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## Coates' Canons Blog: The Two Key Questions for Property Tax Exemptions

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Which of these properties is likely to be exempt from local property taxes?

- A. Vacant, unused land owned by Dook University, a private educational institution. Dook plans to build a new science lab on the land once it raises the necessary funds.
- B. A bookstore owned by the Church of the Good Shepherd. The bookstore is located immediately next to the church's sanctuary and sells religious books primarily to its congregation, although it is open to the general public.
- C. An office building owned by the town of TarHeelville, which leases it to a private law firm.

I think the answer is: not A, maybe B, definitely C. Here's why. Except for property owned by a government, North Carolina property tax exemptions depend on both the *ownership* and the *use* of the property. This fact means that before you can determine whether an exemption applies, you must first answer two key questions:

1. Who owns the property?
2. How is the property being used?

Of the "big four" exemptions (government, religious, educational, and charitable), three require that the property in question be owned by an exempt organization *and* be used by that owner for an exempt purpose. Only the government exemption ignores the use question.

In other words, if property owned by a religious, educational or charitable organization is not used for a religious, educational or charitable purpose, then it isn't exempt from property taxes. See GS 105-278.3, -278.4, -278.7, respectively.

In example A above, Dook's vacant land fails the use requirement. Possible *future* educational use of the property does not justify an exemption.

More difficult exemption cases such as example B above involve land that is being used by the owner for an activity that is related to but not necessarily part of its core religious, educational, or charitable purpose.

The N.C. Court of Appeals tackled this issue in 1994 when it concluded that a day care center operated by a charitable hospitable was "reasonably necessary" to accomplish the institution's charitable purpose and therefore exempt. In the *Moses H. Cone Memorial Hospital* case, 113 N.C. App. 562, the court accepted the hospital's argument that in order to recruit and retain qualified employees it needed the day care center, which was open around the clock and available only for children of hospital employees.

Similarly, in 2007 the Property Tax Commission found that a retail store operated by Habitat for Humanity was reasonably necessary to accomplish its charitable purpose because the store served as a collection point for donated items and provided the opportunity for future Habitat homebuyers to work in the store as part of their required "sweat equity." *In re: Appeal of Habitat for Humanity of Charlotte, Inc., 06 PTC 242.*

In example B, would property used by a church for a bookstore satisfy this standard? I think so, especially considering that GS 105-278.3 defines "religious purpose" to include worship as well as "activities that demonstrate and further the beliefs

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and objectives of a given church or religious body.”

But the more commercial the activity, the less likely it will support an exemption. Seventy years ago the N.C. Supreme Court observed that property held for religious, educational, or charitable purposes “is supposed to be withdrawn from the competitive field of commercial activity . . . But when it is thrust into the business life of the community, it loses its sheltered place, regardless of the characteristic of the owner, for it is then held for profit or gain.” *Rockingham County v. Bd. of Trustees of Elon College*, 219 N.C. 342 (1941).

In that case, the court concluded that commercial real estate owned by Elon College was not exempt despite the fact that the *income* from the property was used for educational purposes. The court held that the educational exemption required that the property itself be used for educational purposes. This same reasoning also would apply to the use requirement found in the religious and charitable exemptions.

Assuming that the bookstore in example B is a modest little endeavor open only a few hours a week and catering primarily to the church’s congregation, almost certainly the property would qualify for an exemption. But were the bookstore a huge operation open every day and selling lots of stuff to customers with no connection with the church, the commercial nature of the activity could threaten the exemption.

These decisions will be extremely fact dependent. Before ruling on questionable exemption applications, assessors and their staffs should gather all relevant information and visit the properties in question.

Example C is the easiest one to deal with because it involves government property, the only one of the big four exemptions for which use is irrelevant. GS 105-278.1 makes no reference to how the property is being used. As a result, all property owned by a federal, state or local government is exempt from local property taxes.

This includes government property being used for commercial purposes, as in example C. The office building will never be taxable in the hands of TarHeelville. But the leasehold interest in that office building could be taxable in the hands of the law firm that is leasing the space.

A leasehold interest in exempt property is one of only two types of intangible property that is subject to property tax, the other being certain computer software. For a discussion of how to value this intangible property, [click here](#).

One final note concerning property tax exemptions: remember that these exemptions apply to property taxes and not necessarily to any other taxes or fees charged by your local government. It’s true that the federal and state governments are generally exempt from all local taxes. But religious, educational and charitable organizations are *not* automatically exempt from other taxes and fees. Privilege license taxes, for example, should be levied on these organizations if their commercial activities fall under one of your privilege license tax categories and your ordinance does not specifically exempt such organizations. The fact that a church or a school or a non-profit is exempt from property taxes does not mean that organization is also exempt from other taxes and fees.

## Links

- [www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.1](http://www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.1)
- [www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.3](http://www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.3)
- [www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.4](http://www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.4)
- [www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.7](http://www.ncga.state.nc.us/gascripts/statutes/statutelookup.pl?statute=105-278.7)
- [www.dorn.com/taxes/property/decisions/scans/mecklenburg/Habitat%20for%20Humanity%20of%20Char.,%2006PTC242,%20Order%20&%20Final%20Dec.pdf](http://www.dorn.com/taxes/property/decisions/scans/mecklenburg/Habitat%20for%20Humanity%20of%20Char.,%2006PTC242,%20Order%20&%20Final%20Dec.pdf)
- [canons.sog.unc.edu/?p=3701](http://canons.sog.unc.edu/?p=3701)