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WHAT THE NONPROFIT LEADER NEEDS TO KNOW ABOUT THE LOBBYING RULES FOR CHARITIES An Explanation of the Rules under the 1976 Lobby Law *by Thomas A. Troyer*

I. Introduction

A. Background.

The final lobbying regulations published by the IRS on August 31, 1990 represented the culmination of an effort, begun in the early 1970's by a large and diverse group of public charities, to develop rules more favorable for charities than the "substantial part" test of section 501(c)(3) of the Internal Revenue Code.

1. In the latter 1960's and early 1970's the IRS received considerable publicity for its challenges to, and denials of charities' exemptions on the grounds of "substantial" lobbying activities.
2. That publicity generated a good deal of anxiety in the charitable community.
3. From 1971 to 1976 charities were quite active in working with Congress to develop curative legislation.
4. And the legislation finally enacted in 1976 — the law which added sections 501(h) and 4911 to the Internal Revenue Code and which the final regulations interpret — was very much a product of the needs, the objectives, and the support of the charitable community.

B. The statute as enacted is elective.

1. The election is very simply made — by filing a one page form with the IRS.
2. And it can be terminated by a public charity at will.

But the effect is that, unless a public charity elects to have the 1976 lobbying rules apply to it, it remains subject to the substantial part test of prior law.

C. With the publication of the final lobbying regulations, the fundamental decision facing most public charities throughout the country is whether to elect to be governed by the new rules.

D. A number of prominent national, state, and local public charities have made the election or are in the process of deciding to do so. And a variety of other state and local charities, are included: Boys' Clubs, Girl Scout groups, Girls' Clubs, organizations concerned with people with disabilities and the victims of particular diseases, and many others.

E. But for several reasons, generally having nothing to do with the merits, the great preponderance of eligible public charities throughout the United States have not elected.

F. To assess the desirability of the election, one must both understand the 1976 rules, as explained by the 1990 regulations, and compare them with considerations which apply under the substantial part test.*

G. First, though, let us turn our attention to understanding the new rules — in broad, general outline.

H. In summary, the rules —

1. Make most public charities eligible to elect
2. Have two principal effects:
 - a. In making lobbying expenditures the sole test of the permissibility of lobbying, they establish specific dollar allowances for a charity's lobbying expenditures, and
 - b. They provide five useful exceptions from "influencing legislation."
3. Create a system highly protective of private foundation grants to lobbying public charities.
4. Contain other provisions, of more limited application.

I. A more detailed description of the rules appears in "Final Lobbying Regulations Provide Workable Guidance," by Walter B. Slocombe, and Eileen Mallon, in the February 1991 issue of the *Journal of Taxation*, pp. 124-130.

II. Eligibility for the rules.

A. The rules are available only to public charities.

1. They do not apply to private foundations — either operating or non-operating.
2. They have important secondary ramifications for private foundations which make grants to public charities.
3. But they do not by their terms apply to private foundations.

B. Among the public charities, the rules are not available to churches or their integrated auxiliaries.

C. Consequently, the principal availability of the rules is to —

1. Publicly supported organizations — groups like the YMCA, the United Way, national health and environmental organizations, state and local affiliates of such organizations, and the great variety of other charitable organizations, large and small, which normally derive a substantial part of their financial support from the general public.

* For convenience, the outline hereafter refers to the 1976 rules, as so explained, as the "rules."

2. Organizations such as museums, symphonies, and parks, which normally derive their support from a combination of fees for their exempt activities and public contributions.
- 3 . Colleges, universities, and other schools.
4. Hospitals and medical research organizations.
5. And satellite or support organizations of public charities.

III. Where they apply, the lobbying rules have two principal effects:

- First, they permit electing public charities to spend certain parts of their budgets each year to influence legislation.
- Second, they provide exceedingly helpful exceptions to the key term "influencing legislation."

A. The expenditure allowances.

1. Under the rules, the sole test of the permissibility of an organization's lobbying is the amount of money it spends for lobbying purposes.
—None of the various other factors relevant under the substantial part test — volunteer time, the importance of the lobbying effort, and the rest — have any application to an electing charity.
2. The rules specify that an electing public charity can spend up to 20% of the first \$500,000 of its "exempt purpose expenditures" (that is, its annual budget, with certain adjustments) each year to attempt to influence legislation.
3. The percentage allowances decline from that level as the charity's annual exempt purpose expenditures rise, ending at 5% of such expenditures over \$1.5 million.
4. The rules provide an overall ceiling of \$1 million for the lobbying expenditures of any one charity in any one year.
5. The effect of this sliding scale is that a charity reaches the maximum permitted ceiling when its exempt purpose expenditures exceed \$17 million.
6. Expenditures for grass roots lobbying (explained below) are limited to one-fourth of the overall expenditure allowances.
7. The other three-fourths can be spent only for direct lobbying.

B. The following chart shows the expenditure allowances at all levels:

Exempt Purpose Expenditures	Total Ceiling	Grass Roots Ceiling
Up to \$500,000	20%	5%
\$500,000 to \$1,000,000	\$100,000 + 15% of excess over \$500,000	\$25,000 + 3.75% of excess over \$500,000
\$1,000,000 to to \$1,500,000	\$175,000 + 10% of excess over \$1,500,000	\$43,750 + 2.5% of excess over \$1,000,000

\$1,500,000 to \$17,000,000	\$225,000 + 5% of excess over \$1,500,000	\$56,250 + 1.25% of excess over \$1,500,000
Over \$17,000,000	\$1,000,000	\$250,000

C. If an organization exceeds any of these designated levels in a particular year, the excess expenditure becomes subject to a 25% excise tax.

1. But the organization does not lose its tax exemption and its qualification to receive deductible charitable contributions; and its managers never become subject to penalty tax by reason of the lobbying activities.
2. Under the rules, an electing public charity loses its exemption only if the sum of its lobbying expenditures, over a moving four-year computation period, exceeds its overall or grass roots ceilings for that entire period by more than 50% — so that a charity can exceed the ceilings for one or more years, pay some excise tax on the amount of the excess expenditures, but retain its exemption so long as it does not go beyond the limits by an aggregate of more than 50% over the four year period.

D. Definitions.

1. "Legislation" includes both introduced bills and specific legislative proposals.
 - a. It does not include general legislative concepts, approaches, or principles which have not been reduced to a specific legislative proposal.
 - b. Quite helpfully, the definition excludes rules adopted by a range of special purpose bodies, such as school boards, housing authorities, water districts, and zoning boards.
2. "Direct lobbying" is defined as direct communication with legislative bodies, members and employees of such bodies, and other government personnel who participate in the formulation of legislation where the communication —
 - a. Refers to specific legislation, and
 - b. Reflects a view on that legislation.
 (Very helpfully for the increasing number and variety of public charities which have reason to participate in initiative or referendum campaigns, such participation is defined as direct lobbying — so that the charities' expenditures in such campaigns are applied against the full expenditure allowances, not the lower grass roots allowances.)
3. The definition of "grass roots lobbying" — communications with the general public on legislative matters — is also consciously generous for electing charities.
 - a. To be within the definition, a communication to the public must:
 - (i) Refer to specific legislation,
 - (ii) Reflect a view on the merits of that legislation, and
 - (iii) Generally, urge its recipients to lobby, or press others to lobby.
 - b. The third of those conditions is of critical importance.
 - c. It has come to be known as the requirement of a "call to action."

d. The breadth of freedom it permits public charities to communicate views on legislative matters to the general public — without having any of the associated expenses counted against their expenditure allowances — is illustrated by an example in the regulations:

"The State Assembly is considering a bill to make gun ownership illegal. This outrageous legislation would violate your constitutional rights and the rights of other law abiding citizens. If this legislation is passed, you and your family will be criminals if you want to exercise your right to protect yourselves."

e. The regulations conclude that this communication is not grass roots lobbying because it does not call upon the public to lobby.

4. "Exempt purpose expenditures" — the base to which the percentage allowances are applied — consist of a charity's entire budget, adjusted as follows:
 - a. Certain fundraising expenses are excluded.
 - b. The costs of earning investment income and carrying on an unrelated business are excluded.
 - c. Capital expenditures are included only to the extent of straight-line depreciation and similar allowances.

IV. There are five exceptions from the term "influencing legislation."

A. In general, they are exceedingly useful for charities making the lobbying election. They rule out of the term "influencing legislation" a number of important kinds of legislatively oriented activities which might well — indeed, in most cases clearly would — otherwise be considered within this exception. And where a charity's activity is within one of the exceptions, none of the charity's costs in carrying it on count as legislative expenditures, to be applied against its expenditure allowances.

B. A broad and highly important exception applies to making available the results of nonpartisan analysis, study, or research on a legislative issue.

The final regulations make clear that such research and analysis need not be neutral to be within this exception. On the contrary, they provide that materials consisting of plain legislative advocacy can qualify. The exception applies to material that takes a clear position on the merits of specific legislation,

1. So long as it contains a sufficiently full and fair exposition of the facts to enable the audience to form an independent opinion;
2. So long as the organization makes the material generally available; and
3. For grass roots communications, so long as the material does not include a direct call upon the audience to contact legislators.

This exception permits robust argument for or against specific legislation where the argument presents the facts fairly and seeks to persuade its audience by rational means (and the other conditions noted above are met). Even before the adoption of the final regulations, the exception (included in the proposed regulations) had proved to be widely useful for electing public charities.

C. A second very important exception is one for membership communications. A charity's communication with its members — by magazine, newsletter, conference, or any other method — is not influencing legislation unless it "directly encourages" its members to lobby. Here again, the organization's communication can comment on pending legislation, evaluate it, and take a position on it so long as the statement does not tell members to lobby legislators — or urge others to lobby.

D. A third important exception excludes charities' discussion of broad social, economic, and similar policy issues whose resolution would require legislation — even if specific legislation on the matter is pending in a legislative body — so long as the discussion does not address the merits of specific legislation.

E. A fourth, narrower exception permits charities to respond to written requests from a legislative body, committee, or subcommittee for technical advice on pending legislation.

F. A fifth exception, also much narrower than the first three, allows electing charities to engage in direct lobbying on matters affecting their own powers, duties, tax exempt status, or the deduction of contributions to them.

G. Overall, the exceptions are an exceedingly important part of the law and the regulations.

1. All are helpful.
2. The first three eliminate from "influencing legislation" important categories of activity that plainly aim for legislative effect.

V. Special rules for private foundations.

A. When the lobbying rules first became effective (at the beginning of 1977), both public charities and private foundations were concerned that the special ban on private foundation lobbying would preclude foundations' grants to public charities conducting lobbying.

B. Following and expanding upon a 1977 IRS ruling addressed to the problem, the final regulations establish a highly protective system for private foundation grants to public charities that lobby.

C. Under the system, so long as a private foundation's grant is not "earmarked" for lobbying, a foundation may make a general purpose grant to a lobbying public charity without penalty tax liability for the foundation.

D. A private foundation may also make a grant to support a specific public charity project that includes lobbying, so long as the grant –

1. Is not earmarked for lobbying, and
2. Is not greater than the amount budgeted by the grantee for the nonlobbying portion of the project.
3. For example, where a public charity seeks foundation funding for a \$100,000 project, of which \$20,000 will be for lobbying, a private foundation could, theoretically, make a non-earmarked grant of up to \$80,000 to support the project.
4. Prudent foundations will allow themselves some cushion below the theoretically permissible grant, but the example illustrates the latitude of the rule.

E. The final lobbying regulations provide very helpful administrative rules for private foundations making such grants.

1. They specify that the foundation may, generally, rely on the budgetary information furnished to it by the prospective grantee.
2. They make clear the grantmaking foundation need not insist on a detailed description of the grantee's proposed lobbying expenses.
3. The grantmaker need have only general budgetary information and a statement signed by one of the grantee's officers regarding its planned lobbying expenditures.
4. Once the grantmaking foundation has complied with these rules, the grant will not become a taxable expenditure for the foundation if the public charity later violates the terms of its grant application.

VI. Other aspects.

A. The final regulations have special rules for the subsequent use, for lobbying purposes, of research or other preliminary work; paid lobbying advertisements in the mass media on pending legislation well known to the general public; affiliated organizations; the allocation of expenses of communications made partly for lobbying and partly for nonlobbying purposes; and transfers to organizations not described in section 501(c)(3).

B. The mass media rule is of quite limited practical application.

C. The other rules apply in practice to special sorts of situations, and one should have a general awareness of them.

D. All are explained in "Final Lobbying Regulations Provide Workable Guidance," *Journal of Taxation*, February 1991, beginning at page 124.

VII. Conclusion.

A. The rules are of much broader utility than is generally recognized.

1. They are helpful not only for major national organizations which lobby Congress regularly.
2. They are useful also for local, municipal, county and state organizations which would like to obtain a city ordinance on smoking or drug education, a county council

measure assisting the handicapped, a state law on an environmental problem, and the almost endless permutations of these examples.

B. A major reason that the great preponderance of eligible public charities did not elect the rules immediately after the enactment of the 1976 law was that they wanted to see the regulations before they made their decisions.

1. The adoption of the final regulations eliminates that cause for deferral of the decision.
2. And the regulations make the election attractive.
3. In many respects, the election is more attractive than it might have appeared from the language of the statute itself.
4. In the main, the final regulations are liberal; their examples clarify the rules considerably; and the rules are as plain and specific as the situations to which they apply permit.

C. Another ground for failure to elect was that many large organizations assumed, or were advised, that their size alone was sufficient to protect them under the substantial part test.

1. During the years of development of the final regulations, we have learned a great deal more about the variety of factors which the Internal Revenue Service may take into account in applying the substantial part test.
2. Some apply entirely without regard to the size of the organization.
3. Hence, it is clear that size alone does not protect the tax qualification of an organization.
4. However, some very large organizations with major programs of activities which constitute “influencing legislation” – even after application of all of the exceptions and special definitional provisions of the rules – may regularly exceed the expenditure allowances; and for them there is no choice but to attempt to live with the uncertainties of the “substantial part” test.

D. A third — pervasive and important — reason for the failure of a great many eligible public charities to make the election has been the stock response of lawyers and other tax advisors, developed and ingrained over many years, that anything even remotely approaching lobbying is very dangerous for a charitable organization.

E. That view is simply wrong now — and dangerously misleading.

F. All practitioners who represent eligible public charities should understand that.

G. The adoption of the final lobbying regulations was a seismic event in the Internal Revenue Code rules governing lobbying by public charities.

H. And that event created a very sharp tilt in the legal terrain — toward electing the lobbying rules.

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