

DC Circ. Mulls Tax-Exempt Status For Ayahuasca Church

By **Sam Reisman**

Law360 (March 11, 2024, 6:04 PM EDT) -- A D.C. Circuit panel on Monday pushed counsel for an Iowa church that uses the psychedelic substance ayahuasca in its ceremonies to explain why the Internal Revenue Service erred in denying it tax-exempt status.

The appeal touches on friction between the federal tax code, the Controlled Substances Act and the Religious Freedom Restoration Act, with appellant Iowaska Church of Healing asserting that its proposed use of ayahuasca was sincere and religious and public policy favored treating the organization no differently than any other church.

Oral arguments held Monday regarding Iowaska Church of Healing's appeal pivoted on whether the IRS correctly applied its discretion to deny nonprofit status to the church simply because it planned to distribute a controlled drug to its members.

Simon A. Steel of Dentons, an attorney for Iowaska Church of Healing, told the panel that the lower federal district court, which sided with the IRS in dismissing the church's case, erred in its interpretation of the interaction between the three statutes in play.

Steel also asserted that the church was organized as a law-abiding entity, modeled on another church whose religious ayahuasca use was ultimately vindicated in court, and had standing to sue because it had suffered an economic injury due to the IRS' refusal to recognize it as an exempt organization under [Internal Revenue Code Section 501\(c\)\(3\)](#). 

"The one controversial purpose here — the ayahuasca tea sacrament — is a sincere exercise of religion protected by RFRA," Steel said. "The IRS has never disputed that in this case."

The use of the psychoactive substance ayahuasca "stems from millennia-old North and South American indigenous practices originating in the Amazon basin, and has been practiced for decades in the United States, Asia, Europe and South America by churches that blend elements of indigenous shamanism with Christianity and Afro-Brazilian religious practices," according to the church's brief.

The brew contains the psychedelic DMT, which is a Schedule I substance under the federal Controlled Substances Act.

Steel said the 2006 U.S. Supreme Court ruling in [Gonzales v. O Centro Espirita Beneficente Uniao do Vegetal](#),  in which the justices unanimously found that a New Mexico church's use of ayahuasca was protected by RFRA, indicated that the federal government was misguided in its assertion that Iowaska needed to exhaust its administrative remedies before turning to the courts to exercise a religious right.

Judge Harry T. Edwards countered by saying the IRS took the position that the church's proposed activity violated public policy and that the agency was therefore correct to reject the request for tax exemption.

"They are simply saying that, under the authority that we have to exercise, we can't grant an exemption," Edwards said. "It is the law of the land, whether you think it should or should not be the law of the land."

Speaking of the IRS, Judge Edwards added later, "They haven't done anything that's inconsistent with the law, and they're following the law."

The appeal follows a March 2023 ruling in D.C. federal court from U.S. District Judge Beryl Howell, who said that as long as the church planned to violate the Controlled Substances Act, it could not be classified mainly as a religious group.

In 2019, Iowaska applied for tax-exempt status from the IRS, but the agency declined on the basis that its sacrament broke federal law, according to court documents. The IRS also made its denial on the grounds that Iowaska was not exclusively organized for religious purposes.

Kathleen E. Lyon of the U.S. Department of Justice's Tax Division, an attorney representing the government parties, told the panel Monday, "Unless Iowaska can show that the prohibitions in the Controlled Substances Act do not apply to it, it cannot carry its burden of showing that it is [organized for] a tax-exempt purpose."

Lyon said the burden was on the church to demonstrate that its activities were lawful, not on the IRS to assess the sincerity of Iowaska's religion. Iowaska would need to secure a religious exemption to the CSA from the Drug Enforcement Administration, a request that the DEA is currently reviewing, Lyon told the appellate panel.

"Iowaska's problem here is not an administrative exhaustion problem, it is an authority problem," Lyon said. "The IRS does not have the authority to make the determination that they want it to make. They're seeking the wrong remedy here, against the wrong agency."

In his rebuttal, Steel told the panel, "The issue here isn't who has the burden of proof. The issue here is when there is a genuinely and substantially disputed question of what public policy, as determined by Congress in both the CSA and RFRA, requires, how is the IRS to resolve that question?"

Steel said under the precedent set by the 1983 U.S. Supreme Court decision in [Bob Jones University v. United States](#), the IRS could only reject a religious application for tax-exempt status from an organization if there was "no doubt" that it was organized for an illegal purpose.

Judge Edwards asked, "Would you agree if I think, as a judge, if I think that there is 'no doubt' that this violates CSA public policy, you lose?"

"Correct," Steel responded. "I agree."

Earlier in arguments, Steel said the church did not concede that the sacrament violated public policy, noting that, with the passage of RFRA, Congress protected religious activity from government interference, subject to the rigorous "strict scrutiny" standard.

Judges Karen LeCraft Henderson, Robert L. Wilkins and Harry T. Edwards sat on the panel for the D.C. Circuit.

The Iowaska Church of Healing is represented by Simon A. Steel, William A. Boatwright and Kenneth J. Pfaehler of Dentons.

The government parties are represented by Kathleen E. Lyon of the U.S. Department of Justice's Tax Division.

The case is Iowaska Church of Healing v. Werfel et al., case number 23-5122, in the U.S. Court of Appeals for the D.C. Circuit.

--Additional reporting by Jonathan Capriel and Anna Scott Farrell. Editing by Stephen Berg.