Ecclesiastical Order of the ISM of AM, Inc. v. Commissioner, 83 T. C. 841 (1984)

A religious organization’s tax-exempt status under section 501(c)(3) is denied when its substantial nonexempt purpose involves counseling individuals on tax avoidance.

Summary

In Ecclesiastical Order of the ISM of AM, Inc. v. Commissioner, the Tax Court denied tax-exempt status to a religious organization under section 501(c)(3) because its primary activity was counseling individuals on tax benefits and avoidance, which constituted a substantial nonexempt purpose. The organization, incorporated in Michigan, offered membership stages for donations, each providing tax advice and benefits. The court found that these activities served private rather than public interests, thus failing the operational test for exemption. The decision emphasized that the presence of a single substantial nonexempt purpose can destroy tax-exempt status, regardless of other religious activities.

Facts

The Ecclesiastical Order of the ISM of AM, Inc. , incorporated in Michigan in 1978, sought tax-exempt status under section 501(c)(3). It operated a home office and 26 chartered orders, focusing on recruiting members through a campaign that emphasized tax benefits of being a minister. The organization offered four stages of membership (Phases of Awareness) for specific donations, providing literature and instructions on maximizing tax benefits, including housing allowances, auto usage, and family support. The materials suggested methods to minimize tax obligations and claimed the organization’s tax-exempt status allowed members to avoid IRS scrutiny.

Procedural History

The Ecclesiastical Order filed for tax-exempt status on January 15, 1980, which was denied by the IRS on February 18, 1981. The organization then filed a petition for declaratory judgment in the U. S. Tax Court, which heard the case fully stipulated. The court reviewed the administrative record and issued its opinion denying the tax-exempt status.

Issue(s)

1. Whether the Ecclesiastical Order of the ISM of AM, Inc. is operated exclusively for religious or charitable purposes under section 501(c)(3).
2. Whether the organization’s activities serve private rather than public interests.
3. Whether the organization’s emphasis on tax benefits constitutes a substantial nonexempt purpose.

Holding

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1. No, because the organization’s primary activity was counseling individuals on tax avoidance, which is not a religious or charitable purpose.
2. Yes, because the organization’s tax counseling primarily benefited its members, not the public.
3. Yes, because the organization’s literature and activities were so permeated with tax advice and avoidance strategies that it constituted a substantial nonexempt purpose.

Court’s Reasoning

The court applied the operational test under section 501(c)(3), which requires that an organization’s activities primarily serve exempt purposes. The court found that the Ecclesiastical Order’s substantial nonexempt purpose was to counsel individuals on tax avoidance, which is not religious or charitable. The court noted that even if the organization genuinely held religious beliefs, the pervasive nature of its tax counseling activities destroyed its exempt status. The court cited precedent that a single substantial nonexempt purpose can negate exemption, emphasizing that the organization’s activities resembled those of a commercial tax service rather than a religious institution. The court rejected the organization’s arguments that it was merely informing members of tax benefits and that discussing taxes was necessary for attracting new members, finding these activities went beyond any bona fide religious purpose. The court also dismissed constitutional arguments, stating that tax exemption is a matter of legislative grace and not a constitutional right, and that the denial was based on the organization’s activities, not its beliefs.

Practical Implications

This decision impacts how religious organizations seeking tax-exempt status under section 501(c)(3) should structure their activities. Organizations must ensure that any discussion of tax benefits remains incidental to their primary religious or charitable purposes. The ruling clarifies that pervasive tax counseling can disqualify an organization from tax-exempt status, even if it genuinely holds religious beliefs. Legal practitioners advising religious organizations should caution clients against structuring their operations primarily around tax benefits. This case also reaffirms that tax exemption is not a constitutional right but a legislative privilege, guiding future cases involving challenges to tax-exempt status denials based on constitutional grounds. Subsequent cases have applied this ruling to deny exemptions to organizations whose primary activities involve tax advice or avoidance.

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