

## **Appellate Court Upholds Housing Allowance for Ministers**

On March 15, 2019, in Gaylor v. Mnuchin the Seventh Circuit Court of Appeals upheld the constitutionality of the clergy housing allowance set forth in section 107(2) of the Internal Revenue Code (the “Code”). That section allows certain religious leaders to exempt church-approved housing allowances from their taxable income. Although section 107(2) refers to “ministers”, the IRS and courts long have interpreted that term to encompass religious leaders of any denomination, regardless of their title, who meet certain requirements. Thus, ministers, priests, pastors, rabbis, cantors, imams and other religious leaders are eligible for the housing allowance.

The decision by the three-judge panel was unanimous, thus putting at ease for the moment the concerns of thousands of ministers and other religious leaders.

### **Background**

The case was brought in 2016 by the Freedom From Religion Foundation (“FFRF”), an organization headquartered in Madison, Wisconsin, and by several of its executives. FFRF’s purposes, as stated in its bylaws, are to promote the constitutional principle of separation of state and church, and to educate the public on matters relating to nontheism.

To tee up a case that could challenge the constitutionality of the housing allowance, FFRF granted several of its executive employees cash housing allowances. The executives then filed amended federal income tax returns for 2011-13 claiming that the allowances did not constitute taxable income to them. In July 2015, the IRS initially disallowed the individual plaintiffs’ claim for 2012. The plaintiffs protested the disallowance, and after the IRS failed to respond to their claim within six months, their claim was effectively denied. The FFRF and its executives then filed a lawsuit in April 2016 in the Western District of Wisconsin, claiming that the clergy housing allowance violated the Establishment Clause of the First Amendment (“Congress shall make no law respecting an establishment of religion . . .”) because it rendered ministers’ allowances tax-free but not theirs. The named defendants were the then Secretary of the Treasury and the Commissioner of the IRS in their official capacities. (The FFRF had previously filed two other lawsuits challenging the housing allowance, but those cases were dismissed for procedural reasons.) Several ministers and churches located in Chicago subsequently intervened in the case as additional defendants. They were represented by The Becket Fund for Religious Liberty.

In an October 2017 decision, District Court Judge Barbara Crabb ruled section 107(2) unconstitutional because it is a unique benefit for ministers. (The plaintiffs had also challenged Code section 107(1), which allows churches to provide tax-free in-kind housing, often called a parsonage or manse, but Judge Crabb dismissed that claim during the course of the case because the plaintiffs had been provided cash allowances, not in-kind housing.)

### **Appeal**

The defendants appealed Judge Crabb’s decision to the Seventh Circuit, which covers Illinois, Indiana and Wisconsin. The Church Alliance filed an amicus brief in the appellate case urging

that court to reverse the district court decision and declare section 107(2) constitutional. More than 30 churches and other religious organizations joined the Church Alliance's brief.

At oral argument, Judge Brennan, who ultimately authored the panel's decision, asked both sides which test the court should apply in determining whether section 107(2) was constitutional, the Lemon test or the Town of Greece test.

The Lemon test refers to a 1971 Supreme Court case, Lemon v. Kurtzman, that involved state aid to parochial schools. The Supreme Court in that case articulated its test for determining whether a particular statute violates the Establishment Clause as follows: "First, the statute must have a secular legislative purpose; second, its principal or primary effect must be one that neither advances nor inhibits religion; ...finally, the statute must not foster "an excessive government entanglement with religion."

The Town of Greece test refers to Town of Greece v. Galloway, a 2014 Supreme Court decision that held opening prayers before town board meetings to be constitutional. In that case the Supreme Court indicated that the Establishment Clause must be interpreted "by reference to historical practices."

The Seventh Circuit's panel's decision on March 15 reversed the district court's decision and upheld the constitutionality of the housing allowance under both the Lemon and Town of Greece tests. In upholding section 107(2) under the Lemon test, the panel held that section 107(2) has a secular purpose in that it puts ministers on an equal footing with secular employees receiving similar benefits. Congress' intent, the panel said, was to "exempt employer-provided housing for employees with certain job-related housing requirements." This is a recognition that other provisions of the Code provide housing benefits for various types of employees, including military employees and employees living abroad. The panel also found section 107(2) to eliminate discrimination between ministers; that is, between those affiliated with churches that can provide in-kind housing benefits such as a parsonage that is tax-free to the minister under Code section 107(1) and those ministers affiliated with churches – perhaps new or less well-established churches – that cannot provide in-kind housing benefits. Finally, the panel indicated that the broad nature of the exemption in section 107(2) avoids "intrusive inquiries into how religious organizations use their facilities". A contrary result, the panel noted, could force congregations to change their religious activities.

The panel also upheld the statute under the Town of Greece historical significance test. The panel found that while the defendants had provided substantial evidence of a lengthy tradition of tax exemptions for religion, particularly for church-owned properties, the plaintiffs had offered "no evidence" that provisions like section 107(2) were historically viewed as an establishment of a religion. The district court had held that the cases involving property tax exemptions were inapplicable to section 107(2), which was an income tax exemption, not a property tax exemption. However, the panel thought this "too fine a distinction" and noted that before the passage of the 16th Amendment in 1913, which sanctioned the current federal income tax scheme, Congress "could not constitutionally tax housing provided to ministers as part of their income."

The panel undoubtedly analyzed the housing allowance under both tests because the viability of the Lemon test is an issue currently before the Supreme Court in a case involving a 40 foot cross-shaped war memorial situated on public land in Blandensburg, Maryland. Oral argument in that case occurred on February 27, and a decision is expected by the end of June.

### **What happens next?**

The plaintiffs could petition to have the case reheard by the Seventh Circuit *en banc*, which means that it would be reheard by all of the dozen or so active judges in the Seventh Circuit. However, under the applicable rules governing appellate procedure such rehearings are not “favored”.

Ultimately, the plaintiffs could petition the Supreme Court to hear the case, but such petitions are long shots particularly in the absence of a conflict among the federal courts of appeals. The Supreme Court receives thousands of such petitions annually, but grants fewer than 100 each year.

There is no guarantee that the housing allowance will not be challenged again, but for now it remains intact.