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South Iowa Methodist Homes, Inc. v. Board of Review: Tax Exemption of Charitable Property in Course of Construction

SOUTH IOWA METHODIST HOMES, INC. v. BOARD OF REVIEW: TAX EXEMPTION OF CHARITABLE PROPERTY IN COURSE OF CONSTRUCTION

Undeterred by the doctrine of strict construction applicable to tax exemption statutes, the Supreme Court of Iowa, in *South Iowa Methodist Homes, Inc. v. Board of Review*,[1] granted exemption to land and a building in the course of construction owned by a charitable institution. This result conformed with a pending amendment to Iowa's tax exemption statute[2] providing for exemption of charitable property while in the course of construction. This Note will evaluate *South Iowa* in light of the conflicting case law presented and the policy behind the exemption of charitable property.

Plaintiffs applied for tax exemption of its land and a building while it was under construction. When completed the building was to be used as a home for the elderly. The pertinent portion of the Iowa statute exempted all grounds and buildings "used" by charitable institutions for their "appropriate objects."[3] It was stipulated that the land and building, when *completed* and *occupied*, would qualify for exemption under the statute. Whether exemption could be granted under these particular facts depended upon the interpretation of the word "used" in the statute.

Involved in the decision was a balancing of various factors regarding the exemption of property from taxation. As a general proposition taxation is the rule and exemption the exception.[4] Thus statutes passed for the purpose of exempting property must be strictly construed and all doubts resolved in favor of taxation. Applying these principles, it would appear that the Iowa statute exempted charitable property only when *actually used*. On the other hand, by providing for exemption of charitable property, the legislature obviously intended to encourage the charitable use of property. If the doctrine of strict construction necessitates a narrow interpretation excluding exemption under these facts, the obvious intent of the legislature would be defeated by adding costs to those charities seeking to make a charitable use of their property.

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1. 136 N.W.2d 488 (Iowa 1965).

2. IOWA CODE ANN. § 427.1(9) (1949) as amended by IOWA CODE ANN. § 427.1(9) (Supp. 1965). The amendment was approved on June 4, 1965 and will take effect July 4, 1966.

3. IOWA CODE ANN. § 427.1(9) (1949) provides in part that the following classes of property shall not be taxed:

> Property of religious, literary, and charitable societies. All grounds and buildings used by . . . charitable, benevolent, . . . and religious institutions and societies solely for their appropriate objects.

4. See *e.g.*, Cornell College v. Board of Review, 248 Iowa 338, 81 N.W. 2d 25 (1957); Trustees of Iowa College v. Baillie, 236 Iowa 235, 17 N.W.2d 143 (1945); Wagner v. Board of Review, 232 Iowa 58, 4 N.W.2d 405 (1942).

In reversing the lower court and granting the exemption, the court said:

> [I]t is in accord with legislative intent, more consistent with our own decisions, and not contrary to any general rule in other jurisdictions to hold that property, which will be exempt under section 427.1 (9) when a building being erected thereon is completed and occupied, is also exempt during the construction period.[5]

Initially, it was questioned whether the statute was not so plain on its face as to provide for exemption without resort to judicial interpretation.[6] The use of the land for construction of the building might constitute an "appropriate object" in itself, thus exempting the land from assessment. The partially completed building was subject to taxation as part of the land.[7] If the land were exempt there would be no basis upon which to tax the building. The court, however, did not pursue this line of reasoning. Rather the issue was reduced to its proper perspective and was considered in the light of the policies which gave rise to the statute. A possible barrier to exemption in *South Iowa* was the rule of strict construction of exemption statutes. As one court in denying exemption under facts similar to those in *South Iowa* stated: "Statutes granting exemptions from taxation are strictly construed to the end that such concession will be neither enlarged nor extended beyond the plain meaning of the language employed."[8] While recognizing that strict construction of tax exemption statutes severely limits exemption in doubtful cases, the court rejected the Board's contention that under a strict construction the word "used" could not be construed to mean "to be used."[9]

Some doubt arose as to whether the rule of strict construction was even applicable in this case. Section 4.2 of the code provided that the "provisions and all proceedings" under the code be construed liberally "with a view to promote its objects and assist the parties in obtaining justice."[10] The *South Iowa* court reasoned that although the legislature did not intend a liberal construction when deciding whether a charitable activity satisfied the "appropriate object" requirement, once the project was considered within the statute on this basis, Section 4.2 called for a liberal construction.[11] This

5. South Iowa Methodist Homes, Inc. v. Board of Review, 136 N.W.2d at 492.

6. 136 N.W.2d at 489.

7. See Wagner v. Board of Review, 232 Iowa 58, 4 N.W.2d 405 (1945).

8. Cedars of Lebanon Hosp. v. Los Angeles County, 35 Cal.2d 729, 734, 221 P.2d 31, 34 (1950).

9. South Iowa Methodist Homes, Inc. v. Board of Review, 136 N.W.2d at 489.

10. IOWA CODE ANN. § 4.2 (1949). This section provides:
> The rule of the common law, that statutes in derogation thereof are to be strictly construed, has no application to this code. Its provisions and all proceedings under it shall be liberally construed with a view to promote its objects and assist the parties in obtaining justice.

11. 136 N.W.2d at 489-90.

reasoning was not supported by authority. Furthermore, section 4.2 is not specifically directed to the code provisions on taxation. It is a general rule of construction applicable throughout the code. Section 4.2 appears to be aimed at negating the common law rule of construction that all statutes in derogation of the common law are to be strictly construed. It seems clear that such a construction would have conflicted with the established rule of strict construction of exemption statutes enunciated in previous Iowa decisions.[12]

In any event, it appears that the *South Iowa* court did not adopt the rule of liberal construction and granted exemption despite the doctrine of strict construction. Colorado has liberally construed its exemption statute and granted exemption to property in the court of construction.[13] The court in *South Iowa*, however, rejected these cases[14] because the Colorado court had utilized a liberal construction of its tax exemption statute.

Speaking in favor of exemption in *South Iowa* were the anomalies which would arise if exemption were denied. In *National Bank of Burlington v. Huenke*,[15] the court held that trust funds to be applied to the construction of an exempt building were exempt from taxation. In *South Iowa*, as stipulated by the parties, the property in controversy would be exempt when the building was completed and occupied.[16] If exemption were denied, use of exempt funds to build an exempt building would not preclude taxation during the construction period. The dissent attempted to distinguish the *Huenke* case on the grounds that *Huenke* dealt with a section of the exemption statute[17] dealing with moneys and credits and placing stress upon the ownership of the trust funds.[18] The court in *Huenke* based its decision on the fact that although the hospital had not yet been constructed, the trust funds were firmly committed and could not be diverted from the purpose of constructing the hospital. While this distinction appears valid, it seems equally clear that when a charity has partially completed construction of a building a firm commitment would be present from which, in the ordinary course of events, the charity would not be diverted.

Another anomaly arises out of the fact that when a charity has purchased a building (already fit for use) to be used for an

12. *E.g.*, Cornell College v. Board of Review, 248 Iowa 338, 81 N.W.2d 25 (1957); Trustees of Iowa College v. Baillie, 236 Iowa 235, 17 N.W.2d 143 (1945); Wagner v. Board of Review, 232 Iowa 58, 4 N.W.2d 405 (1942).

13. See McGlone v. First Baptist Church of Denver, 97 Colo. 427, 50 P.2d 547 (1935); El Jebel Shrine Ass'n v. McGlone, 93 Colo. 334, 26 P.2d 108 (1933).

14. 136 N.W.2d at 491.

15. 250 Iowa 1030, 98 N.W.2d 7 (1959).

16. 136 N.W.2d at 489.

17. See IOWA CODE ANN. § 427.1(10) (1949).

18. 136 N.W.2d at 494 (dissenting opinion).

"appropriate object" such property can qualify for exemption before July 1 of the tax year.[19] If exemption were denied under the present facts, property on which a building was completed by July 1 would be taxable at its value on the assessment date. The *South Iowa* court states: "While these results may not reach the stage of being absurd or ridiculous, they certainly are inconsistent, unjust and unfair."[20]

Before turning to the cases considered by the court, it is necessary to examine briefly the rationale behind the exemption of charitable property from taxation. It has been said that "the fundamental ground upon which all such exemptions are based is a benefit conferred on the public by such institutions, and a consequent relief, to some extent of the burden upon the state to care for and advance the interests of its citizens."[21] The benefits derived by the public from charitable institutions far outweigh the trivial inequality caused by an exemption of their property.[22] Furthermore, in the absence of private charity, the state would be obliged to carry out these functions with the result that the tax burden would be increased to provide revenues for these additional activities. It would seem therefore that exemption of charitable property is not merely a favor conferred upon charities by the state. It is based on sound reasoning and is in the best interests of the state:

> It is obvious that the welfare exemption is designed to serve both social and economic ends. The electors of the state must be deemed to have been aware of the need of the services afforded by the designated organizations when carried on impartially without self-interest. Implicit in the legislation is the knowledge that the maintenance of the facilities and the dispensation of the services as a result of private contributions of funds and personal effort become less of a burden on the taxpaying public than would be the

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19. IOWA CODE ANN. § 427.1(25) (1949). This section provides:
In any case where no such claim for exemption has been made to the assessor prior to the time his books are completed, such claims may be filed with the local board of review or with the county auditor not later than July first (1st) of the year for which such exemption from taxation is claimed, and a proper assessment shall be made either by the board of review or by the county auditor, if such property is all or in part subject to taxation.
Essentially the same result was reached prior to this statutory provision by case decision. Iowa Wesleyan College v. Knight, 207 Iowa 1238, 224 N.W. 502 (1929).

20. 136 N.W.2d at 490.

21. Book Agents of Methodist Episcopal Church, South v. Hinton, 92 Tenn. 188, 190, 21 S.W. 321, 322 (1892).

22. Brenau Ass'n v. Harbison, 120 Ga. 929, 48 S.E. 363 (1904) (dictum). The dissent in *South Iowa* questioned whether the inequalities caused by the shifting of the tax burden were in fact "trivial." It would seem doubtful in view of the insatiable demands for revenue by the state and the increase of property exempt from taxation. The charitable exemption is firmly established, however, and as long as this is the case it seems the policies behind such exemption should be given full effect.

cost under public ownership and control.[23]

A lesser tax burden enables the charity to make its services more widely available. The resulting reduction in cost to the charity is deemed a greater benefit to the public than would be a decrease of the public tax burden if such property were not exempt.[24] Tax exemption of charitable property is a recognition of the benefits society receives from the work carried on by the charities. *South Iowa* involves the determination of that point at which the property of a charitable institution begins to fulfill the purposes for which exemption is granted. Inherent in the conclusion reached in *South Iowa* is the fact that exemptions are provided to aid charities in the *formation* as well as the continuation of the property utilized in providing charity.

Several jurisdictions utilize a strict construction of their exemption statutes. In arriving at opposite conclusions, the cases illustrate the dichotomy existing as to the exemption of property in the course of construction, which concededly would be exempt when completed and used.

In *Cedars of Lebanon Hosp. v. Los Angeles County*,[25] the California court refused to grant exemption to a nearly completed student nurses residence. Admittedly the building would be exempt when completed and used. The statute provided for exemption of property "used exclusively"[26] for exempt purposes. The court said that "such express limitation, making use the focal point of consideration, contemplates *actual use*, as differentiated from an *intention to use* the property in a designated manner."[27] The California court went on to say that even if the statute was not to be limited by the doctrine of strict construction, under no theory of construction could a building in the course of construction be viewed as being *used* for any purpose.[28]

Pennsylvania has adhered closely to the view expressed in the *Cedars* case. *Dougherty v. City of Philadelphia*[29] construed the exemption statute requiring "actual use and occupation."[30] The Pennsylvania Supreme Court held that a new school building, in course of erection on a newly purchased lot which had never been exempt from taxation, was not entitled to exemption. The same result was reached when a building was completed and used before

23. Cedars of Lebanon Hosp. v. Los Angeles County, 35 Cal.2d 729, 750-51, 221 P.2d 31, 41 (1950) (dissenting opinion).
24. *Ibid.*
25. 35 Cal.2d 729, 221 P.2d 31 (1950).
26. See CAL. REV. & TAX. CODE § 214.
27. 35 Cal.2d at 742, 221 P.2d at 39.
28. *Ibid.*
29. 112 Pa. Super. 570, 172 Atl. 177 (1934).
30. Pa. Laws 1919, act 1021, § 1, as amended by Pa. Laws 1925, act 388, § 1. The same requirements are now found in PA. STAT. ANN. tit. 72, § 5020-204(1) (Supp. 1964).

the end of the tax year.[31] This line of reasoning, however, has been abandoned in at least three instances.

The first exception is found in *Dougherty* itself. The taxpayer in that case also owned a lot adjacent to the non-exempt land and had maintained a school building on this land for a number of years. During this period the land and building had been exempt. The old building was then razed and construction was begun on a new building. The Pennsylvania court said that this property was not subject to taxation since the temporary absence of actual use did not destroy the original exemption which had attached to the land and the old building.[32]

A second exception was recognized in *Appeal of Children's Hosp. of Philadelphia*[33] in which the court held that land upon which a hospital addition was being built was entitled to exemption. This land had been previously exempted on the basis that it was necessary to the proper utilization of the original hospital building. In this case the court propounded an interesting question when it asked: "Would anyone contend that if a hospital burned to the ground, that the ground on which a new structure was being built and the uncompleted building itself, would be subject to taxation?"[34]

This question was answered in *Summerfield Methodist Episcopal Church v. City of Philadelphia*[35] wherein the court held that when a church building had been destroyed by fire, the property was exempted from taxation during the time it took to construct a new building.

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31. Jewish Maternity Ass'n v. Philadelphia, 24 Pa. Dist. 307 (C.P. 1915).

32. 112 Pa. Super. at 575-77, 172 Atl. 179-80 (dictum). The court held, however, that as part of the premises for which exemption was claimed was not exempt, the bill had to be dismissed.

33. 82 Pa. Super. 196 (1923). The court held that since the land had been exempted previously and would soon be "used" for charitable purposes again, the fact that it was temporarily not being "used" for charitable purposes while it was under construction did not make the property subject to taxation. Two hypothetical situations show the arbitrary and anomalous results obtained under the Dougherty and Children's cases: XYZ Hospital owns a parking lot across the street from the main hospital building which is exempt from taxation. Thereafter XYZ Hospital ceases to use the lot for parking and begins construction of an additional building on the lot. Under the Children's and Dougherty cases, the property would be exempt during the course of construction. Now if XYZ Hospital purchased a parking lot across the street which had previously been privately owned and operated and not exempt from taxation, the property would be taxable while the building was in course of construction under the Dougherty decision. In both situations the same building is being built for the same charitable purposes, yet under one set of facts the property is exempt and under the other it is taxable.

34. *Id.* at 198 (dictum).

35. 88 Pa. D. & C. 134 (C.P. 1954). This case dealt with a church building, but the same reasoning would appear to be applicable to charitable property as stated by the dictum in the *Children's* case.

It may be summarily stated that in Pennsylvania charitable property in the course of construction will be exempt from taxation if the land had been used previously for an exempt purpose and the cessation of actual use is limited to situations involving repair, restoration, or enlargement. As to the issue presented in *South Iowa*, however, Pennsylvania would probably deny exemption.

New Jersey similarly denied exemption to property in the course of construction under its exemption statute requiring that the property be "actually used."[36] Carrying the requirement to a "drily logical" extreme, the court denied exemption to a home for the elderly which had been completed but not occupied and used before the assessment date.[37]

In rejecting the "actual use" doctrine, evident in the Pennsylvania and New Jersey cases, the Iowa court distinguished these cases on the ground that the Pennsylvania and New Jersey statutes were more stringent than the Iowa statute. The court obviously preferred the dissent in the *Cedars* case. An examination of the decisions reveals the basic elements which have led the courts to adopt the "actual use" test rejected in *South Iowa*.

The rule of strict construction of exemption statutes presents the most ominous barrier to exemption of charitable property while under construction. The reasoning supporting this rule is that exemptions are provided only by the grace of the sovereign power.[38] The granting of such grace is viewed as an appropriation of public funds. To the extent that certain property is exempt from taxation it is necessary to increase the rate of taxation on other properties to provide the funds necessary to carry on the functions of the government.[39] The granting of an exemption is in effect a restraint of sovereign power and as such must be strictly construed against those receiving such concession. Courts have frequently applied the rule of strict construction where the argument for exemption

36. See Institute of Holy Angels v. Borough of Ft. Lee, 80 N.J.L. 545, 77 Atl. 1035 (Sup. Ct. 1910), construing N.J. Laws 1903, act 394. The present requirement that property be "actually and exclusively used" is found in N.J. STAT. ANN. § 54:4 - 3.6 (Supp. 1964).

37. Borough of Longport v. Max & Sarah Bamberger Seashore Home, 91 N.J.L. 330, 102 Atl. 633 (Ct. Err. & App. 1917) (per curiam). This case was distinguished in Trenton Ladies Sick Benefit Soc'y v. City of Trenton, 19 N.J. Misc. 176, 17 A.2d 809 (B.T.A. 1941), where a home for the aged erected by a charitable organization had been completed and had opened its doors prior to the assessment date. No applications were received before the assessment date. The court granted the exemption and, in distinguishing the Bamberger case, said that there the home was not yet ready for applications even though fully constructed.

38. Town of Milford v. Comm'r of Worcester County, 213 Mass. 162, 165, 100 N.E. 60, 62 (1912).

39. Massachusetts Gen. Hosp. v. Inhabitants of Belmont, 233 Mass. 190, 124 N.E. 21 (1919). See ZOLLMAN, AMERICAN LAW OF CHARITIES, §§ 686-696 (1924), which discusses the rule of strict construction and the rule of liberal construction of exemption statutes.

has been highly persuasive.[40] Dissenters, on the other hand, have called for exemption in these cases under a "strict but reasonable" interpretation:

> It is no answer to say that in such cases the policy was one of liberal construction. Under the 'strict but reasonable' formula announced the result should be the same. When an exemption appears under that rule of construction, the 'reasonable' application of the exemption language in my opinion requires a result in conformity with the general rule accepted in the foregoing cases.[41]

Pennsylvania has on occasion been compelled to retreat from the results of strict construction where there has been a prior use of the land for exempt purposes. Thus, in *Dougherty*[42] the taxpayer claimed exemption for two adjacent lots. On each lot an old building had been razed and a new building erected. It seems illogical that the court should have come to opposite conclusions with respect to the tax status of the two lots. Under a strict construction of the exemption statute, neither propery was being actually used at the time of the assessment since both buildings were in the course of construction.

In any event, while many cases can be said to turn on this difference between strict and liberal construction, it would seem that the specific statutory language of exemption statutes presents an equally limiting effect on the exemption of charitable property in course of construction. *State v. Fisher*[43] dealt with a statute which required property to be "used"[44] for charitable purposes. The New Jersey court, while denying exemption under the facts, questioned what the result would have been if actual preparation had been commenced toward use of the property. In *Institute of Holy Angels v. Borough of Ft. Lee*,[45] however, the court said this question had been rendered moot by the insertion of the words "actually used"[46]

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40. See Cedars of Lebanon Hosp. v. Los Angeles County, 35 Cal.2d 729, 221 P.2d 31 (1950); Dougherty v. City of Philadelphia, 112 Pa. Super. 570, 172 Atl. 177 (1924). Some of the principles applicable under the rule of strict construction of tax exemption statutes are evident in the Pennsylvania decisions. Thus a claimant of exemption from taxation must show affirmative legislation in support of his claim and must show that his case is clearly within it. Dougherty v. City of Philadelphia, 314 Pa. 298, 171 Atl. 583 (1934). Furthermore the statute creating the exemption must be strictly construed against the taxpayer and if the right to exemption is doubtful, the doubt must be construed in favor of taxation. Harrisburg v. Cemetary Ass'n, 30 Dauph. 302, 9 Pa. D. & C. 773 (C.P. 1927).

41. Cedars of Lebanon Hosp. v. Los Angeles County, 35 Cal.2d at 754, 221 P.2d at 46 (dissenting opinion).

42. 112 Pa. Super. 570, 172 Atl. 177 (1934).

43. 68 N.J.L. 143, 52 Atl. 228 (Sup. Ct. 1902).

44. N.J. Laws 1886, act 1078. The present requirement that the property be "actually and exclusively used" is found in N.J. STAT. ANN. § 54:4-3.6 (Supp. 1964).

45. 80 N.J.L. 545, 77 Atl. 1035 (Sup. Ct. 1910).

46. N.J. Laws 1903, act 394. The present requirement that property

in place of "used" and that a building under construction, intended for an exempt use, was not exempt until so used. These two cases illustrate that the New Jersey court was at least aware of a possible difference in results had the statute in the *Holy Angels* case required only "use" rather than "actual use."

Underlying the formation of charitable exemption statutes in terms of *actual use* is the theory that such exemptions are granted on a *quid pro quo* basis.[47] Under this theory there is no basis upon which to predicate exemption until society is actually reaping the benefits that enure from a charitable use of property. This is a manifestation of the view that private charities relieve the state of a burden which it would otherwise have to carry on. In return for these services, the state relieves the charities of the tax burden. It is this traditional concept that leads legislatures to frame exemption statutes in terms of use. Such statutes, together with the rule of strict construcion, preclude the flexibility needed to resolve situations which do not meet the set legal standards, but which in terms of logic, fairness and justice warrant a less stringent test.

Another well established basis for the doctrine of "actual use" is the judicial reluctance to extend exemption to mere charitable intentions. The *Cedars* court said:

> It is argued that some effect should be given to these factors: that the exemption here is sought for property on which considerable progress had already been made with the building, that work was being diligently prosecuted, and upon its completion it was in fact used pursuant to its design for an exempt purpose—as distinguished from a claim made with respect to vacant land on which it is the intention to start construction at some future date. But these considerations attesting to the exercise of the institution's good faith in carrying out its building program are wholly immaterial. . . .[48]

The dissent in *South Iowa* expressed the fear that such intentions

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be "actually and exclusively used" is found in N.J. STAT. ANN. § 54:4-3.6 (Supp. 1964).

47. As stated by one court: ". . . and it is only in those cases where the property is put to some use calculated to minimize the expenses of government that public policy justifies an exemption." Medical Soc'y of Kings County v. Neff, 34 App. Div. 83, 85, 53 N.Y. Supp. 1077, 1079 (Sup. Ct. App. Div. 1898). This theory was later rejected in New York where the court said:

> There is no more ground for holding that an educational corporation receives its tax exemption upon the principle of non-taxation of public places, and as a 'quid pro quo' etc., than a like holding as to exemptions made to religious and charitable, etc., corporations.

Application of Thomas S. Clarkson Memorial College of Technology, 274 App. Div. 732, 87 N.Y.S.2d 491 (1949). See Note, *Tax Exemption of Charitable Property*, 80 U. PA. L. REV. 724 (1931-32).

48. 35 Cal.2d at 743, 221 P.2d at 40.

may never be carried out.[49] Thus the exemption having been granted, the tax revenue is lost forever.

Rejecting the "actual use" doctrine, the *South Iowa* court adopted instead the more liberal view expressed in *Village of Hibbing v. Commissioner of Taxation.*[50] This approach utilizes the "intention to use" doctrine in arriving at the conclusion that charitable property in course of construction is exempt from taxation.

The *Hibbing* court granted exemption to a building being remodeled and fitted to a charitable use:

> [T]he right to exemption depends upon the concurrence of the institution's ownership and use of the property as a public hospital. The right of exemption carries with it, *as an incident*, a reasonable opportunity by an institution entitled to tax exemption of its property, in execution of an intention so to do, to adapt and fit property acquired by it for the use upon which the right of exemption rests.[51]

This view has also been adopted in New York. The court there had held that the real property of a charitable corporation was exempt from taxation, though not in actual use because of the absence of suitable buildings, where the erection of such buildings was contemplated in good faith.[52] Texas has also exempted property of charitable institutions during *bona fide* preparation for actual operation.[53]

The "intention to use" doctrine is based on the premise that once a charitable institution expends money and does work on a program designed to result in the use of property for charitable purposes, the statutory requirements are satisfied and the property is within the objects of the exemption provisions.[54] In adopting this

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49. 136 N.W.2d at 494-95 (dissenting opinion).

50. 217 Minn. 528, 14 N.W.2d 923 (1944). The dissent in *South Iowa* contended that the case was not in point since the main question before the court was the sufficiency of equitable ownership as a basis for tax exemption. The exemption of property being adopted and fitted for charitable use, however, was very much in issue. No attempt to distinguish the case on the basis that it did not involve the erection of a building, but merely adoptation of an existing building, can be validly supported in view of the language of the court in providing for exemption of charitable property during the time necessary to fit acquired property to charitable use.

51. *Id.* at 535, 14 N.W.2d at 926-27 (emphasis added).

52. *In re* Miriam Osborn Memorial Home Ass'n, 140 N.Y. Supp. 786 (Sup. Ct. 1912). The charitable organization had frequently discussed a building program and had set up a fund for such purposes.

53. See Hedgecroft v. City of Houston, 150 Tex. 654, 244 S.W.2d 632 (1952), wherein it was held that property acquired for use as a hospital and a clinic was exempt not only during the period of actual operation, but also during the period in which preparations necessary to ready the premises for actual operation were being made.

54. See, *e.g.*, McGlone v. First Baptist Church of Denver, 97 Colo. 427, 50 P.2d 547 (1935); El Jebel Shrine Ass'n v. McGlone, 93 Colo. 334, 26 P.2d 108 (1933).

view, the Iowa court has recognized that where a building is actually in the course of erection, the property is entitled to exemption. This holding signifies a somewhat restrained adoption of the "intention to use" doctrine. Other states have gone so far as to hold that the buying of land and the drawing up of plans,[55] the breaking of land,[56] and the destruction of a building for the purpose of constructing a new one[57] constitute such a *bona fide* intention as to qualify for exemption.

When evaluating the Iowa court's decision, it must be remembered that the exemption statute was designed to encourage charitable institutions to devote their land to charitable uses.[58] It is submitted that, while the "actual use" doctrine does aid charitable institutions in their endeavors, it is not until facilities are completed that the charity receives any benefit whatsoever. The "actual use" doctrine lacks the necessary inducement for expanding facilities and establishing new facilities. This observation takes on added significance when it is noted that many exemption statutes provide that all revenues taken in by charities from the use of exempt lands must be used for the maintenance, repair and necessary increase of facilities.[59] As stated by the dissent in *Cedars*:

> Expansion is necessary to keep abreast of increased public need due to population and other changes. Under modern conditions, neither a hospital nor any other welfare service can remain static. If the trust funds, contributions and earnings are tax exempt, no good reason requires a denial of exemption because of the temporary use of assets to construction purposes, where the property in its converted state is also exempt.[60]

The court in *South Iowa* reasoned that to tax the charity when it was seeking to expand or build facilities would not be within the spirit of tax exemption statutes.[61] Furthermore, since charities carry on their programs by relying heavily on public contributions

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55. See Board of Foreign Missions of the Methodist Episcopal Church v. Board of Assessors, 244 N.Y. 42, 154 N.E. 816 (1926). *Contra*, City and County of Denver v. George Washington Lodge Ass'n, 121 Colo. 470, 217 P.2d 617 (1950), where an architect had prepared first sketch of a building and the realty had been rezoned to permit erection of building.

56. El Jebel Shrine Ass'n v. McGlone, 93 Colo. 334, 26 P.2d 108 (1933) (Construction of foundation).

57. McGlone v. First Baptist Church of Denver, 97 Colo. 427, 50 P.2d 547 (1935). *Contra*, Dougherty v. City of Philadelphia, 112 Pa. Super. 570, 172 Atl. 177 (1934) (by implication).

58. 136 N.W.2d at 490.

59. See PA. STAT. ANN. tit. 72, § 5020-204(c) (Supp. 1964), which requires that "the entire revenue derived by the same be applied to the support and to increase the efficiency and facilities thereof, the repair and the necessary increase of grounds and buildings thereof, and for no other purpose." See also N.J. STAT. ANN. § 54:4-3.6 (Supp. 1964).

60. 35 Cal.2d at 753, 221 P.2d at 46 (dissenting opinion).

61. 136 N.W.2d at 490.

it would appear illogical to reclaim such contributions in the form of taxes.

As noted, the dissent argued that too often the avowed intentions of charities go awry, that there is no assurance the building will ever be completed, or if completed, that it will be used for charitable purposes.[62] This contention poses a serious problem which has not been adequately resolved by the states adopting the "intention to use" theory.

In final analysis, the court's determination rested on the adoption of one of two cases: the *Hibbing* case[63] which represents the "intention to use" doctrine or the *Cedars* case[64] adopting the "actual use" doctrine.

The efficacy of *Cedars* was certainly to be doubted in light of subsequent events. After *Cedars* the California legislature proposed an amendment to the constitution and an additional section to the exemption statute which resulted in exemption for charitable facilities in the course of construction.[65] When viewed along with the strong dissent in *Cedars*, the similarity in the statutory language involved,[66] and the harshness of the *Cedars* conclusion, it is conceivable that the court was hesitant to adopt a line of reasoning subsequently changed by the legislature. The dissent objected to this analysis of *Cedars*, noting that the legislature may say what the law shall be, not what it is or has been.[67] While this argument seems sound, it overlooks the main purpose of the Iowa court in looking at decisions from other jurisdictions. The value of the *Cedars* case was not whether the case was correctly decided, but whether or not the reasons underlying the decision were applicable to the issue before the Iowa court. Thus the value of the case came not only from the decision reached but also from the subsequent action of the legislature based on the result thus reached.

Even more significant, however, is the fact that the Iowa legislature, as previously noted, had passed a statutory amendment not in effect at the time this controversy arose. The amendment exempted property under the statute during the course of construc-

62. 136 N.W.2d at 494-95 (dissenting opinion).

63. 217 Minn. 528, 14 N.W.2d 923 (1944).

64. 35 Cal.2d 729, 221 P.2d 31 (1950).

65. CAL. REV. & TAX CODE § 214.1. This section provides that as used in § 214,

> Property used exclusively for religious, hospital, or charitable purposes shall include facilities in the course of construction . . . together with the land on which the facilities are located. . . ."

The statute took effect the first Monday of March 1954. The constitutionality of this statute was contingent upon the passage of an amendment to the California constitution. The constitutional amendment was adopted at the general elections on November 2, 1954.

66. *Compare* IOWA CODE ANN. § 427.1(9) (1949) ("used . . . solely") *with* CAL. REV. & TAX CODE § 214 ("used exclusively").

67. South Iowa Methodist Homes, Inc. v. Board of Review, Iowa , 136 N.W.2d at 493-94 (dissenting opinion).

tion.[68] With the issue thus rendered moot in the future by this amendment, the court may have been reluctant to deny exemption where it was so clearly enunciated that the legislature felt such property should be exempt. In any event, it is submitted that the court in *South Iowa* has reached a just result.

In conclusion, it would appear that charitable property in course of construction should be exempt from taxation where such property will be exempt when completed and occupied. A strict construction of exemption statutes does not require an unreasonable result. The rule of strict construction does not require that "the narrowest possible meaning be given to words descriptive of exemption, for a fair and reasonable interpretation must be made of all laws, with due regard for the ordinary acceptation of the language employed and the object sought to be accomplished thereby."[69] When the construction given to a statute proves to be in derogation of the admitted purposes of that statute, it should be the rule of construction which retreats and not the objects of the statute. If the statute is designed to encourage the *formation* and proper growth of charities as well as to maintain their existence, no rule of construction should stand in the way. Statutes which are especially difficult to construe in favor of exemption for facilities in course of erection[70] might be replaced with language more susceptible to providing the needed flexibility to meet such issues. Perhaps the preferable result would be obtained by following California's solution which requires "use"[71] but specifically exempts facilities in course of erection.[72]

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68. IOWA CODE ANN. § 427.1(9) (1949) as amended by IOWA CODE ANN. § 427.1(9) (Supp. 1965). The amendment was approved on June 4, 1965 and will take effect July 4, 1966.

69. Cedars of Lebanon Hosp. v. Los Angeles County, 35 Cal.2d at 735, 221 P.2d at 35. See COOLEY, TAXATION, § 674 (4th ed. 1924).

70. See Pa. Stat. Ann. tit. 72, § 5020-204(1) (Supp. 1964) ("actual use and occupation"); N.J. STAT. ANN. § 54:4-3.6 (Supp. 1964). ("actually and exclusively used").

71. CAL. REV. & TAX. CODE § 214.

72. CAL. REV. & TAX. CODE § 214.1. It should be noted, however that as in California, such a solution may require not only a statutory change but also a constitutional amendment. Pennsylvania serves as a good example. In Mullen v. Commissioners of Erie County, 85 Pa. 288 (1877), affirming Erie County Commissioners v. Bishop, 13 Phila. 509 (1877), it was held that under the Act of May 14, 1874, P.L. 158, land upon which a church was in the course of construction was not exempt from taxation. To remedy the result reached in this case, the Act of June 4, 1879, P.L. 90, was passed. This Act provided that:

> Nothing in the act to which this is a supplement shall be taken as implying that any building, though incomplete or in the course of construction shall be subject to taxation, where said building was intended under provision of said act, to be exempt from taxation when completed.

The Act of June 4, 1879, P.L. 90 was declared unconstitutional in Pittsburgh v. Phelan, 11 Pa. Dist. 572 (C.P. 1901), as far as church property was concerned since the constitution provided that such property, in order to be

Finally, the fear expressed by the dissent[73] as to whether charitable intentions will ever be carried out can easily be provided for, thereby meeting one objection to the "intention to use" doctrine. For example, the land and partially completed building could be taxed, with a refund provided when the building is actually completed and used. Alternatively, the charity could post a bond in the amount of the taxes which would lapse when "actual use" commenced.

In order to prevent abuse, however, exemption of facilities in course of construction should be limited by a requirement that the work be carried out and the building be put in use within a reasonable time.[74] Furthermore only a *bona fide* intention, that is an intention manifested by the actual expenditure of money and carrying on of work, would appear to deserve exemption. The mere holding of land by a charitable institution, or purely nominal acts toward construction should not be sufficient.

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exempt, must be an actual place of religious worship. The court in Jewish Maternity Ass'n v. City of Philadelphia, 24 Pa. Dist. 307, 309 (C.P. 1915), in denying exemption to a hospital which was in course of construction at assessment date held that the Act of June 4, 1879, P.L. 90 was in conflict with the constitution as an expository act attempting to constrain the court to adopt a particular construction of a previously enacted statute and an "attempt to exempt a species of property which does not fall within any of the classes which the legislature is empowered to exempt." Thus the act was declared unconstitutional in its entirety, both as to religious property and charitable property.

73. South Iowa Methodist Homes, Inc. v. Board of Review, 136 N.W.2d at 494-95 (dissenting opinion).

74. See Village of Hibbing v. Comm'r of Taxation, 217 Minn. 528, 535, 14 N.W.2d 923, 926-27 (1944). Such a reasonable time limit would include the flexibility apparent in El Jebel Shrine Ass'n v. McGlone, 92 Colo. 334, 26 P.2d 108 (1933) in which the court recognized that the world-wide depression had prevented the completion of many similar buildings.