from Other Exemptions Afforded Religious Actors

Finally, Zelinsky and others have suggested that the exemptions found in FICA, the ACA, and elsewhere, provide constitutional cover for the parsonage exemption. Indeed, Zelinsky claims that invalidating the parsonage exemption could somehow cast those other exemptions into doubt.²⁷² The argument depends in part on the fact that the regulations under § 107 incorporate the regulations under § 1402, which apply to both FICA and the ACA.²⁷³ Those regulations define who qualifies as a minister and what counts as sacerdotal. The difficulty with these arguments is that the exemptions for FICA and the ACA are purportedly necessary to ensure that the government does not force people to take actions that violate their religious beliefs. No one argues that such concerns motivate the parsonage exemption.

Social Security and Medicare taxes are commonly referred to as payroll taxes because they are assessed on a taxpayer’s wages. Social Security taxes apply to the first \$118,000 earned, while Medicare taxes apply to all wage income.²⁷⁴ Typically, the employer pays half the tax,

²⁷¹ Returning for a moment to the entanglement argument, if § 119 is constitutionally suspect because some churches may change their behavior to qualify their ministers for an exemption, so are a host of other tax rules that churches take advantage of. Moreover, § 107 requires a far greater inquiry into religious doctrine and practice than § 119.

²⁷² See Zelinsky, *supra* note 10, at 1667-71.

²⁷³ I.R.C. § 5000A(d)(2) (2018).

²⁷⁴ SOC. SEC. ADMIN., FACT SHEET: 2016 SOCIAL SECURITY CHANGES 1 (2016), <https://www.ssa.gov/news/press/factsheets/colafacts2016.pdf>. For Social Security taxes, employers and employees each pay 6.2%, for a total of 12.4%. For Medicare taxes, employers and employees each pay 1.45%, for a total of 2.9%. *Id.* Thus, self-

and the employee pays the other half. What appears on payroll stubs and the year-end W-2 is the employee portion of the tax. By definition, self-employed people do not have an employer, and the Self-Employed Contributions Act imposes the full tax on such people, but it allows them to deduct half the tax against their income for income tax purposes,²⁷⁵ thus putting them in the same position as those with employers.

Certain religious traditions object to these taxes because they can be viewed as a form of gambling.²⁷⁶ To account for this and to avoid forcing people to violate their religious beliefs, Congress permits those who object to these taxes on religious grounds to opt out. Churches that object to FICA on religious grounds may opt out of paying and collecting the tax for all employees by filing the appropriate forms.²⁷⁷ All churches are automatically excused from paying and collecting such taxes for ministers, thus treating ministers as if they were self-employed.²⁷⁸ However, employees and ministers are then responsible for the full amounts of such taxes under the Self-Employment Contributions Act (“SECA”), unless they too object on religious grounds and have filed the appropriate paperwork.²⁷⁹

The ACA exemptions follow a similar pattern. As part of the ACA, the government requires all health insurance plans to cover contraceptives, which some find objectionable on religious grounds. To avoid forcing people to violate their religious beliefs, the ACA permits taxpayers with religious objections to opt out of contraceptive health coverage.²⁸⁰ In such cases, the government requires insurers to step in and provide the benefits themselves.²⁸¹

In contrast, the parsonage exemption is not based on a purported religious objection to paying income taxes on housing compensation. Ministers are already subject to the income tax, and churches must report their income to the IRS. They already include the value of housing and housing allowances for payroll tax purposes. Requiring

employment taxes are 15.3%, at least until the Social Security limit has been hit.

²⁷⁵ *Id.*

²⁷⁶ The Federal Unemployment Tax also falls into this category. See TAX GUIDE, *supra* note 24, at 22.

²⁷⁷ *Id.* at 21 (explaining that the appropriate form is Form 8274).

²⁷⁸ See *id.* Churches are also not required to withhold taxes for ministers, though they can enter into arrangements to do so. *Id.* at 22.

²⁷⁹ *Id.* at 23.

²⁸⁰ *Health Benefits & Coverage: Birth Control Benefits*, HEALTHCARE.GOV, <https://www.healthcare.gov/coverage/birth-control-benefits> (last visited Jan. 22, 2017).

²⁸¹ *Id.*

ministers to include *all* their income in the income tax base would not force anyone to violate a religious belief. Thus, the existence of these other exemptions, based on religious belief, does not bolster the case for the parsonage exemption. Nor would eliminating the parsonage exemption put these other exemptions at risk.

CONCLUSION

The parsonage exemption singles out religious actors for a special tax benefit, raising serious Establishment Clause issues. Nonetheless, some argue that the exemption passes constitutional muster because it is part of a broad, neutral policy that happens to include ministers. Others claim that tax exemptions should not be considered subsidies for Establishment Clause purposes. Accepting, *arguendo*, that the parsonage exemption raises Establishment Clause concerns, supporters further argue that the Free Exercise Clause permits Congress to exempt ministerial housing from income tax as an accommodation for religion, to reduce church-state entanglement, ensure equal treatment of all religions, and to protect other exemptions found elsewhere.

The Supreme Court's jurisprudence in this area is somewhat muddled, making it difficult to determine what test the Court will apply, let alone how its analysis will play out. However, regardless of the constitutional test used, the exemption is part of the Tax Code, and understanding how it and other housing provisions function within the Tax Code helps to establish the predicates on which the exemption should be judged.

As demonstrated above, the parsonage exemption differs from other housing provisions found in the Tax Code in both purpose and effect, undermining claims that it is part of a neutral, broad-based policy allowing for tax-free housing, similar to the exemption at issue in *Walz* or § 501(c)(3). Instead, the parsonage exemption looks far more like the targeted tax exemption the Supreme Court found unconstitutional in *Texas Monthly*. Moreover, disregarding tax exemptions for Establishment Clause purposes ignores economic reality and permits the government to subvert the First Amendment.

Nor is the parsonage exemption an appropriate accommodation for religion. The parsonage exemption significantly entangles government in religious questions and requires oversight in ways that the generally applicable rule in Code § 119 would not. The parsonage exemption also violates core tax principles of horizontal and vertical equity. The claim that a broad exemption, including cash allowances, is necessary to ensure that all ministers are treated the same overlooks real

differences in compensation between ministers. It also provides a subsidy to ministers not available to laypersons performing the same jobs. Finally, the tax exemptions for religious actors from the payroll taxes and under the ACA cannot provide the parsonage exemption cover because they are designed to ensure that churches and ministers need not violate their religious beliefs, while the parsonage exemption is not so designed.