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NOTES

APPLYING A PUBLIC BENEFIT REQUIREMENT TO TAX-EXEMPT ORGANIZATIONS

*Bob Jones University v. United States*¹

On its face, section 501(c)(3) of the Internal Revenue Code² is simply a tax exemption, freeing certain organizations from the burdens of paying federal income tax. The result of this exemption, however, is equivalent to direct payments by the government to these institutions.³ The Internal Revenue Service (IRS) thus is in a position to regulate private conduct by determining which groups are exempt.

In *Bob Jones University v. United States*,⁴ the United States Supreme Court upheld the denial of tax exempt status to religious schools that practice racial discrimination.⁵ Although the decision will significantly affect religious schools, its potential impact is much broader, affecting every tax-exempt organization. By holding that section 501(c)(3) provides exemptions only to organizations that meet the common law definition of “charity,” the Court effectively determined that several hundred thousand organizations⁶ must

1. 103 S. Ct. 2017 (1983), *aff'g*, *Bob Jones Univ. v. United States*, 639 F.2d 147 (4th Cir. 1980) and *Goldsboro Christian Schools v. United States*, 644 F.2d 879 (4th Cir. 1981).

2. (1976). *See generally* Bittker & Rahdert, *The Exemption of Nonprofit Organizations from Federal Income Taxation*, 85 YALE L.J. 299 (1976).

3. *Regan v. Taxation with Representation*, 103 S. Ct. 1997, 2000 (1983). *But see* *Walz v. Tax Comm'n*, 397 U.S. 664, 690 (1970) (Brennan, J., concurring) (exemptions and subsidies are “qualitatively different”); Bittker & Rahdert, *supra* note 2, at 357-58 (exemptions only reflect “the application of established principles of income taxation to organizations . . . which do not seek profit”). A large and diverse group of organizations are exempt under § 501(c)(3). *See, e.g.*, Rev. Rul. 472, 1975-2 C.B. 208 (halfway house); Rev. Rul. 533, 1970-2 C.B. 112 (day-care center); Rev. Rul. 372, 1968-2 C.B. 205 (sports museum). *See generally* INTERNAL REVENUE SERVICE, DEP'T OF THE TREASURY, CUMULATIVE LIST OF ORGANIZATIONS (1983) (groups eligible to receive donations deductible under I.R.C. § 170(c) (1982)).

4. 103 S. Ct. 2017 (1983). The Court upheld the denial of tax-exempt status to two separate schools, *Bob Jones University* and *Goldsboro Christian Schools*.

5. *Id.* at 2029.

6. Benenson, *Tax Exemption Controversy*, 1982 EDITORIAL RESEARCH REP.

“demonstrably serve and be in harmony with the public interest” to retain their exempt status.⁷

The application of common law principles to section 501(c)(3) implies that the IRS may enforce important national policies by denying tax exemptions to nonconforming organizations. These policies include the elimination of racial discrimination in education, and the Court used language in *Bob Jones* that makes other forms of discrimination possible targets of IRS action. The first amendment and sincerely held religious beliefs notwithstanding, the Court also decided that religious organizations also must comply with important public policies to retain their exemptions.

Since 1965, the IRS has struggled to determine whether tax-exempt status should be denied to private, racially discriminatory schools.⁸ Following a 1970 preliminary injunction barring it from granting exemptions to such schools in Mississippi,⁹ the IRS reversed its policy and announced that it would deny tax benefits to racially discriminatory schools.¹⁰ The case challenging the Mississippi exemptions was decided on the merits in 1971. The resulting opinion approved of the new IRS policy and permanently enjoined the granting of exemptions to any school in Mississippi that practices racial discrimination in the admissions process.¹¹

Later, Revenue Ruling 71-447 established that “[a] private school that does not have a racially nondiscriminatory policy as to students does not qualify for exemption.”¹² Revenue Ruling 75-231 specifically applied 71-447 to church-operated schools.¹³ Proposed IRS procedures designed to enforce these rulings and the progress of cases through the federal appellate courts generated a great deal of controversy.¹⁴ In response, Congress postponed implemen-

211, 227.

7. 103 S. Ct. at 2029.

8. See Annot., 7 A.L.R. FED. 548, 552 (1971). The IRS suspended the granting of such exemptions for new applicants in 1965 and lifted the suspension in 1967. *Id.*

9. *Green v. Kennedy*, 309 F. Supp. 1127, 1140 (D.D.C.), *appeal dismissed sub nom. Cannon v. Green*, 398 U.S. 956 (1970).

10. IRS News Release (July 10, 1970), *reprinted in Bob Jones*, Petition for Certiorari, Joint App. at A235. The IRS not only stated that it would revoke tax exempt status, but also announced that gifts to such schools would not be deductible by the donor. *Id.*; see also I.R.C. § 170 (1982) (charitable contribution deduction).

11. *Green v. Connally*, 330 F. Supp. 1150 (D.D.C.), *aff'd per curiam sub nom. Coit v. Green*, 404 U.S. 997 (1971).

12. Rev. Rul. 447, 1971-2 C.B. 230. Suits were filed in 1976 to seek stricter IRS compliance with the *Green* injunction and Revenue Ruling 71-447. Note, *The Judicial Role in Attacking Racial Discrimination in Tax-Exempt Private Schools*, 93 HARV. L. REV. 378, 381-82 (1979). An injunction ordering stricter IRS enforcement followed. *Green v. Miller*, 45 A.F.T.R. 2d (P-H) 8-1566 (D.D.C. May 5, 1980); Laycock, *Tax Exemptions for Racially Discriminatory Religious Schools*, 60 TEX. L. REV. 259, 265 (1982).

13. Rev. Rul. 231, 1975-1 C.B. 158.

14. See *Tax Exempt Status of Private Schools: Hearings Before the Sub-*

tation of the proposed procedures in September, 1979.¹⁵ Two years later, the IRS changed its policy again, claiming that it lacked authority to deny exemptions to religious schools.¹⁶

One of the institutions in *Bob Jones, Goldsboro Christian Schools*, was incorporated in 1963 as a church-affiliated school and has always had an admissions policy that excludes blacks.¹⁷ After an IRS determination that Goldsboro did not meet the requirements of Revenue Rulings 71-447 and 75-231, the school paid a portion of its overdue taxes and filed for a refund.¹⁸ The IRS counterclaimed for the remaining overdue taxes. In *Goldsboro Christian Schools v. United States*,¹⁹ the District Court for the Eastern District of North Carolina held that racial discrimination in private schools violated an important federal policy.²⁰ Determining that neither the free exercise nor the establishment clause²¹ prohibits denial of section 501(c)(3) status to Goldsboro,²² the court held that federal tax benefits must be denied.²³

Bob Jones University (University), has operated with the goal of “unqual-

comm. on Oversight of the Comm. on Ways and Means on Proposed IRS Revenue Procedure Affecting Tax Exemption of Private Schools, 96th Cong., 1st Sess. (1979) [hereinafter cited as *Hearings*]; Benenson, *supra* note 6, at 215-16; Laycock, *supra* note 12, at 259-60; Note, *supra* note 12, at 382-84.

15. Treasury, Postal Service and General Government Appropriations Act, 1980, Pub. L. No. 96-74, §§ 103, 615, 93 Stat. 559, 562, 577 (1979); *see also* Note, *Bob Jones University v. United States*, *Survey of Developments in the Fourth Circuit*, 1981, 84 W. VA. L. REV. 705, 715-16 (1982).

16. 103 S. Ct. at 2025. The “IRS position” or similar words refer here to the IRS position at the trial court level that the exemptions should be denied. The changes in the IRS position reflected the views of the Reagan Administration. Laycock, *supra* note 12, at 259-60.

17. 103 S. Ct. at 2024. Goldsboro Christian Schools based its policy on its interpretation of the Bible. This interpretation holds that Caucasians, Hebrews, and Blacks (along with Orientals) each descended from a different son of Noah. Although cultural or biological mixing of the races is considered to be a violation of God’s will, the school apparently would not bar the admission of any racial group other than blacks. Petition for Certiorari at 40-44, 83, *Goldsboro Christian Schools v. United States*, No. 81-1 (U.S. 1983).

18. 103 S. Ct. at 2024. Denial of exempt status under § 501(c)(3) results in the loss of federal income tax exemption, exempt status under I.R.C. § 3121(b)(8)(B) (1982) (Federal Insurance Contribution Act) (FICA), and exempt status under *id.* § 3306(c)(8) (Federal Unemployment Tax Act) (FUTA). Thus, Goldsboro was required to pay overdue employee withholding, FICA, and FUTA taxes. *Bob Jones*, 103 S. Ct. at 2024. If an organization loses exempt status under § 501(c)(3), contributions to it are not deductible under I.R.C. § 170 (1982). *See Bob Jones Univ. v. Simon*, 416 U.S. 725, 728-30 (1974); note 10 *supra*.

19. 436 F. Supp. 1314 (E.D.N.C. 1977), *aff’d per curiam*, 644 F.2d 879 (1981), *aff’d*, 103 S. Ct. 2017 (1983).

20. 436 F. Supp. at 1318.

21. U.S. CONST. amend. I (“Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof. . .”).

22. 436 F. Supp. at 1319-20.

23. *Id.* at 1318.

ifiedly affirming and teaching the inspiration of the Bible."²⁴ About 5,000 students are enrolled in courses ranging from kindergarten through graduate school.²⁵ The University has used the courts in a determined, but unsuccessful attempt to retain federal tax and other benefits. In 1970, the IRS notified the University that it would challenge the University's tax-exempt status.²⁶ In *Bob Jones University v. Simon*,²⁷ the University's attempt to enjoin the IRS from revoking its tax-exempt status was denied by the Supreme Court without reaching the merits.²⁸ The Court held that no injunction could issue until a determination of tax liability was made.²⁹ This decision permitted the University to judicially challenge its loss of exempt status only after receiving an unfavorable IRS ruling.³⁰

In an apparent attempt to retain exempt status while minimizing the harm to its beliefs and policies,³¹ the University began to liberalize its admissions practices. In 1971, married blacks became eligible for admission.³² Two years later, unmarried black employees of the University with four years of service became eligible.³³ Finally, in 1975, the University opened its doors completely to students of all races, but it retained its stringent policy against

24. *Bob Jones Univ. v. United States*, 468 F. Supp. 890, 893 (D.S.C. 1980) (quoting University Certificate of Incorporation), *rev'd*, 639 F.2d 147 (4th Cir. 1980), *aff'd*, 103 S. Ct. 2017 (1983).

25. 469 F. Supp. at 894.

26. *Id.* at 892-93.

27. 416 U.S. 725 (1974).

28. *Id.* at 749.

29. *Id.* The holding was based on the Anti-Injunction Act, I.R.C. § 7421(a) (1982), which prohibits suits to restrain the assessment or collection of taxes before the IRS determines that liability exists. *But cf. id.* § 7428(a)(1)(A) (1982) (1976 Tax Reform Act amendment allowing declaratory judgments of § 501(c)(3) and § 170(c)(2) status). As a general rule, once administrative appeal procedures are exhausted, the taxpayer can challenge a tax assessment by: (1) filing suit in the Tax Court without paying the tax, I.R.C. § 6213(a) (1982); (2) paying the tax and filing suit in federal district court, *id.* § 7422(a) (1982); 28 U.S.C. § 1346(a)(1) (1982); or (3) paying the tax and filing suit in the Court of Claims, I.R.C. § 7422(a) (1982); 28 U.S.C. § 1346(a)(1) (1982). *See* A. KRAGEN & J. McNULTY, FEDERAL INCOME TAXATION 7 (2d ed. 1974). In a suit seeking a declaratory judgment under the 1976 Tax Reform Act, the same courts have jurisdiction, but the disputed taxes need not be paid. I.R.C. § 7428 (1982).

30. *See* text accompanying note 125 *infra* (criticism of current procedures for reviewing IRS rulings). The University suffered another judicial defeat when the Fourth Circuit upheld the Veteran's Administration position that the University's admissions policy precluded it from operating as a VA-approved institution. *Bob Jones Univ. v. Johnson*, 396 F. Supp. 597, 600-01, 608 (D.S.C. 1974) (applying the due process clause and Title VI of the Civil Rights Act of 1964, § 601, 42 U.S.C. § 2000d (1976)), *aff'd mem.*, 529 F.2d 514 (4th Cir. 1975).

31. *See* Note, *Favorable Tax Treatment is Accorded a University Displaying Religiously Motivated Racial Discrimination*, 2 WHITTIER L. REV. 713, 728 (1980).

32. 103 S. Ct. at 2022-23. Married blacks presented less risk of interracial dating or marriage. *Bob Jones*, 468 F. Supp. at 894.

33. 103 S. Ct. at 2022 n.5.

interracial dating and marriage.³⁴

After the IRS determined that the University owed half a million dollars in unemployment taxes, the University paid twenty-one dollars of the disputed amount, and brought suit seeking a refund. The IRS filed a counterclaim for the unpaid taxes.³⁵ The South Carolina District Court held for the University, distinguishing *Goldsboro* on the basis that the University no longer followed a policy of discriminatory admissions.³⁶ The court also stated that: (1) no “clearly declared federal public policy against racial discrimination by religious organizations” exists;³⁷ (2) the IRS anti-discrimination rules applicable to educational organizations do not apply to a primarily religious organization such as Bob Jones University;³⁸ (3) the first amendment prohibits the denial of tax benefits to otherwise eligible religious organizations that discriminate racially;³⁹ and (4) the IRS exceeded its authority in adding to section 501(c)(3) a requirement that an organization provide a public benefit and conform to public policy.⁴⁰

A divided panel of the Fourth Circuit reversed, approving of the IRS Revenue Rulings.⁴¹ The same circuit subsequently affirmed *Goldsboro*.⁴² The Supreme Court granted certiorari, combined the cases for argument,⁴³ and af-

34. *Id.* at 2023. The final relaxation of the admissions rules was apparently prompted by at least three events. In April, 1975, the IRS had notified the University of the proposed revocation of its § 501(c)(3) status. *Id.* The previous year the Fourth Circuit had upheld the denial of VA educational benefits to University students. *See* note 30 *supra*. Perhaps most importantly, the Fourth Circuit had just determined that 42 U.S.C. § 1981 (1976) created a cause of action in favor of victims of discriminatory admissions policies of private schools. *McCrary v. Runyon*, 515 F.2d 1082, 1087 (4th Cir. 1975), *aff'd*, 427 U.S. 160 (1976); *see also* 103 S. Ct. at 2023 (revised University dating rules).

35. 103 S. Ct. at 2023. For nonprofit schools, the major tax benefits stemming from § 501(c)(3) are exemption from federal unemployment and social security taxes, as well as an increase in contributions resulting from the tax deductions allowed to donors. For federal tax purposes, gifts to the schools would not be taxable to the schools as income, so loss of § 501(c)(3) status would not normally result in income tax liability, *see* I.R.C. § 102 (1982) (excludes value of gifts received from gross income), even if “income,” broadly defined, exceeded expenses.

36. *Bob Jones*, 468 F. Supp. at 899.

37. *Id.* at 897.

38. *Id.*

39. *Id.* at 897-901.

40. *Id.* at 901-07.

41. *Bob Jones Univ. v. United States*, 639 F.2d 147 (4th Cir. 1980), *aff'd*, 103 S. Ct. 2017 (1983). The Fourth Circuit found that the IRS had not exceeded its authority or violated the first amendment in applying the regulation. 639 F.2d at 155.

42. 644 F.2d 879 (4th Cir 1981) (*per curiam*).

43. *See Bob Jones*, 103 S. Ct. at 2021; Laycock, *supra* note 12, at 261 & n.17. The change in the administration’s position not only raised a storm of protest, *N.Y. Times*, Jan. 19, 1982, at A27, col. 1, it left the denial of tax exemptions cause without an advocate. Consequently, the Supreme Court appointed an *amicus curiae* to defend the fourth circuit decisions. *Bob Jones*, No. 81-1 (U.S. April 19, 1982); Laycock, *supra* note 12, at 261 & n.18; *see also* *N.Y. Times*, Feb. 28, 1982, § IV, at 18, col. 1 (Rea-

firmed both, with Justice Powell concurring and Justice Rehnquist dissenting. The Court found that exempt organizations not only must fall within one of the categories of section 501(c)(3), but that they must also provide a public benefit and conform to public policy.⁴⁴ The public benefit and public policy requirements are derived from the common law of charities, which was shaped largely by the common law and English statutes concerning the meaning of charitable trusts.⁴⁵ "Public benefit" and "public policy" are two distinct concepts.⁴⁶ An organization can confer a public benefit even if some of its activities are against public policy; conversely, an organization may violate no public policy, yet offer no public benefit.⁴⁷ Treating the policy requirement as a corollary to the benefit requirement is the soundest approach.⁴⁸ Thus, an otherwise eligible organization should be considered charitable if it confers a net public benefit. Contravention of public policy is merely a factor in determining if a net benefit exists. This combination of the two concepts was expressed in the Supreme Court's determination that "[t]he institution's purpose must not be so at odds with the common community conscience as to undermine any

gan administration's retreats from IRS trial court position).

44. 103 S. Ct. at 2026-29. The exempt categories are for religious, scientific, literary, or educational organizations and organizations that provide testing for public safety, aid amateur athletics, or prevent cruelty to children or animals. I.R.C. § 501(c)(3) (1982). With the addition of the *Bob Jones* public benefit requirement, there are four types of activities: (1) charitable activities; (2) activities that are not charitable but not against public policy; (3) activities that violate an important public policy, but are not sufficiently evil to offset the benefits of the charitable activities; and (4) activities that are "so at odds with the common community conscience as to undermine any public benefit that might otherwise be conferred;" 103 S. Ct. at 2029. The second type of activity will result in the loss of exempt status only if it is substantial. *Better Business Bureau v. United States*, 326 U.S. 279, 283 (1945); *Stevens Bros. Found. v. Commissioner*, 324 F.2d 633, 638 (8th Cir. 1963), cert. denied, 376 U.S. 969 (1964); B. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* § 11.2 (4th ed. 1983). The fourth type of activity will result in a loss of exempt status whether substantial or not. See *Bob Jones*, 103 S. Ct. at 2036 (implies that any form of racial discrimination will cause loss of exemption). The effect of the third category was not decided by the Court. *Id.* at 2031 n.21.

45. See *Bob Jones*, 103 S. Ct. at 2026-28; M. CHESTERMAN, *CHARITIES, TRUSTS AND SOCIAL WELFARE* 6 (1979). See generally 4 A. SCOTT, *THE LAW OF TRUSTS* § 377 (3d ed. 1967).

46. Simon, *The Tax-Exempt Status of Racially Discriminatory Religious Schools*, 36 *TAX L. REV.* 477, 483-85 (1981). Simon has distinguished three theories in support of the IRS interpretation: public benefit, charitable trust, and public policy.

47. A school that provides unsafe playground equipment, for example, may be contravening public policy while it confers a substantial educational benefit to the public. Yet a religious organization, such as a convent isolated from public contact, provides no legally recognizable public benefit, while violating no public policy. See *Gilmour v. Coats*, 1949 A.C. 426 (gift to cloistered convent not deductible). The reasoning in *Gilmour* was that the nuns provided no tangible religious or other services. *Id.* at 446, questioned in M. CHESTERMAN, *supra* note 45, at 160-63.

48. 103 S. Ct. at 2028; see also Simon, *supra* note 46, at 485 (public benefit, public policy, and charitable trust theories "are all parts of a coherent analysis . . . [which supports] the same interpretation of the statute").

public benefit that might otherwise be conferred.”⁴⁹

Citing legislative history, the Court found that Congress did not intend for all organizations that are educational, religious, or within another 501(c)(3) category to be exempt, and that a public benefit requirement exists.⁵⁰ The Court also referred to the parallel wording of I.R.C. section 170(c).⁵¹ Section 170(c) defines charitable contributions and 501(c)(3) defines exempt organizations by using almost identical wording. The Court found this persuasive in reaching its conclusion that 501(c)(3) organizations must also be charitable.⁵²

The addition of the public benefit requirement to tax-exempt charities is not a novel idea. In *Commissioners of Income Tax v. Pemsel*,⁵³ the House of Lords held that “charitable purposes” had the same meaning in the income tax statutes as it had in the law of charitable trusts.⁵⁴ Although section 501(c)(3) does not define “charitable purposes,” the list of exempt organizations is analogous to the traditional list of charitable organizations.⁵⁵ “Charita-

49. 103 S. Ct. at 2029. The public policy requirement can be applied to the Code without regard to the law of charities. For example, granting deductions for fines incurred by a company violating state highway laws would support activity contrary to public policy and undermine state law enforcement. *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30, 34-36 (1958). Despite the absence of any specific authority, the IRS was held to have correctly disallowed the attempt to deduct the fines as business expenses. The *Bob Jones* Court avoided relying on *Tank Truck*, referring to it only in passing. 103 S. Ct. at 2028 n.17. Although *Tank Truck* was subsequently incorporated into the Code, I.R.C. § 162(f) (1982), Congress has expressed an intent to limit the doctrine to denying deductions under § 162 for fines, bribes, and antitrust treble damage awards. *Id.* § 162(c), (f), (g); S. REP. NO. 552, 91st Cong., 1st Sess. 274-75 (1969), reprinted in 1969-3 C.B. 423, 597.

50. 103 S. Ct. at 2028; see H.R. REP. NO. 1860, 75th Cong., 3d Sess. 19 (1938); 55 CONG. REC. 6728 (1917) (statement of Sen. Hollis).

51. (1982).

52. 103 S. Ct. at 2026. Section 170(c)(2) does not provide deductions for contributions to organizations that provide testing for public safety, but is otherwise similar to § 501(c)(3).

53. 1891 A.C. 531.

54. *Id.* at 583; M. CHESTERMAN, *supra* note 45, at 59-60. *But cf.* *Dingle v. Turner*, 1972 A.C. 601, 624 (no reason to apply charitable trust law concepts to tax law definition of “charity”). The English experience with the income tax was influential in shaping the 1894 income tax law. See 26 CONG. REC. 584-88 (1894) (information inserted by Rep. Bryan); *id.* at 6612-15 (information inserted by Rep. Hill).

55. See *International Reform Fed’n v. District Unemployment Compensation Bd.*, 131 F.2d 337, 339 (D.C. Cir.), *cert. denied*, 317 U.S. 693 (1942). State governments have often used terms found in the law of charities in providing for tax exemptions. Reiling, *Federal Taxation: What Is a Charitable Organization?*, 44 A.B.A. J. 525, 526 (1958); e.g., ARIZ. CONST. art. IX, § 2 (“Property of educational, charitable and religious associations . . . may be exempt from taxation by law.”); W. VA. CONST. art. X, § 1 (“[P]roperty used for educational, literary, scientific, religious or charitable purposes . . . may by law be exempted from taxation.”) The West Virginia provision was strictly construed to invalidate an exemption granted to commercial property held by a charitable trust. *Central Realty Co. v. Martin*, 126 W. Va. 915, 920, 30 S.E.2d 720, 723-26 (1944).

ble" is used as one category of 501(c)(3) organizations, and this would indicate that the public benefit requirement should apply only to that category of organizations.⁵⁶ The deviation from the literal words of section 501(c)(3) is, according to the Court, necessary to effect Congress's intent to apply the legal definition, and not the narrower lay definition, of "charity."⁵⁷

This departure from the literal language of the statute has subjected the IRS to strong criticism.⁵⁸ Use of the disjunctive "or" in section 501(c)(3) ordinarily means that "charitable" would not limit or define the terms "religious" or "educational."⁵⁹ Even if there is sufficient ambiguity in this section to justify a review of the legislative history, it is difficult to find persuasive evidence that Congress intended to impose a public benefit requirement.⁶⁰

Concepts developed under charitable trust law should not be uncritically applied to tax statutes.⁶¹ In *Walz v. Tax Commission*,⁶² the Court found that

One important effect of the *Bob Jones* decision is the adoption, by the Supreme Court, of the traditional definition of "charitable purposes." 103 S. Ct. at 2025-28.

56. See note 58 and accompanying text *infra*.

57. 103 S. Ct. at 2025-26; see also *Pfeiffer v. Commissioner*, 88 F.2d 3 (2d Cir.) (Hand, J., dissenting) (criticism of overly strict application of the "plain meaning" rule), *aff'd sub nom. Helvering v. Pfeiffer*, 302 U.S. 247 (1937); cf. *Reiling*, *supra* note 55, at 527 (section 501(c)(3) was intended to incorporate common law definition of "charity").

58. See, e.g., 103 S. Ct. at 2039 (Powell, J., concurring); *id.* at 2040-43 (Rehnquist, J., dissenting); Note, *The Internal Revenue Service's Revocation of the Tax Exempt Status of a Private Religious College Does Not Violate the First Amendment*, 50 U. CIN. L. REV. 615, 624-25 (1981); Note, *The Internal Revenue Service's Treatment of Religiously Motivated Racial Discrimination by Tax Exempt Organizations*, 54 NOTRE DAME LAW. 925, 930 (1979).

59. *Reitner v. Sonotone Corp.*, 442 U.S. 330, 339 (1978); see also *St. Martin Evangelical Lutheran Church v. South Dakota*, 451 U.S. 772, 791 (1981) (Stevens, J., concurring) (resort to legislative history is appropriate only when statute is ambiguous); *TVA v. Hill*, 437 U.S. 153, 184 n.29 (1978) (same); cf. *Kimberley School v. Town of Montclair*, 2 N.J. 28, 33-35, 65 A.2d 500, 502-03 (1949) (applying "plain meaning" rule to property tax exemption statute and holding that a nonprofit school is exempt whether or not it is charitable). Another basis for challenging the IRS interpretation can be derived from § 501(c)(3). The public benefit requirement consists of two parts: the organization must provide a benefit, and the beneficiaries must constitute a portion of the general public. M. CHESTERMAN, *supra* note 45, at 136. Since § 501(c)(3) includes the second limitation (in its prohibition on private benefit), and omits the first, the addition of the public benefit requirement seems inappropriate. If Congress intended for traditional charity law to be applied, the prohibition on private benefit is superfluous.

60. Comment, *Tax Exemptions for Educational Institutions: Discretion and Discrimination*, 128 U. PA. L. REV. 849, 863 (1980); see *Bob Jones*, 103 S. Ct. at 2040-42 (Rehnquist, J., dissenting); H.R. REP. NO. 1337, 83d Cong., 2d Sess. 51, reprinted in 1954 U.S. CONG. & AD. NEWS 4017, 4077.

61. See, e.g., *Thomas v. Harrison*, 24 Ohio Op. 2d 148, 156, 191 N.E.2d 862, 872 (P. Ct. 1962) (IRS determination that organization is not charitable not binding under state mortmain law); E. FISCH, D. FREED & E. SCHACHTER, *CHARITIES AND CHARITABLE FOUNDATIONS* § 3, at 3 (1974) ("[A] charity for purposes . . . of tort immunity or the rule against perpetuities may not be a charity for tax purposes.").

providing state property tax exemptions to religious organizations did not violate the establishment clause.⁶³ The Court, however, specifically rejected the theory that religious organizations could be granted exemptions on the basis of their contributions to social welfare.⁶⁴ This statement from *Walz* is inconsistent with the theory that Congress could use a public benefit analysis to justify tax exemptions to religious organizations.⁶⁵

The national policy against racial discrimination in education is "unmistakably clear"⁶⁶ and "compelling."⁶⁷ In *Bob Jones*, the Court found that this policy is so important that a violation of it would "undermine any public benefit that might otherwise be conferred."⁶⁸ Segregated private schools distort the viewpoint of their students, perpetuating the racism of the school's supporters.⁶⁹

Although private discrimination is a significant social problem, an even greater conflict with public policy results from interference with public school integration.⁷⁰ As the federal courts began to enforce *Brown v. Board of Education*⁷¹ in the South, thousands of "segregation academies" opened to accommodate the "white flight" from the newly integrated schools.⁷² These schools

62. 397 U.S. 664 (1970).

63. *Id.* at 680.

64. *Id.* at 674. The public benefit requirement was applied to religious organizations in England before the disestablishment of the Church of England. At that time, the Church provided many of the welfare services subsequently provided by the state. See Note, *The Internal Revenue Service's Revocation of the Tax Exempt Status of a Private Religious College Does Not Violate the First Amendment*, 50 U. CIN. L. REV. 615, 626-27 (1981). Trusts to support religions other than the established Church were treated as invalid as against public policy. M. CHESTERMAN, *supra* note 45, at 77. See generally *id.* chs. 2-5.

65. See Note, *supra* note 64, at 626-27.

66. 103 S. Ct. at 2032.

67. *Id.* at 2035.

68. *Id.* at 2029; see text accompanying note 49 *supra*.

69. See Drake, *Tax Status of Private Segregated Schools: The New Revenue Procedure*, 20 WM. & MARY L. REV. 463, 506-07 (1979).

70. The existence of discriminatory schools in Goldsboro, North Carolina evidently did not prevent that city from experiencing one of the nation's most successful school desegregations. Black and white achievement test scores rose after desegregation. R. MAYER, C. KING, A. BORDERS-PATTERSON & J. MCCULLOUGH, *THE IMPACT OF DESEGREGATION IN A SOUTHERN CITY* 85, 105 (1974). Unfortunately, it seems that few other school systems have experienced similar success. See Crain & Mahard, *Segregation and Black Achievement: A Review of the Research*, 42 LAW & CONTEMP. PROBS., Summer, 1978, at 17, 18 n.2.

71. 347 U.S. 483 (1954).

72. See *Norwood v. Harrison*, 413 U.S. 455, 457 (1973). These schools often received significant state support to undermine federal desegregation orders. *E.g.*, *Griffin v. County School Bd.*, 377 U.S. 218, 221 (1964) (tuition grants); *Brown v. South Carolina State Bd. of Educ.*, 296 F. Supp. 199, 199 (D.S.C.) (scholarships), *aff'd per curiam*, 393 U.S. 222 (1968); *Poindexter v. Louisiana Fin. Assistance Comm'n*, 275 F. Supp. 833, 835 (E.D. La. 1967) (tuition grants), *aff'd per curiam*, 389 U.S. 571 (1968); see Annot., *supra* note 8, at 550.

continue to provide a "haven to parents seeking to avoid public school integration."⁷³

The majority opinion, the concurring opinion by Justice Powell, and the dissenting opinion by Justice Rehnquist all concluded that denying tax benefits did not violate the first amendment.⁷⁴ The free exercise clause limits the government's power to interfere with religious practices.⁷⁵ If the government can demonstrate a compelling public interest, however, a neutrally applied restriction on free exercise is permitted.⁷⁶ In *Lemon v. Kurtzman*,⁷⁷ the Court stated that to be valid under the establishment clause, a statute must: have a secular purpose; not have a primary effect of inhibiting or advancing religion; and not create excessive entanglement with religion.⁷⁸ These decisions have created a balancing test, weighing the first amendment values against the government interest at stake.⁷⁹

Denying section 501(c)(3) status only indirectly burdens the free exercise of religious beliefs and practices. The IRS rulings do not prohibit any religion from operating racially discriminatory schools.⁸⁰ Bob Jones and Goldsboro can continue to operate, can still voice their religious beliefs and, if they are will-

73. Case Comment, *Racial Exclusion by Religious Schools: Brown v. Dade Christian Schools, Inc.*, 91 HARV. L. REV. 879, 886 (1978); Comment, *Section 1981 after Runyon v. McCrary: The Free Exercise Right of Private Sectarian Schools to Deny Admission to Blacks on Account of Race*, 1977 DUKE L.J. 1219, 1252. Bob Jones University was not a typical segregation academy because its discriminatory policies preceded *Brown* by several years. See *Bob Jones*, 468 F. Supp. at 893-94.

74. See, e.g., 103 S. Ct. at 2044 n.3 (Rehnquist, J., dissenting); *id.* at 2036 (Powell, J., concurring).

75. See generally J. NOWAK, R. ROTUNDA, & J. YOUNG, CONSTITUTIONAL LAW 1053 (2d ed. 1983).

76. *United States v. Lee*, 455 U.S. 252, 257-58 (1982) (upholding Social Security taxation of Amish employer because of overriding government interest in raising revenue); *Prince v. Massachusetts*, 321 U.S. 158, 170 (1944) (state's interest in guaranteeing child welfare justifies forbidding sale of religious tracts by children).

77. 403 U.S. 602 (1971).

78. *Id.* at 612-13.

79. Compare *Everson v. Board of Educ.*, 330 U.S. 1, 17-18 (1947) (state can provide free transportation to students of religious schools as well as public school students because benefit to religious groups is indirect and promotes child safety) with *Wolman v. Walter*, 433 U.S. 229, 253-54 (1979) (state cannot provide free transportation to parochial students for field trips because benefit aids religious groups more directly and inures to school rather than students). While a state may not provide unaudited funds to a parochial school to offset expenses incurred by state testing requirements, *Levitt v. Committee for Pub. Educ. & Religious Liberty*, 413 U.S. 472, 480-82 (1973), audited funding procedures are permissible because they insure that secular purposes are furthered. *Committee for Pub. Educ. & Religious Liberty v. Regan*, 444 U.S. 646, 660-62 (1980).

80. See *Simon*, *supra* note 46, at 502-05. Congress can make distinctions in exercising its taxing power, even though they impose indirect burdens on the free exercise of religious beliefs. Cf. *Braunfeld v. Brown*, 366 U.S. 599, 603-09 (1961) (state Sunday closing law upheld against the objections of Jews who observed Sabbath on Saturday).

ing to forgo tax-exempt status, presumably they can retain their present policies.⁸¹

The government interest in eliminating racial discrimination is compelling.⁸² This interest is as important as those interests previously held sufficient to justify burdening free exercise.⁸³ The federal government has, for example, the power to launch a vigorous attack on the practice of polygamy⁸⁴ or to impose social security taxes on Amish employers;⁸⁵ and state child-labor laws may prohibit the selling of religious literature by children,⁸⁶ despite the burden on religious beliefs.

The Court briefly disposed of a contention that providing tax benefits to some, but not all, religious groups was forbidden by the establishment clause. The Court found that section 501(c)(3), as interpreted, had a secular purpose and was neutral in effect. The government can enforce a neutral law with a secular purpose even if a coincidental effect is to favor one religion over another.⁸⁷

The most important establishment clause concern in *Bob Jones* is excessive entanglement. Denying a tax exemption based upon an IRS determination that a religious school discriminates racially does create government-church entanglement.⁸⁸ As the Court indicated, however, the entanglement problem would exist even if sincere religious practices were excluded from the IRS ruling. The IRS would then be required to examine the sincerity of a religious belief that supports discrimination.⁸⁹

81. Liability may exist under 42 U.S.C. 1981 (1976). See notes 135-37 and accompanying text *infra*.

82. *Bob Jones*, 103 S. Ct. at 2029-31, 2035; *cf.* *Norwood v. Harrison*, 413 U.S. 455, 468-69 (1973) (discrimination in private schools "exerts a pervasive influence on the entire educational process"); *Cooper v. Aaron*, 358 U.S. 1, 19 (1958) (students have a "fundamental" right to be free from racial discrimination).

83. Note, *supra* note 31, at 731; notes 66-73 and accompanying text *supra*.

84. See *Late Corp. of the Church of Jesus Christ of Latter Day Saints v. United States*, 136 U.S. 1, 49 (1890); *Reynolds v. United States*, 98 U.S. 145, 166-67 (1879); Worthing, "Religion" and "Religious Institutions" Under the First Amendment, 7 PEPPERDINE L. REV. 313, 318-19 (1980).

85. *United States v. Lee*, 455 U.S. 252, 261 (1982).

86. *Prince v. Massachusetts*, 321 U.S. 158, 167-70 (1944).

87. *Bob Jones*, 103 S. Ct. at 2035 n.30 (citing *McGowan v. Maryland*, 366 U.S. 420, 442 (1961) (Sunday closing laws upheld as only incidentally coinciding with the tenets of some religions)); see also *United States v. Lee*, 455 U.S. 252, 263 (1982) (Stevens, J., concurring) (tax law that is entirely neutral in general application is not constitutionally suspect).

88. See Laycock, *supra* note 12, at 264; Note, *The Internal Revenue Service's Treatment of Religiously Motivated Racial Discrimination by Tax Exempt Organizations*, 54 NOTRE DAME LAW. 925, 931 (1979); *cf.* *Walz*, 397 U.S. at 698-99 (Harlan, J., concurring) ("[T]he more discriminating and complicated the basis of classification for an exemption—even a neutral one—the greater the potential for state involvement in evaluating the character of organizations.").

89. 103 S. Ct. at 2035 n.30; *cf.* *Walz*, 397 U.S. at 674 ("Either course, taxation of churches or exemption, occasions some degree of involvement with religion."). The

The Court concluded that legal and practical reasons justify granting extensive authority to the IRS to interpret the Code.⁹⁰ The majority opinion first concludes that the IRS position was correct, and only then does it discuss the authority of the IRS.⁹¹ Instead of reaching its own conclusions and then examining the authority of the IRS,⁹² the Court could have upheld the rulings as reasonable interpretations of the IRC. If the rulings were upheld in this manner, it would be irrelevant that the Court, in the absence of an IRS interpretation, might have reached a different result.

Unless "weighty reasons" exist, courts will not overturn agency interpretations.⁹³ Congress has given the Secretary of the Treasury and the Commissioner of Internal Revenue broad authority to issue regulations and interpret the Internal Revenue Code.⁹⁴ Treasury regulations, consequently, will be upheld unless "unreasonable and plainly inconsistent with the revenue statutes."⁹⁵ The courts have specifically recognized the necessity of allowing the IRS to make policy decisions when literal application of the Code would have an undesirable result.⁹⁶

After recognizing that congressional inaction is normally of little use in determining the validity of administrative action, the Court found that Congress' failure to overturn the IRS interpretation of section 501(c)(3) was evidence of its acquiescence or approval. The Court pointed out that Congress was "acutely aware" of the 1970 and 1971 IRS rulings due to their controversial nature.⁹⁷ In the dozen years since these rulings, despite "exhaustive hearings" and the introduction of thirteen bills to overturn them, Congress has not altered section 501(c)(3).⁹⁸ In spite of many changes to the Code, including

district courts avoided an inquiry into the sincerity of the religious beliefs involved by finding or assuming that the beliefs were sincere. *Bob Jones*, 468 F. Supp. at 894-96 (court and IRS found sincerity); *Goldsboro*, 436 F. Supp. at 1317 (sincerity assumed for purposes of partial summary judgment).

90. 103 S. Ct. at 2031-32.

91. *Id.* at 2030.

92. *Id.* at 2030-32.

93. *Brewster v. Gage*, 280 U.S. 327, 336 (1930); B. SCHWARTZ, ADMINISTRATIVE LAW § 4.6, at 160 (2d ed. 1984).

94. 5 U.S.C. § 301. (1982); I.R.C. §§ 7801(a), 7802(a), 7805(a) (1982); see also *Commissioner v. Portland Cement Co. of Utah*, 450 U.S. 156, 169 (1981) (because Congress has determined that the Treasury Department, rather than the courts, should administer the tax laws, Commissioner's regulations are given great deference).

95. *Commissioner v. South Tex. Lumber Co.*, 333 U.S. 496, 501 (1947).

96. See, e.g., *Tank Truck Rentals, Inc. v. Commissioner*, 356 U.S. 30, 35 (1958); see also note 49 *supra*.

97. 103 S. Ct. at 2033.

98. E.g., H.R. 1096, 97th Cong., 1st Sess. (1981); H.R. 3225, 94th Cong., 1st Sess. (1975); see also *Administration's Change in Federal Policy Regarding the Tax Status of Racially Discriminatory Private Schools, Hearings Before the House Comm. on Ways and Means*, 97th Cong., 2d Sess. (1982); *Equal Educational Opportunity, Hearings Before the Senate Select Comm. on Equal Educational Opportunity*, 91st Cong., 2d Sess (1970).

the addition of section 501(i),⁹⁹ Congress has not only left section 501(c)(3) intact, it has recognized that racial discrimination in education is inconsistent with tax exempt status.¹⁰⁰

As Justice Rehnquist indicated, the "implicit ratification" argument has some weaknesses.¹⁰¹ The failure of one Congress to change an interpretation of a statute enacted by a prior Congress, perhaps of a different era and with another party in the majority, is of almost no value in construing the statute.¹⁰²

Even assuming that congressional inaction implicitly ratifies administrative rulings, it is difficult to find a ratification in the case of section 501(c)(3). The IRS adopted one interpretation of the exemption and deduction sections sixty years ago, changed its interpretation in the early seventies, and changed or attempted to change its interpretation while the present controversy was pending before the Supreme Court.¹⁰³ If Congress "ratified" the post-1970 IRS construction of section 501(c)(3), it can be argued with even greater force, as Justice Rehnquist indicated, that Congress "ratified" the long-standing pre-1970 interpretation.¹⁰⁴ At best, Justice Rehnquist contended, little can be discerned from Congress' actions (or inaction) and words, either before or after 1970.¹⁰⁵

Neither Goldsboro nor Bob Jones profess any hatred toward blacks. Goldsboro opposes both "cultural" and "biological" mixing of the races and completely excludes blacks.¹⁰⁶ In contrast, Bob Jones claims that it does not have any religious convictions against admitting blacks,¹⁰⁷ and, in 1975, it offi-

99. Act of Oct. 20, 1976, Pub. L. No. 94-568, pt. (a), 90 Stat. 2697, 2697 (current version at I.R.C. § 501(i) (1982)).

100. 103 S. Ct. at 2032-34 (citing S. REP. NO. 1318, 94th Cong., 2d Sess. 8, reprinted in 1976 U.S. CODE CONG. & AD. NEWS 6051, 6058).

101. *Id.* at 2043-45 (Rehnquist, J., dissenting).

102. See *United States v. Wise*, 370 U.S. 405, 411 (1962); R. DICKERSON, *THE INTERPRETATION AND APPLICATION OF STATUTES* 179-83 (1975).

103. See text accompanying note 16 *supra*.

104. See *Bob Jones*, 103 S. Ct. at 2043 (Rehnquist, J., dissenting); Dye & Webster, *Sup. Ct. in Bob Jones holds that exempt organizations are bound by law of charity*, 59 J. TAX'N 70, 72 (1983); *cf.* Brief for the United States at 24, *Bob Jones*, 103 S. Ct. 2017 (1983) ("An administrative reversal of position so many years later provides no legal basis for ascribing to a much earlier Congress an intent patently at odds with the very words of the statute.").

105. 103 S. Ct. at 2043 (Rehnquist, J., dissenting); Comment, *supra* note 60, at 863 ("little evidence of a systematic legislative policy behind . . . list of exempt organizations")

106. Petition for Certiorari, *Goldsboro Christian Schools*, Joint App. at 41. Allegedly, no blacks ever applied to Goldsboro. Brief for Petitioner, *Goldsboro Christian Schools* at 43.

107. *BOB JONES UNIVERSITY, THE BOMB AND ITS FALLOUT 4* (1983). Apparently, until "agitation" made the idea impractical, Bob Jones University considered establishing a separate institution to educate blacks. Petition for Certiorari, Joint App. at A111.

cially abandoned its racially discriminatory admissions policy.¹⁰⁸ The University does prohibit interracial dating and marriage by its students.¹⁰⁹ Citing prior Supreme Court decisions that support its conclusion that such limits on interracial association are forms of race discrimination, the majority refused to distinguish the policies of Bob Jones from those of Goldsboro.¹¹⁰ The Court used a single paragraph to dispose of Bob Jones' claim that it is nondiscriminatory.¹¹¹

What the Court chose not to do is as significant as what it did. It could have vacated the cases as moot and dismissed the appeal once the IRS decided that it would not defend its position before the Court. Another option was issuing a narrowly written opinion approving of the IRS interpretation without imposing a general public benefit requirement on all section 501(c)(3) organizations.¹¹²

The public benefit requirement may create problems for all section 501(c)(3) organizations. The test may be expanded to punish discrimination other than that based on race. In addition, the vagueness of the public benefit and public policy concepts can create uncertainty for charitable organizations. The possibility that the public benefit requirement could be applied to punish sex discrimination was raised by the original brief for the United States (composed before the administration chose not to defend the IRS rulings). The brief implied that sex discrimination was roughly comparable to racial discrimination, but it stated that the Commissioner had no intention of denying exempt status to punish sex discrimination.¹¹³

108. See note 34 and accompanying text *supra*.

109. *Bob Jones*, 468 F. Supp. at 894-95.

110. 103 S. Ct. at 2036. Neither the concurring opinion by Justice Powell, nor the dissent by Justice Rehnquist distinguished between the two institutions' policies.

111. *Id.* But *cf.* Note, *supra* note 15, at 712 (criticism of the Fourth Circuit's support in finding that Bob Jones violated an important public policy).

112. Other options were available. *E.g.*, Allen, *The Tax-Exempt Status of Segregated Schools*, 24 TAX L. REV. 409, 424-31 (1969) (racially discriminatory schools serve a noneducational purpose and therefore are not operated exclusively for an exempt purpose); *id.* at 426 (schools serve no public purpose); *id.* at 429-31 (exemptions are forbidden "assistance" to discriminatory organizations within the meaning of the Civil Rights Act of 1964).

113. (Draft) Brief for the United States at 37. The original brief also noted that the "constitutional and federal statutory proscriptions are far less pervasive" with regard to sex discrimination. *Id.* This disclaimer can hardly be reassuring to § 501(c)(3) organizations, since this IRS position may change, just as its stand on racially discriminatory schools changed. See Brief of Petitioner, Goldsboro Christian Schools at 36 (pressure on IRS to deny exemptions to schools practicing sex discrimination); Brief of the National Jewish Commission on Law and Public Affairs (COLPA) as Amicus Curiae at 3 (courts could apply public policy analysis to punish treatment of women by many Catholic, Protestant, Jewish, and other religious groups); Dye & Webster, *supra* note 104, at 74 (single-sex colleges, churches without female clergy, and religious organizations that confer benefits only on coreligionists "are all now subject to question"). But *cf.* P. TREUSCH & N. SUGARMAN, TAX-EXEMPT CHARITABLE ORGANIZATIONS 126 (2d ed. 1983) (no court has held that sex discrimination is inconsistent with the §

The vagueness of the public benefit concept could have a chilling effect on the activities of exempt organizations and result in random and inconsistent enforcement.¹¹⁴ There is little vagueness in the IRS position as applied. Probably any form of racial discrimination will result in the loss of tax benefits. By failing to carefully limit the future application of the public benefit requirement to prohibit racial discrimination, however, the Court has left the lower courts and the IRS to develop new, unpredictable limitations on charities.

Past attempts to apply public policy or public benefit requirements to non-profit organizations have had undesirable results. In some states, statutes have required that local courts approve the applications of nonprofit groups seeking to incorporate.¹¹⁵ Some local judges required that the organizations conform to public policy or corporate status was denied.¹¹⁶ As might be expected, unpopular organizations were denied corporate status,¹¹⁷ judges used their personal views in reviewing applications,¹¹⁸ and inconsistent approvals and denials of corporate status resulted.¹¹⁹ There is a danger that the IRS policy could vary with each change in the political climate.¹²⁰ The attempt by the IRS to aban-

501(c)(3) status of social clubs). The public benefit requirement might also be expanded to deny § 501(c)(3) status to discrimination based on sexual preference. Nixon, *Pity the Heathen Court*, LIBERTY, July-Aug. 1983, at 19, 21; cf. B. HOPKINS, *supra* note 44, § 6.9, at 135-36 (organizations that discriminate on basis of marital status, national origin, handicap, or age will risk losing exempt status).

114. See *Patton v. United States*, 281 U.S. 276, 306 (1930) ("public policy" so vague that it "should be accepted as the basis of a judicial determination if at all, only with the utmost circumspection"); *Big Mama Rag, Inc. v. United States*, 631 F.2d 1030, 1035 (D.C. Cir. 1980) (vague laws do not provide notice to public or guidelines for officials); Comment, *supra* note 60, at 877-79 (chilling effect and abuse of discretion).

115. See, e.g., MO. REV. STAT. § 352.060 (1978). In Missouri, an alternate means of incorporation exists, permitting direct application to the Secretary of State. *Id.* §§ 355.050-.055.

116. See *Association for Preservation of Freedom of Choice v. Shapiro*, 9 N.Y.2d 376, 382, 174 N.E.2d 487, 489, 214 N.Y.S.2d 388, 391 (1961); McAulay & Brewster, *In re Application of the Association for the Preservation of Freedom of Choice*, 6 How. L.J. 169, 170 (1960); Note, *Judicial Approval as a Prerequisite to Incorporation of Non-Profit Organizations in New York and Pennsylvania*, 55 COLUM. L. REV. 380, 388-89 (1955).

117. McAulay & Brewster, *supra* note 116, at 171 (criticizes denial of nonprofit corporate status to a white group advocating racial segregation). The New York Court of Appeals subsequently held that the lower courts had no statutory power to apply the public policy test. *Association for the Preservation of Freedom of Choice v. Shapiro*, 9 N.Y.2d at 382, 174 N.E.2d at 489, 214 N.Y.S.2d at 391; see also Comment, *supra* note 60, at 877.

118. Note, *supra* note 116, at 388-89.

119. *Id.* at 389.

120. The federal tax authorities have also occasionally sought to apply a public policy analysis to various organizations. Fifty years ago, a deduction for a contribution to an anti-vivisection society was determined not to be a charitable gift. The contention, overturned by the courts, was that the societies were not charitable because they opposed a governmentally-approved practice. *Pennsylvania Co. for Ins. on Lives & Granting of Annuities v. Helvering*, 66 F.2d 284 (D.C. Cir. 1933).

don its position that Bob Jones and Goldsboro were ineligible for exemptions is an example of such a change.¹²¹

Some question exists as to the ability of the IRS to adequately enforce its rulings. Some private schools have retained their tax exemptions even after federal courts (in cases not involving exempt status) have found them to be discriminatory.¹²² Justice Powell feared that the majority would give too much power to the IRS in an area beyond the agency's expertise.¹²³ IRS agents are presumably specialists in tax law and generally lack the expertise to handle complex non-tax matters.¹²⁴ Furthermore, the procedures for judicially challenging unfavorable IRS actions are of little value due to the time and formality involved.¹²⁵

There are, however, defenders of the IRS ability to determine exempt status. The IRS already makes important decisions relating to nontax matters,¹²⁶ and it has created a separate division to audit exempt organizations.¹²⁷ The IRS regularly holds hearings on matters of public concern,¹²⁸ and, since 1976, organizations have been able to seek a judicial determination of their exempt status once an unfavorable IRS ruling is made, without first being required to incur tax liability.¹²⁹ A plan to shift the determination of exempt status to another agency was considered in 1969. The plan was rejected, partially because of the high regard Congress has for IRS enforcement

121. See Benenson, *supra* note 6, at 211. The IRS initially was hostile to claims by public interest law firms that they deserved § 501(c)(3) status. This position may have been due to the controversial nature of such firms and the outcries of private interests threatened by the firms' activities. P. TREUSCH & N. SUGARMAN, *supra* note 113, at 113.

122. *Hearings*, *supra* note 14, at 5 (statement of Jerome Kurtz, Commissioner of Internal Revenue); Letter from Arthur Flemming to Rep. Chisholm (May 16, 1978), *reprinted in id.* at 237.

123. 103 S. Ct. at 2039 (Powell, J., concurring).

124. See Note, *The IRS, Discrimination, and Religious Schools: Does the Revised Revenue Procedure Exact Too High a Price?*, 56 NOTRE DAME LAW. 141, 151-52 (1980).

125. P. TREUSCH & N. SUGARMAN, *supra* note 113, at 287.

126. Drake, *supra* note 69, at 507. Revenue provisions and their interpretation have an impact, for example, on the decision to marry, *compare* I.R.C. § 1(a) (1982) *with id.* § 1(c) (marriage penalty); or buy a house, *see id.* § 163 (interest on mortgages deductible). The Bureau of Narcotics and Dangerous Drugs evidently makes decisions as to whether religious organizations require the use of an otherwise illegal drug to practice their religion. *See* 21 C.F.R. § 1307.31 (1983); Comment, *Brave New World Revisited: Fifteen Years of Chemical Sacraments*, 1980 WIS. L. REV. 879, 900-01. If the Bureau is capable of making such a difficult determination involving first amendment issues and so unrelated to its basic function, the IRS should be similarly capable.

127. P. TREUSCH & N. SUGARMAN, *supra* note 113, at 53.

128. *See, e.g.*, 1983-26 I.R.B. 1 (announcement of hearings on proposed regulations relating to personal service corporations); 1983-12 I.R.B. 1 (hearings relating to credit for increasing research activities).

129. I.R.C. § 7428 (1982); P. TREUSCH & N. SUGARMAN, *supra* note 113, at 284. *But see* text accompanying note 125 *supra*.

capabilities.¹³⁰

Even if narrowly construed, *Bob Jones* will still have a significant impact upon discriminatory religious schools. Many of these schools will become subject to social security and federal unemployment compensation taxes.¹³¹ The loss of deductible-donor status under section 170(c) will greatly reduce their fund-raising capabilities.¹³²

The loss of section 501(c)(3) status will have other, incidental, effects. Exempt organizations are often exempt from state taxes, eligible to receive reduced postage rates, and benefit from other provisions of state or federal law.¹³³ The total economic burden will be significant, and the schools will also be stigmatized by the loss of section 501(c)(3) status.¹³⁴

The *Bob Jones* decision has important implications for civil rights law. In *Runyon v. McCrary*,¹³⁵ the Court expressly declined to decide whether religious schools would be subject to a section 1981 action.¹³⁶ The rejection of the first amendment defenses in *Bob Jones* implies that such defenses will not prevail in a 1981 suit.¹³⁷

Troubled by the majority's broad language, Justice Powell based his concurring opinion on the theory of implicit ratification by Congress.¹³⁸ While

130. P. TREUSCH & N. SUGARMAN, *supra* note 113, at 277-78.

131. See note 18 *supra*. Up to 3,000 schools may be affected. Drake, *supra* note 69, at 505.

132. *Bob Jones Univ. v. Simon*, 416 U.S. at 729-30; Dye & Webster, *supra* note 104, at 73.

133. P. TREUSCH & N. SUGARMAN, *supra* note 113, at 15. Financial benefits may be lost at the federal, e.g., 39 U.S.C. § 3626(a) (1976) (reduced postage rates); 40 U.S.C. § 484(k)(1) (1976) (eligibility to receive surplus federal property), and state levels, e.g., MO. REV. STAT. § 143.441 (1978) (income tax exemption for organizations qualifying under § 501(c)(3)).

134. Note, *supra* note 64, at 626; Comment, *supra* note 60, at 874. These burdens may result in changes in the schools' policies, indirectly encourage donations to nondiscriminatory schools, and give a psychological boost to minority groups. See Drake, *supra* note 69, at 505-06 (might shift donations to exempt organizations); *id.* at 506 ("psychological value" to minorities); Note, *supra* note 31, at 728 (*Bob Jones* may change its policy since it has changed before). Unfortunately, the denial of exempt status may serve to certify racist policies and provide publicity for segregated schools, providing an unintended economic benefit.

135. 427 U.S. 160 (1976) (section 1981 action allowed against private secular schools).

136. *Id.* at 167.

137. Comment, *Section 1981 Liability for Racially Discriminatory Sectarian Schools*, 38 WASH. & LEE L. REV. 1237, 1247 (1981) (interpreting Fourth Circuit's decision in *Bob Jones* to mean that the government interest in eliminating race discrimination outweighs religious groups' interest in freedom from neutrally applied laws). *But see* J. NOWAK, R. ROTUNDA & J. YOUNG, *supra* note 75, at 651 (potential § 1981 liability "is more serious than the tax exemption issue for it would end the existence of these schools by government rule" and any prediction of the Court's decision "would be speculative").

138. 103 S. Ct. at 2036-39 (Powell, J. concurring).

Justice Powell should be commended for seeking to limit the use of the public benefit standard, his reliance on the implicit ratification theory ignored the central issue of whether the IRS exceeded its authority. If the IRS had the power to make its interpretations, implicit ratification is not needed. If the IRS exceeded its authority, it is difficult to see how a failure by Congress to act can legitimize such a usurpation of power. Both proponents and critics of the implicit ratification theory stress the action or inaction of Congress in regard to the correctness of the IRS interpretation.¹³⁹ What is crucial, however, is whether the IRS had the power to make the interpretation, regardless of whether it was correct in some abstract sense.¹⁴⁰

The effects of the *Bob Jones* decision will largely be determined by those enforcing the rulings it upheld. The courts and the IRS may place the burden of proof upon religious schools and other exempt organizations to show they do not discriminate.¹⁴¹ The burden of proving nondiscrimination could threaten the first amendment rights of religious schools that do not discriminate,¹⁴² while creating difficulties for all section 501(c)(3) organizations subject to the public benefit requirement.¹⁴³

Despite all the possible implications of the *Bob Jones* decision, it is unlikely that any of the "worst case" scenarios will occur. The IRS developed the public benefit doctrine only after a great deal of prodding by the courts.¹⁴⁴ Furthermore, the courts will probably continue to show substantial deference toward freedom of religion¹⁴⁵ and may limit the precedential value of *Bob Jones* to the particular fact situations considered.

139. See notes 97-105 and accompanying text *supra*.

140. See notes 93-96 and accompanying text *supra* (scope of IRS authority); *cf.* Unemployment Compensation Comm'n v. Aragon, 329 U.S. 143, 153 (1946) (Commission can be upheld even if there are reasonable alternatives or the court would have reached a different result); B. SCHWARZ, INTRODUCTION TO ADMINISTRATIVE LAW 193-98 (1958) (agency decisions are reviewed for "reasonableness," not "rightness").

141. Laycock, *supra* note 12, at 264-65.

142. There are already indications that courts may place the burden of proof on the schools. See *Judge Orders Affirmative Action as Condition for Tax Exemption*, TR.AXIS, July-Aug. 1983, at 9 (citing *Green v. Regan*, Civ. Act. No. 1355-69 (D.D.C. July 22, 1983)). *Green* held that tax exemptions would be denied to schools that "cannot demonstrate that they do not racially discriminate." *Id.* (quoting opinion).

143. Laycock, *supra* note 12, at 264-65.

144. Brief of the National Association for the Advancement of Colored People, Amicus Curiae in Support of Affirmance at 23 n.25; see also notes 8-10 and accompanying text *supra*.

145. Examples of the Supreme Court's willingness to uphold religious first amendment claims in the face of otherwise valid laws are numerous. See, e.g., *Wisconsin v. Yoder*, 406 U.S. 205, 234 (1972) (state cannot require compulsory attendance of high school age children of Old Order Amish); *Sherbert v. Verner*, 374 U.S. 398, 410 (1963) (state cannot deny unemployment compensation to a person whose unemployment results from a religiously-based refusal to work on Saturday); *West Va. Bd. of Educ. v. Barnette*, 319 U.S. 624, 642 (1943) (public school cannot require that Jehovah's Witness children salute the flag).

Still, a danger does exist that the federal government might, in a less tolerant era, construe *Bob Jones* in such a way as to justify official repression of certain religious groups or other organizations.¹⁴⁶ The Court could have issued a narrow ruling, perhaps approving of the IRS rulings as within the range of administrative discretion while disapproving of a broad public benefit requirement.¹⁴⁷ The Court can, and should, clarify and limit its decision to a prohibition on racial discrimination. This will remove the undesirable implications of the public benefit requirement while continuing to affirm the federal policy of eradicating discrimination. The best means of limiting the language of *Bob Jones* would be to devise a standard for applying the public benefit test in a manner that preserves the identity of charitable organizations while preventing tax benefits from indirectly supporting private racial discrimination.¹⁴⁸ If such a standard cannot be found, *Bob Jones* should be limited to its facts.

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146. Nixon, *supra* note 113, at 21.

147. Cf. Dye & Webster, *supra* note 104, at 73 (broad language "is particularly troubling because the Court's opinion did not need to be so broad to achieve its result"); Devins, *Did the High Court Go Too Far to Make a Politically Popular Ruling?*, Nat'l L.J., June 20, 1983, at 13, col. 1 (ruling is "dangerously and needlessly overbroad").

148. The following standards would limit the types of activities supporting revocation of the exemption while preserving the identity of exempt organizations: (1) Does the activity discriminate against what would be a suspect class if state action were involved, e.g., race, national origin, or religion? This standard would provide a guide for organizations seeking to limit their exposure, yet it would be flexible enough to accommodate changing Court perceptions on the scope of strict scrutiny review. (2) Is the discrimination necessary to preserve the identity of the exempt organization? Thus, while a religious group may be free to exclude members of other religions from its activities and retain its exemption, an organization that is primarily educational, literary, or scientific would not enjoy the same privilege. The sincerity of a religious group's beliefs should not be questioned. See notes 88-89 and accompanying text *supra*. Organizations should be classified according to function, rather than purpose. Thus, a religious school would be treated as an educational institution, rather than a religious group. Compare *Bob Jones*, 103 S. Ct. at 2035 n.29 (stressed educational function of the University) with *Bob Jones*, 468 F. Supp. at 897 (emphasized school's religious purpose).