Recent Case Concerning the Interplay of a Municipal Sign Ordinance and Federal Law Protecting Religious Assemblies from Discriminatory Land Use Rules and Decisions

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In 2000, Congress unanimously passed a law known as the Religious Land Use and Institutionalized Persons Act to prevent cities and towns from using land-use regulations and zoning to discriminate against religious assemblies. The fundamental provision creating this rough accommodation between municipal interests in their planning and zoning matters and religious assemblies trying to find a home or change the manner in which they will use a property is the "Equal Terms" provision of the statute.

RLUIPA's "Equal Terms" section provides that "[n]o government shall impose or implement a land use regulation in a manner that treats a religious assembly or institution on less than equal terms with a nonreligious assembly or institution." Thirty-one words that, at least upon a first reading, seem relatively noncontroversial. Lawyers, of course, are skilled in the art of analyzing seemingly simple phrases until they become confusing jumbles subject to multiple differing interpretations. Such is the predicament in which the Equal Terms provision finds itself, having been interpreted differently by at least two (and, if you really want to get into the weeds, more) Federal Courts of Appeal. By its October 7, 2020, decision in *Signs for Jesus v. Town of Pembroke, NH*, the First Circuit has joined the fray.

> "Under the Eleventh Circuit's test, if a municipality allows any nonreligious entity to take an action under its zoning regulations (e.g. put up a sign, or locate in a specific zone), it must also allow a religious entity to take that action unless the differential treatment of the religious entity can satisfy strict scrutiny."

While the Third, Sixth, Seventh, Ninth, and Eleventh Circuits have all adopted their own slightly different tests to analyze Equal Terms challenges, the real dispute comes down to one basic distinction: should the Equal Terms provision be applied literally, or should municipalities only be required to treat religious entities equally with *similarly situated* nonreligious entities?

According to the Eleventh Circuit, the Equal Terms provision should be applied literally and broadly in favor of religious exercise. Under the Eleventh Circuit's test, if a municipality allows any nonreligious entity to take an action under its zoning regulations (e.g. put up a sign, or locate in a specific zone), it must also allow a religious entity to take that action unless the differential treatment of the religious entity can satisfy strict scrutiny. The Third Circuit, by contrast, has held that a religious entity is not entitled to be treated on equal terms with *every* nonreligious entity. Rather, under the Third Circuit test, a regulation will violate the Equal Terms provision only if it treats religious assemblies or institutions less favorably than secular

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comply with any of the Rev. Proc. 2019-38 guidelines.

What guidelines, then, *should* you follow in order to claim a section 199A deduction on your net real estate rental income without a significant risk of an IRS audit? I suggest the five guidelines below. As a former trial attorney for the IRS, I think the IRS will respect these guidelines. Obviously, however, I can't guarantee this result.

- First, as noted, you shouldn't use a triple-net lease agreement with your tenants, since, if you do, the IRS may claim that your rental business is, as noted, a mere passive investment or a hobby rather than a section 199A trade or business. Instead, your lease agreement should provide, among other things, that if your tenants need real estate maintenance or repairs, they themselves may not arrange for them. Instead, they must contact you, and you or your agents will provide them with these services promptly and for fair market charges.
- Second, you must keep reasonably accurate records concerning the types of real estate rental services that you and your agents perform for your tenants and the number of hours you and they devote to on these services. The services may include, as noted, property maintenance and repairs; they may also include advertising of available rental properties, interviewing and approving potential new tenants, negotiating real estate rental leases with them, and periodic inspections of the properties they rent from you. But an IRS General Counsel's Memorandum suggests that to be safe under section 199A, you should engage in relatively varied types of rental services in each relevant taxable year—say, three or more types.
- Third, you must spend enough time on your rental real estate business to make it reasonably likely that this business will be profitable. However, if you have good tenants who require very little of your time, one Tax Court case suggests that your rental real estate business must nevertheless be treated by the IRS as a section 199A trade or business and thus can qualify for a section 199A pass-through deduction under that section even if you spend as little as two hours a month on it.
- Fourth, a U.S. Supreme Court case suggests that you should engage in your real estate rental services "regularly and continuously."
- Fifth, you must not use any of your rental properties even occasionally as vacation properties for yourself and your family.

In short, to maximize the likelihood that the IRS will not challenge section 199A deductions you claim from your net real estate rental income on the grounds that your real estate rental business is not a section 199A trade or business, you need to do some careful planning, and you must provide your tenants, by yourself or through your employees, agents, or independent contractors, with a variety of real estate rental services. But in my view, if you follow the above five guidelines, you stand a very good chance of maximizing your section 199A pass-through deduction.

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entities that are similarly situated as to the regulatory purpose.

At first blush, the Eleventh Circuit test seems to make some sense. After all, the Equal Terms provision does not contain the words "similarly situated" or require a comparator. From a practical standpoint, however, the Eleventh Circuit's test raises some interesting issues (if you're a lawyer), several of which are illustrated by the *Signs for Jesus* case.

Signs for Jesus involved a church's request to replace its traditional wooden sign, on which it displayed scheduling and religious messages, with an "electronic changing sign," which could be manipulated from afar to project different religious messages and curricula to passersby. The Town of Pembroke's sign ordinance, however, bans electronic signs in the part of town where the church is located, the Limited Office District. Undeterred, the church applied for a permit to install an electronic sign. The town's code enforcement officer denied the permit, citing the ordinance. The church sought reconsideration of that decision and, alternatively, requested a variance from the Zoning Board of Adjustment. After the ZBA denied both requests, the church initiated an action in federal court claiming that the denials violated, among other laws, the RLUIPA Equal Terms provision. In support of its claim, the church argued that the town allowed three secular institutions to place electronic signs in the Limited Office District: a gas station (whose electronic sign was in existence prior to the adoption of the electronic sign provision and therefore constituted a lawful preexisting nonconforming use), the local School Administrative Unit (a subdivision of the state which, pursuant to RSA 674:54, is exempt from local zoning regulations), and the New Hampshire Department of Transportation (also exempt from local zoning regulations).

Rigid application of the Eleventh Circuit's test to the facts of the *Signs for Jesus* case leads to a potentially interesting result. Specifically, if government actors—nonreligious entities—are exempt from local zoning regulations, and religious entities cannot be treated on "less than equal terms" with *any* nonreligious entities, a case might be made that all religious entities are therefore also exempt from zoning. Does the existence of a secular nonconforming use in a particular district mean that every religious institution must be permitted to install an equivalent nonconforming use? The result, in the end, is that religious entities are not treated equally with secular entities. Rather, when compared with non-governmental secular entities, or secular entities that do not enjoy rights associated with a nonconforming use, religious entities are actually treated *more favorably*.

Perhaps recognizing this concern, the First Circuit threw its lot in with the Third Circuit, finding that none of the secular institutions identified by the church (the gas station, the school, or the DOT) constituted appropriate "comparators" for purposes of an Equal Terms claim. The Court quoted and affirmed U.S. District Court Judge Paul J. Barbadoro's opinion, in which he noted that the governmental actors – Pembroke Academy and NH DOT – were not viable comparators "because the State has deprived the Town of any power to regulate governmental land uses." As a result, the sign ordinance's exemption for these "legally required" signs "merely reflects Pembroke's lack of authority to regulate governmental land use." Nor was the gas station sign a proper comparator: the town was still disabled from regulating the gas station sign, but by a different legal regime, one that allows lawful preexisting nonconforming uses to continue indefinitely.

For the time being, we now have certainty as to how the First Circuit—and Federal District Courts for New Hampshire, Maine, Massachusetts and Puerto Rico—will interpret the Equal Terms provision. That said, it may only be a matter of time before the Supreme Court will settle this issue once and for all.

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Mr. Cole and Ms. Carrier represented the Town of Pembroke in the zoning board and the ensuing litigation described in this article.