"Are You Ready for Some (Political) Football?"
How Section 501(c)(3) Organizations Get Their Playing Time During Campaign Seasons

Daniel C. Willingham

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“ARE YOU READY FOR SOME (POLITICAL) FOOTBALL?” HOW SECTION 501(c)(3) ORGANIZATIONS GET THEIR PLAYING TIME DURING CAMPAIGN SEASONS

Daniel C. Willingham*

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The Tax Code makes charitable organizations exempt from taxation because they perform services that would otherwise be left to the government. However, there is great concern that charitable organizations could be used for non-charitable purposes, including as a means to influence election outcomes and the legislative process. Even

1. H. Rep No. 1860, 75th Cong. 3d Sess. 3, 3-4 (1939). This report is summed up by the following quote: “The Government is compensated for the loss of revenue by its relief from financial burden which would otherwise have to be met by appropriations from public funds, and by the benefits resulting from the promotion of the general welfare.” Id. at 19.

2. Nancy E. McGlamery & Rosemary E. Fei, Taxation with Reservations: Taxing Nonprofit Political Expenditures After Citizens United, 10 ELECTION L. J. 449, 452 (2011). See also Lloyd Hitoshi Mayer, What Is This 'Lobbying' That We Are So Worried About?, 26 YALE L. & POL’Y REV. 485, 486-89 (2008). Mayer provides a comprehensive look at limitations placed on lobbying activities through the Tax Code as well as other legislation. Mayer argues these limitations are the result of our society's negative view of lobbyists. However, this view is not persuasive in the context of the Tax Code. Society’s unfavorable perception of lobbyists may in part help maintain the limitation on tax-exempt organizations engaging in lobbying, but other activities, including commercial activities and private inurement, are prohibited for tax-exempt organizations as well even though there is no pejorative view of either business activities or an individual earning income. Thus, in the context of tax-exempt organizations, lobbying activities are just another item on the list of endeavors that are not “charitable.” Id.

Even the ban on campaign activities appears to have nothing to do with the public’s lowly view of lobbying or politics. Another, more pragmatic, political reason why Mayer’s analysis does not fit the Tax Code restrictions with respect to campaign activities comes from the legislative history of this ban. The prohibition was merely convenient for the powerful Senate Minority Leader Lyndon Johnson at the time Congress passed this legislation. See infra notes 24-27 and accompanying text.

in the early nineteenth century Alexis de Tocqueville observed in *Democracy in America* that “[t]he two chief weapons that [political] parties use in order to obtain success are the newspapers and public associations.”

Still, the Tax Code makes such abuse difficult by imposing significant limitations on the ability of charitable organizations to obtain and keep their tax-exempt status when they engage in political campaign activities and lobbying.

Charities are, no doubt, crucial to the everyday activities of American society. Charities perform vital functions that strengthen communities, improve the quality of life for all citizens, and lessen the government’s burden to provide numerous necessary services. Common charitable organizations include schools, museums, community theatres, conservation groups, organizations that help the poor and homeless, churches, and hospitals. Therefore, without charities, much of our population would be uneducated, uncultured, self-centered, unsophisticated, and physically and emotionally unhealthy. Thus, although one may oppose the mission of a few select charities, it is nonetheless difficult to downplay the necessary role of charities on a collective basis.

Charities have long enjoyed tax advantages because they provide such important benefits to society. The first statute granting tax benefits to charitable organizations in the United States was the Wilson-Gorman Tariff Act of 1894. This legislation established a two percent corporate...
tax rate. In addition, it exempted from this tax "[c]orporations, companies, or associations organized and conducted solely for charitable, religious, or educational purposes, including fraternal beneficiaries." Although the United States Supreme Court quickly struck down this statute in *Pollock v. Farmers' Loan & Trust Co.*, Congress had ignited the trend of carving out favorable tax treatment for charitable organizations.

The Corporate Income Tax Act of 1909 marked another attempt by Congress to pass legislation to benefit charitable organizations. This time the legislation was upheld as the Populist Movement, which favored taxing businesses to provide more government services to individuals, gained traction in the mainstream political climate. In addition to allowing the tax-exemption for charitable organizations, however, the 1909 statute also contained language prohibiting the exemption for organizations that distribute earnings and profits in a

Note that granting tax-exempt status for organizations engaged in charitable work was not uniquely an American phenomenon. It appears that, like much of America's legal tradition, this piece was borrowed from England. In 1274, England granted an exemption from papal taxation to hospitals established to treat leprosy. See generally W.E. Lunt, *A Papal Tenth Levied in the British Isles from 1274 to 1280*, 32 ENG. HIST. REV. 49-89, 86 (1917).

One English scholar explains the charitable tax-exemption on the grounds that, "beginning with the fifteenth century the State, in most cases the municipalities, took over the function of administering charity, and that consequently it was thought that property devoted to a public use should be freed from the burden of taxation." See generally Philip Adler, *Historical Origin of the Exemption From Taxation of Charitable Institutions, in Tax Exemptions on Real Estate An Increasing Menace: A Study by the Westchester County Chamber of Commerce* 54 (1922).


8. Id.
10. Pub. L. No. 53-227, 28 Stat. at 556. See also Pollock, 157 U.S. 429. The Court held that the taxes imposed by the Wilson-Gorman Tariff Act of 1894 were unconstitutional on the grounds that they resulted in a direct tax that was not apportioned. Id. See also U.S. CONST. art. I § 2, cl. 2. Requiring that direct taxes imposed by the federal government be apportioned among the states. Id.
12. Some commentators argue that, by this time, the Populist Movement was co-opted by the Democratic Party. Although co-option hurt this movement by diluting it, co-option helped the movement by giving it mainstream credibility. For further discussion on the Populist Movement during this era, see LAWRENCE GOODWYN, THE POPULIST MOVEMENT: A SHORT HISTORY OF THE AGRARIAN REVOLT IN AMERICA (1990).
manner similar to a corporation paying dividends to shareholders. This became known as the private inurement limitation.

The ratification of the Sixteenth Amendment in 1913 and the passage of the Revenue Act of 1913 established the modern federal income tax for individuals. This Constitutional provision created the federal income tax for individuals. This legislation kept the charitable exemption provision from the 1909 legislation, and also added a tax deduction for individuals who made contributions to charitable organizations. Similar deductions for estates and corporations followed in 1918 and 1936, respectively.

In 1919, the first limitation on political involvement was created. This came when the Treasury Department issued regulations that denied the exemption for "organizations that disseminated controversial or partisan propaganda." Congress further developed the limits on political involvement in the Revenue Act of 1934. This act established the "substantial part" test for organizations "organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes." This limit barred significant lobbying activities by stating that "[n]o substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation." If an organization failed the "substantial part" test under this regime, it was subject to penalties, including the possible loss of the tax-exemption, and donors could not deduct their donations.

13. Id.
14. This limitation is now defined in Treas. Reg. § 1.501(c)(3)-1(c)(2) (2008), which explains that an organization is not allowed tax-exempt status "if its net earnings inure in whole or in part to the benefit of private individuals." Id.
15. U.S. CONST. amend. XVI. The language of this provision states that, "Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration." Id. See also Revenue Act of 1913, Pub. L. No. 16, 83 Stat. 114 (1913). Contra note 10 and accompanying text.
16. U.S. CONST. amend. XVI.
18. Id.
21. Haswell, 500 F.2d at 1140.
22. Id. at 1136. The 1934 legislation appears, in part, to be a response to Slee v. Commissioner, 42 F.2d 184 (1930). In this case, the Second Circuit ruled that the American Birth Control League was not entitled to tax-exempt status because it engaged in significant campaign and lobbying activities. Slee, 42 F.2d at 185. The court reasoned that, since the organization devoted substantial efforts to distributing materials to the public and legislators to shape public opinion and change laws that banned contraceptives, its purpose was not exclusively charitable,
In the middle of the twentieth century, members of Congress grew concerned that the contemporary application of the “substantial part” test left the door open for organizations to engage in excessive campaign activities and lobbying.\textsuperscript{23} This was particularly true for then Senate Minority Leader Lyndon Johnson, who had won election to the Senate in 1948 by a dangerously slim margin in the Democratic primary and feared that anti-Communist Section 501(c)(3) groups would campaign against him in 1954, thereby robbing him of reelection.\textsuperscript{24} This fear of excessive campaign and lobbying activities moved both Congress and the United States Supreme Court to seek a more neutral position with respect to those activities.\textsuperscript{25}

Congress, directed by Johnson, enacted the first piece of legislation prohibiting charities from supporting any political campaign in 1954.\textsuperscript{26} This statute kept the “substantial” test for lobbying.\textsuperscript{27} In addition, the

\begin{itemize}
  \item educational, or scientific. \textit{Id.}
  \item 23. Arnsberger, Ludlum, Riley, & Stanton, \textit{supra} note 6.
  \item 24. For an overview of the 1948 election, see \textit{ROBERT A. CARO, THE YEARS OF LYNDON JOHNSON: MEANS OF ASCENT}, 318-25, 327-49, 359-84, 394-95 (1990). Caro points out that Johnson won a tightly-contested runoff election in the Democratic primary against the highly-renowned former governor of Texas, Coke Stevenson. \textit{Id.} After many allegations of fraud against both Johnson and Stevenson, the Democratic State Central Committee named Johnson the victor by a narrow margin of eighty-seven votes. \textit{Id.}
  \item Regarding Johnson’s ulterior motives for excluding charities from all campaign activities, see James D. Davidson, \textit{Why Churches Cannot Endorse or Oppose Political Candidates}, \textit{40 REV. OF RELIGIOUS RES.} 16 (1998). This article provides an in-depth look at the political currents, including the opposition Johnson anticipated in the 1954 general election campaign for United States Senate from right-wing groups such as Facts Forum and the Committee for Constitutional Government. \textit{Id.} These perceived obstacles led to Johnson’s enthusiastic support for the 1954 amendment. \textit{Id.}
  \item 25. Although the neutrality doctrine was gaining a stronger foothold by the 1950s, it was by no means new. Prior to 1950, courts had interpreted the previous Tax Code provisions as a means to seek neutrality. See Judge Learned Hand’s opinion in \textit{Slee}, 42 F.2d at 185. In this case, Judge Hand wrote, “[p]olitical agitation such as this is outside the statute, no matter how innocent the aim . . . Controversies of that sort must be conducted without public subvention; the Treasury stands aside from them.” \textit{Id.}
  \item 27. \textit{Id.} Note that Johnson made clear that Congress was attempting to make the federal government neutral in such activities when he said the statute’s purpose was to “deny tax-exempt status not only to those people who influence legislation but also to those who intervene in any political campaign on behalf of any candidate for any public office.” \textit{See 100 CONG. REC. 9604} (1954).

There is little analysis in the legislative history of this provision, and commentators have found it nearly impossible to justify the differing treatment between political campaign activities and lobbying activities. Many commentators have yet to find a satisfactory means to define the two. \textit{See generally} Gregory L. Colvin, \textit{Political Tax Law After Citizens United: A Time for Reform}, \textit{TAX ANALYSTS} (2010), \textit{available} at http://www.adlercolvin.com/attorneys/documents/sugarman.pdf; Johnny Rex Buckles, \textit{Not Even a Peep? The Regulation of Political Campaign Activity by Charities Through Federal Tax Law}, 75 U. CIN. L. REV. 1071 (2007); Amelia Elacqua, \textit{Eyes Wide Shut: The
1954 act also allowed Section 501(c)(4) non-profit organizations to be established for the promotion of "social welfare." Following that lead, in 1959 the United States Supreme Court ruled that businesses could not deduct expenses incurred to promote or defeat legislation.

This sequence of events solidified the federal government's policy inclinations toward neutrality by ensuring that it would not subsidize either political campaigns or substantial lobbying efforts. However, Congress failed to define clearly when lobbying efforts are "substantial" under the Tax Code. Moreover, the Treasury Department failed to define it in the regulations, and courts gave numerous, and sometimes seemingly conflicting, facts and circumstances opinions. As a result, in 1976 Congress added the Section 501(h) expenditure election to the Tax Code as an alternative to relying solely on the imprecise definition of "substantial" under the case law.

This history provides the background for how the Tax Code treats charities today. Charities still enjoy tax-exempt status under Section 501(c)(3). In addition, donors receive a deduction for contributions that they make to Section 501(c)(3) organizations, subject to certain statutory limitations. Finally, similar limitations on political campaign activities and lobbying still exist, although the nuances have been tweaked over the years through case law and revenue rulings.


29. Cammarano v. United States, 358 U.S. 498, 512-13 (1959). In the Majority opinion, the Court noted that denial of the deduction was not a violation of First Amendment rights to free speech because the petitioners were not prohibited from exercising their Constitutional right to free speech. Id. Instead, they were merely required to pay for that activity out of their own pockets. Id.
32. See infra notes 37-60 and accompanying text.
33. See infra note 38.
34. See infra Sections III and IV. They analyze in detail the contours of the "substantial part" test and the § 501(h) expenditure election, respectively.
The purpose of this Article is to analyze the ways in which Section 501(c)(3) organizations take part in lobbying activities while still maintaining their tax-exempt status. 35 This topic is crucial as we revisit these same issues at all levels of government every election season. 36

This Article examines the Tax Code, treasury regulations, revenue rulings, case law, and scholarly research. Its purpose is to provide a detailed analysis of the current law and how exempt organizations can apply it in practice. To achieve this goal, this Article is broken down into seven parts. Section II provides the statutory framework under which Section 501(c)(3) organizations operate. Sections III and IV examine the “substantial part” test and the Section 501(h) expenditure election, respectively. If an organization routinely fails both the “substantial part” test and the Section 501(h) test, then it should establish

35. This Article only examines Section 501(c)(3) organizations, although other organizations may enjoy tax-exempt status. In addition, the purpose of this Article is not to argue whether the tax-exemption is sound public policy. Neither is the objective here to argue how much charitable organizations should or should not be allowed to participate in politics. This Article only looks at how political activities and lobbying inhibit tax-exempt status, although other impermissible activities such as commercial activity and private inurement may threaten tax-exempt status as well.

36. See Judith E. Kindell & John Francis Reilly, Election Year Issues, IRS (2002), available at http://www.irs.gov/pub/irs-tege/eotopic02.pdf. This article argues that not only are tax-exempt organizations more likely to drift into campaign activities during election years, but they are also likely to engage in more lobbying activities since the legislative process is brought to the forefront of the public’s attention. Id.

See also Nanette Byrnes, Activist Churches Bait IRS, But Agency Won’t Bite So Far, NBCNEWS (June 21, 2012, 4:28 PM ET), http://bottomline.msnbc.msn.com/_news/2012/06/21/12343407-activist-churches-bait-irs-but-agency-wont-bite-so-far?lite. This article points out that some pastors planned to provoke the IRS in the 2012 election cycle by delivering sermons for or against political candidates. Id. To see that similar events have played out in past election cycles, see Josh Getlin, Pulpits Ring with Election Messages, L.A. TIMES, Nov. 01, 2004, available at http://articles.latimes.com/2004/nov/01/nation/na-pulpitI; see also Peter Slevin, 33 Pastors Flout Tax Law with Political Sermons, WASH. POST, Sept. 29, 2008, available at http://www.washingtonpost.com/wp-dyn/content/article/2008/09/28/AR2008092802365.html. Ultimately, the IRS did not revoke any church’s tax-exempt status, despite the fact that pastors even sent letters to the IRS agents to inform them of these plans. See Amy J. Harris, Pastors Group Defies IRS Ban on Politics, S.F. CHRON., Nov. 20, 2012, available at http://www.sfgate.com/nation/article/Pastors-group-defies-IRS-ban-on-politics-4055607.php. In addition to seeing an influx of political activities in election years, some commentators have observed that the long-term trend has been for tax-exempt organizations to become increasingly more involved in politics. See Rosemary E. Fei & Gregory L. Colvin, How to Set Up and Maintain an Action Fund Affiliated With a Charity, 15 TAX’N OF EXEMPTS 184, 192 (2004). In particular, this article states that, “[m]ore and more tax-exempt organizations seem compelled to find their full-throated voices through multiple affiliates devoted to public policy and political affairs.” Id.

For an analysis that argues that churches have become more politically involved in the last half century, see generally Vaughn E. James, Reaping Where They Have Not Sowed: Have American Churches Failed to Satisfy the Requirements for the Religious Tax Exemption?, 43 CATHOLIC LAWYER 29, 48-69 (2005).
an affiliated Section 501(c)(4) organization, which is covered in Section V. Section VI attempts to tie all the rules together for the “substantial part” test, the Section 501(h) election, and the use of a Section 501(c)(4) affiliate. Section VI then provides a proposal on how Section 501(c)(3) charitable organizations advance their tax-exempt purposes through lobbying while still protecting their tax-exempt status during campaign seasons. Section VII offers some final thoughts on why the study of this area of the law is so important.

II. STATUTORY FRAMEWORK

According to Section 501(a), a Section 501(c) organization is exempt from taxation unless it fails specified requirements for the exemption. An individual may receive a deduction of up to fifty-percent of her contribution base for the taxable year. Other contributors may deduct the lesser of: thirty-percent; or fifty-percent of the amount that the taxpayer’s contribution base for the taxable year exceeds the charitable contributions allowed to an individual. For both individuals and other contributors, the excess deductions can roll forward for five taxable years beyond the taxable year in which the taxpayer made the contribution.

First, the organization must be legally recognized. In order to be legally recognized, an organization can be set up as a (1) corporation; (2) community chest; (3) fund; or (4) foundation.

Second, the organization must be operated exclusively for an exempt purpose. The following is a list of the seven codified tax-exempt purposes. First, the organization can be established for religious

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38. I.R.C. § 501(c)(3). Also note that political campaign activities are strictly forbidden by § 501(c)(3) organizations. For the nuances of this rule, see infra note 58.
39. I.R.C. § 501(c)(3). Also note that political campaign activities are strictly forbidden by § 501(c)(3) organizations. For the nuances of this rule, see infra note 58.
40. I.R.C. § 501(c)(3).
41. Id.
42. Id.
purposes. Thus, churches and associations of churches enjoy tax-exempt status. Second, the organization can perform charitable activities. This includes activities that involve: (1) providing relief to the poor, distressed, and underprivileged; (2) erecting or maintaining public buildings, monuments, or works; (3) lessening the burdens on government; or (4) promoting social welfare through methods listed above or through lessening neighborhood tensions, eliminating prejudice and discrimination, protecting human and civil rights, or combating community deterioration and juvenile delinquency. Third, the organization can conduct scientific research. Fourth, the organization can be established for reasons related to testing for public safety. Fifth, the organization can carry out literary or educational purposes. Sixth, the organization can foster national or international amateur sports competition. Finally, the organization can be established for the

43. Id.
44. Note that Section 170(b)(1)(A)(i) allows the tax deduction for "churches or a convention or association of churches," thereby meaning this definition of religious "groups" should apply in determining the tax-exemption as well. For the IRS’s definition of "church," based on a compilation of revenue rulings and case law, see “Churches” Defined, IRS.Gov, http://www.irs.gov/Charities-&-Non-Prof’its/Churches-&-Religious-Organizations/Churches—Defined (last visited Apr. 8, 2013). This article contains the fourteen-point factors test that the IRS uses. Id. The most important factors tend to be: (1) membership composed of body of believers; (2) regular assembly as a congregation; and (3) engagement in recognized worship. Also note that the IRS looks at “mail order churches” with great skepticism. Id. This is because churches are not required to file the annual information return, Form 990, thereby making them a convenient option for abusers to seek private benefits. Id. See also Basic Bible Church v. Comm’r., 74 T.C. 846 (1980); People of God Community v. Comm’r., 75 T.C. 127 (1980); Unitary Mission Church of Long Island v. Comm’r., 74 T.C. 507 (1977), aff’d 647 F.2d 163 (2d Cir.1981).
45. I.R.C. § 501(c)(3).
47. I.R.C. § 501(c)(3). See also Treas. Reg. § 1.501(c)(3)-1(d)(5). This provision only applies to scientific research conducted for the public benefit as opposed to research for private benefit or commercial gain. Treas. Reg. § 1.501(c)(3)-1(d)(5). This means the results of the research must be made public on a nondiscriminatory basis, conducted for the benefit of the government, or directed toward benefitting the public.
48. I.R.C. § 501(c)(3). See also Treas. Reg. § 1.501(c)(3)-1(d)(4) which says this provision applies to the testing of consumer products to be used by the general public.
49. Id. See also Treas. Reg. § 1.501(c)(3)-1(d)(3) (defining "educational" as instruction or training to an individual as well as to the public). The Examples to the regulations list schools (elementary, secondary, trade schools, and colleges or universities, so long as the above carry out a regularly scheduled curriculum, have a regular faculty, and have a regularly enrolled body of students), public discussion forums, correspondence courses through the use of television and radio (and likely internet), museums, zoos, planetariums, symphony orchestras, and other similar organizations, as being "educational." Id.
50. I.R.C. § 501(c)(3). Such organizations include state high school activities associations and, currently, the National College Athletic Association ("NCAA"). Of course, now it is the norm for NCAA member schools in the major conferences to pay football and men’s basketball coaches $1 million or more, as well as to conduct activities within athletic departments (e.g. media relations,
prevention of cruelty to animals or children. This requirement provides that, unlike for-profit businesses that pay out equity shares, a non-profit organization cannot distribute its earnings in this fashion. Because organizations may be tempted to pay profit shares disguised as salary to employees, this is a fact-intensive question.

Fourth, no substantial part of the organization’s activities may consist of lobbying activities. To demonstrate this, organizations must pass the “substantial part” test or overcome the hurdle in the expenditure election under Section 501(h). The time dedication required by participating athletes, and selling event tickets and memorabilia) in a manner similar to professional sports teams. This has led some commentators to call into question whether the NCAA’s tax-exempt status should be revoked on the grounds that these activities are private inurement and commercial activities. See Amanda Pintaro, Is the NCAA Fulfilling its Tax-Exempt Status?, ILL. BUS. L. J. (2010), available at http://www.law.illinois.edu/bljournal/post/2010/02/21/Is-the-NCAA-Fulfilling-its-Tax-Exempt-Status.aspx; John D. Colombo, The NCAA, Tax Exemption and College Athletics, 2010 U. ILL. L. REV. 109 (2010); Amy C. McCormick & Robert A. McCormick, The Emperor's New Clothes: Lifting the NCAA's Veil of Amateurism, 45 SAN DIEGO L. REV. 495 (2008). See also Steve Weiberg, NCAA’s Tax-Exempt Status Questioned, USA TODAY (Oct. 5, 2006, 2:40 PM ET), http://www.usatoday.com/sports/college/2006-10-04-ncaa-tax-status_x.htm. This article reports on Congress's threats to challenge the NCAA’s tax-exempt status. For the letter from House Ways and Means Committee Chairman Bill Thomas to NCAA president Miles Brand, see Congress’ Letter to the NCAA, USA TODAY (Oct. 5, 2006, 1:57 PM EDT) http://www.usatoday.com/sports/college/2006-10-05-congress-ncaa-tax-letter_x.htm.

In defense of the NCAA, Brand issued a letter to the Ways and Means Committee arguing that coaches are paid salaries similar to other high-profile faculty members on college campuses and that heavy media exposure to athletic programs generate interest in universities and help recruit non-athlete students to the school for educational reasons. See Brand to Congress: NCAA Deserves Tax-Exempt Status, ESPN (Nov. 6, 2006, 12:52 PM EDT), http://sports.espn.go.com/ncaa/news/story?id=2662739.

1. I.R.C. § 501(c)(3).
2. Id.
3. For a good illustration on how to apply these rules, see Church of Scientology of California v. Comm’r, 823 F.2d 1310 (9th Cir. 1987). In this case, the court held that private benefit did exist because the church paid its founders ten-percent of the royalties for literature the church sold, the church provided the founders’ living expenses, and the founders had extensive control over church assets, which they often used for their own benefit. Id.
5. I.R.C. § 501(c)(3).
6. See infra Section III. Generally speaking, the “substantial part” test requires that an organization may only devote an insignificant portion of its resources to activities intended to influence legislation.
7. See infra Section IV. I.R.C. § 501(h) creates a mechanical test, based solely on an organization’s expenditures, to determine whether an organization has engaged in excessive lobbying activities, thereby causing it to lose its tax-exempt status under Section 501(c)(3).
Fifth, the organization may not engage in any political campaign activities for or against a candidate for office. A "candidate for public office" is defined as any person who holds herself out as a contestant in any national, state, or local elected public office. The prohibition against political campaign activities, according to the language of Section 501(c)(3), is absolute. Thus, many commentators argue that there is no manner in which a Section 501(c)(3) organization can engage in insubstantial or de minimis campaign activities. However, this view overlooks crucial case law and revenue rulings. For this reason, this

58. Treas. Reg. 1.501(c)(3)-1(c)(3)(iii) (2008). The statutory language suggests absolutely no political campaign activities should be allowed. For commentary that subscribes to this somewhat inadequate interpretation, see Gina M. Lavarda, Nonprofits: Are You at Risk of Losing Your Tax-Exempt Status?, 94 IOWA L. REV. 1473, 1490 (2009). The analysis in this article is lacking because it relies solely on the ruling in Ass’n of the Bar of the City of New York v. Comm’r from the Second Circuit as if it is identical to all rulings on the subject. In addition, this case dealt with an organization that rated a broad range of candidates in an upcoming election. This analysis fails to account for other jurisdictions that have heard cases that have fact patterns with less significant political campaign activities.

Although the statute makes this prohibition appear to be absolute and therefore allow for no political campaign activities whatsoever, no matter how insignificant, case law and revenue rulings paint a slightly different picture.

The relevant revenue rulings involve universities that were § 501(c)(3) organizations that got involved in politics. The IRS likely allowed for some leeway because of the prevalent belief that college campuses are intended to be a "market place of ideas" and therefore free speech and free association rights are more expansive than they are in other contexts. For a more in-depth discussion on how Constitutional doctrines may serve as a limit on the IRS, see infra notes 63-66 and accompanying text. See Rev. Rul. 72-512, 1972-2 C.B. 246 (holding that a university was not sufficiently engaged in a political campaign by giving political science students course credit for working on campaigns). See also Rev. Rul. 72-513, 1972-2 C.B. 246 (holding that a university was not involved in lobbying or campaign activities although it provided funding, office space, and staff for a student newspaper that published political op-eds). See also infra note 76, 78-79 and accompanying text.

The Tax Code treats political activities and lobbying as distinctly different. However, commentators observe that there are many shared policy objectives in regulating both areas, and the two overlap significantly. For a discussion on the relationship between the two, see generally Richard Briffault, Lobbying and Campaign Finance: Separate and Together, 19 STAN. L. & POL’Y REV. 105 (2008).

59. Treas. Reg. 1.501(c)(3)-1(c)(3)(iii). Note that this rule utilizes a broad scope in that it applies to any campaign for a candidate for any office. See Rev. Rul. 67-71, 1967-1 C.B. 125 (holding that an organization was not entitled to an exemption because it helped in a campaign running for a seat on the local school board).

60. See St. Louis Union Trust Co. v. United States, 374 F.2d 427, 432 (8th Cir.1967) (holding that an insignificant foray into politics is "not fatal." See also Rev. Rul. 72-512, 1972-2 C.B. 246 and Rev. Rul. 72-513, 1972-2 C.B. 246 where the IRS appears to be backing down from a constitutional fight, since the § 501(c)(3) organizations involved were universities.

In Rev. Rul. 72-512, a university allowed students to receive course credit for working on political campaigns. The IRS upheld the tax-exemption on the grounds that the students’ activities were "reasonably germane to the course of instruction" and the fact that the activities were part of university curriculum and used university employees and facilities to help with this educational
rule could possibly provide some flexibility for organizations, although it is by no means an open avenue that organizations should pursue regularly.

III. THE "SUBSTANTIAL PART" TEST

The "substantial part" test comes from Section 501(c)(3). The statute says that to remain exempt, an organization must have:

\[\text{No substantial part of [its] activities... consisting of} \text{ carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.} \]  

Thus, there are two issues to determine whether an organization passes the "substantial part" test: (1) whether an activity constitutes a political activity or lobbying; and, if so, (2) whether the political activity or lobbying is a substantial portion of the organization's total activities. Relying on the two-part test may be risky and uncertain because it is factors-based. Still, case law does provide guidance on the issue and it may be necessary for larger organizations that are more likely to be harmed by the Section 501(h) expenditure election, discussed in Section IV.

A. Lobbying Activities

Lobbying is the attempt to influence legislation. The regulations provide a broad definition for the term "legislation." This definition includes statutes at the federal, state, and local levels. It also includes referendums, initiatives, and constitutional amendments. However, it

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process "does not make the university a party to the expression or dissemination of political views of the individual students in the course of their actual campaign activities within the intendment of Section 501(c)(3)." The IRS mentioned in this revenue ruling that the university did not influence students to work on any particular campaigns and the university had to be paid for facilities or services performed by the students involved in this program.

In Rev. Rul. 72-513, a university sponsored a newspaper that printed political opinions and supported and opposed political candidates. The IRS appeared to grant deference in these cases because it feared the consequences of losing a battle over Constitutional doctrine. For a discussion of the Constitutional issues, see infra notes 75-79.

61. I.R.C. § 501(c)(3).
64. Id.
does not include action taken with the executive branch unless such action is taken to persuade officials in the executive branch to influence legislation. It also does not include litigation activities within the judicial branch.

Courts use all facts and circumstances to determine whether an organization’s activities are intended to influence legislation. Contacting legislators or their staff directly in an attempt to persuade them to vote a certain way is lobbying. In addition, asking members of the executive branch to support or oppose legislation is considered lobbying as well. The IRS has even gone so far as to rule that contacting senators to persuade them to support or oppose nominees for the federal courts is lobbying. In contrast, activities that are not considered lobbying include testifying in legislative hearings when the organization is invited by a legislative committee to do so and the organization’s publication of a nonpartisan study, analysis, or research.

There is a conflict over whether molding public opinion is lobbying. This is because the molding of public opinion by itself does not necessarily influence legislation. For example, an organization can bombard the public with the organization’s opinions through

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65. Id. See infra note 195 and accompanying text.
66. Four types of Section 501(c)(3) organizations may engage in litigation. These types are: (1) legal aid organizations; (2) human and civil rights defense organizations; (3) public interest law firms; and (4) organizations that attempt to achieve charitable goals through the institution of litigation as plaintiff. See Litigation by IRC 501(c)(3) Organizations, IRS (1984), available at http://www.irs.gov/pub/irs-tege/eotopics84.pdf.
68. Haswell v. United States, 500 F.2d 1133, 1133 (Ct. Cl. 1974).
69. Rev. Rul. 67-293, 1967-2 C.B. 185. In this revenue ruling, the IRS determined that a charitable organization did not qualify for Section 501(c)(3) status. Id. The organization operated animal shelters and sought government officials to support legislative measures to protect animals’ well-being. Id. The IRS determined that its lobbying activities were substantial even though it “rarely contact[ed] legislators in its own name, but merely encourag[ed] others to do so.” Id.
70. Notice 88-76, 1988-27 I.R.B. 34. Here, the IRS "considered the question of whether attempting to influence the Senate confirmation of an individual nominated by the President to serve as a federal judge constitutes an ‘exempt function . . . . [T]he Service’s position is] that such activity constitutes an attempt to influence legislation within the meaning of Section 501(c)(3) and related Code provisions.” Id.
71. Rev. Rul. 70-449, 1970-2 C.B. 112. In this revenue ruling, the IRS determined that, a university that operated a nationally prominent biology research department “is not engaged in prohibited legislative activity if, at the request of a legislative committee, a representative testifies as an expert witness on pending legislation affecting the organization.” Id.
72. Rev. Rul. 64-195, 1964-2 C.B. 138. The IRS held in this revenue ruling that an organization that studied the law and court systems to assist lawyers in their continuing legal education could conduct “nonpartisan study, research and assembly of materials in connection with court reform” and disseminate these findings to the public. Id.
advertisements on television, through the radio, in newspapers, and via the internet. However, if the public simply ignores these opinions and fails to attempt to sway legislators on the issue, then the organization has not influenced legislation.

Still, the Supreme Court’s ruling in Christian Echoes v. United States suggests that attempting to mold public opinion does count as lobbying. In contrast, treasury regulation 1.501(c)(3)-1(d)(2) completely controverts Christian Echoes in saying:

The fact that an organization, in carrying out its primary purpose, advocates social or civic changes or presents opinion on controversial issues with the intention of molding public opinion or creating public sentiment to an acceptance of its views does not preclude such organization from qualifying under § 501(c)(3) so long as it is not an action organization of any one of the types described in paragraph (c)(3) of this section.

In light of these circumstances, organizations can make a reasonable case that they are allowed to mold public opinion. However, although the Christian Echoes ruling was delivered nearly forty years ago, it is still good law today.
Even if an activity is intended to influence legislation, in order for the activity to be attributed to the tax-exempt organization, the exempt organization must be sufficiently involved in carrying out the prohibited involvement. In Revenue Ruling 72-513, the IRS held that a university was not involved in lobbying although it provided funding, office space, and staff for a student newspaper that published political op-eds.\(^{76}\) Granted, college campuses are likely given somewhat greater leeway in distributing political opinions, because universities are intended to be a "marketplace of ideas."\(^ {77}\) Thus, the IRS appears to have been, at least in part, backing down from a possible constitutional fight.\(^ {78}\) Nonetheless,

\[^{76}\text{Rev. Rul. 72-513, 1972-2 C.B. 246.}\]
\[^{77}\text{See also Susan Brooks Thistlethwaite, IRS Clears Obama’s Church, WASH. POST, May 2, 2008, available at http://newsweek.washingtonpost.com/onfaith/panelists/susan_brooks_thistlethwaite/2008/05/irs_clears_obamas_church.html. Here, the church’s attorney suggested that the IRS ignored administrative courtesies during the investigation and waited until Obama was the frontrunner as the Democratic nominee for president until it started to investigate in an attempt to draw more media attention. \textit{Id.}\}
\[^{78}\text{See also }\text{INTERNAL REVENUE SERV., FINAL REPORT: PROJECT 302: POLITICAL ACTIVITIES COMPLIANCE INITIATIVE 1 (2006) and INTERNAL REVENUE SERV., 2006 POLITICAL ACTIVITIES COMPLIANCE INITIATIVE 1 (2007). According to these investigations conducted during the 2004 and 2006 campaigns, the IRS has documented that at least a dozen churches made statements for or against candidates during each campaign season. It is significant to note that the only Section 501(c)(3) groups that should expect this Constitutional protection are college campuses and churches. See generally Hazelwood Sch. Dist. et. al. v. Kuhlmeier et al., 484 U.S. 260 (1988). In this case, the United States Supreme Court suggests that the First Amendment protections are somewhat limited for high school student newspapers. \textit{Id. Contra this with the notion that college newspapers, as Justice Holmes asserts in }\textit{Abrams}, have broader First Amendment protections. As a result, the application of Rev. Rul. 72-}
the IRS also relied on the insufficiency of control to find that the university was not involved in political activities or lobbying.\textsuperscript{79}

\textbf{B. Whether the Lobbying Activities Are \textquote{\textquotedblleft}Substantial\textquoteright\textclosecurlyquote{}}

Courts generally apply one of three tests to determine whether an organization’s lobbying activities are \textquote{\textquotedblleft}substantial.\textquoteright\textsuperscript{80} These tests are: (1) a percentage test based on \textquote{\textquotedblleft}time and effort;\textquoteright\textsuperscript{83} (2) a percentage test that examines monetary expenditures; or (3) a factors test that examines all facts and circumstances to determine whether the lobbying is substantial.\textsuperscript{81}

1. The Time and Effort Test

The time and effort test, established in \textit{Seasongood v. Comissioner},\textsuperscript{82} looks at the organization’s \textquote{\textquotedblleft}time and effort\textquoteright\textsuperscript{83} spent on lobbying. In \textit{Seasongood}, the Sixth Circuit held that less than five percent of an organization’s \textquote{\textquotedblleft}time and effort\textquoteright\textsuperscript{84} spent on lobbying activities was insufficient to be \textquote{\textquotedblleft}substantial.\textquoteright\textsuperscript{85} It is significant to note that, in addition to setting the five-percent guideline, \textit{Seasongood} also emphasized that the \textquote{\textquotedblleft}time and effort\textquoteright\textsuperscript{86} spent on lobbying are the critical factors to examine.\textsuperscript{87}

\begin{center}
\textsuperscript{513} should be confined to college campuses, and not interpreted to apply to educational institutions more broadly.
\end{center}

\textsuperscript{79}. Rev. Rul. 72-513.
\textsuperscript{81}. Id.
\textsuperscript{82}. 227 F.2d 907 (6th Cir. 1955).
\textsuperscript{83}. Id. at 912. This case provides a conservative but certain standard of five-percent. Id.
\textsuperscript{84}. Id.
\textsuperscript{85}. Id.

The organization in this case engaged in activities to promote Cincinnati’s sanitation efforts and school systems. Id. The ruling states in relevant part,

\begin{quote}
\textit{Seasongood} testified that something less than 5\% of the time and effort of the League was devoted to the activities that the Tax Court found to be \textquote{\textquotedblleft}political.\textquoteright\textsuperscript{88} In view of the rule, that this remedial statute must be liberally construed to effect its purpose, and in view of the fact that \textit{Seasongood}’s evidence was not successfully challenged either by adversary witnesses or destructive analysis, we conclude that the so-called \textquote{\textquotedblleft}political activities\textquoteright\textsuperscript{89} of the League were not in relation to all of its other activities substantial, within the meaning of the section.
\end{quote}

\textsuperscript{86}. Id.
\textsuperscript{87}. Id.
\textsuperscript{88}. Id.
\textsuperscript{89}. Id.
In *League of Women Voters of the United States v. United States*, the court refused to provide a specified percentage. However, the court still analyzed the time an organization spent to determine whether its lobbying activities were “substantial.” In calculating time spent, the court included time spent studying, discussing, and formulating a position on the issues, in addition to the time spent actually contacting government officials. This ruling is unfavorable to organizations because it utilizes such a broad scope to define how much time is spent on lobbying activities. Still it is beneficial in that it encompasses only time, and does not consider other resources such as money spent, property used, or information disseminated.

The Tax Court denoted a slightly different standard in *World Family Corporation v. Commissioner*, a case that actually dealt with private inurement. In *World Family*, a Section 501(c)(3) organization raised money to provide financial assistance to a church’s missionaries and funded scientific research. The organization promised to pay fundraisers a twenty percent commission for soliciting funds to the organization. The court struck down the twenty percent standard on the grounds that it reflected “substantial” private inurement, thereby subjecting the organization to penalties and threatening its tax-exempt status. The court went further and noted that a ten percent commission would be acceptable as “insubstantial.”

Many practitioners have attempted to carry this ten percent standard over to the lobbying activities arena by assuming that ten percent of an organization’s activities can be devoted to lobbying without violating the

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87. *Id.* In this case, the League of Women Voters of the United States (“the League”) was a residuary legatee under a will. The IRS required the estate in question to pay estate taxes on the donation to the League. *Id.* Speaking of the League’s activities, the court stated on page 382 that, “[i]t was its purpose, through its membership and its officials, to do what it could to influence those who were in a position to bring about [the desired] results, if they could be persuaded to do so.” *Id.* at 382. After analyzing the League’s publications, communications to its local chapters, and its activities, the court concluded on page 383 that “the influencing of legislation is the League’s main purpose and reason for being.” In light of these findings, the court determined that the League was engaged in substantial lobbying activities and therefore ineligible for the estate tax-exemption. *Id.* at 383.
88. *Id.* at 386.
89. *Id.*
90. 81 T.C. 958 (1983).
91. *Id.* at 961.
92. *Id.* at 962.
93. *Id.* at 967.
94. *Id.*
"substantial part" test.\textsuperscript{95} Still, there are risks associated with applying the ten percent standard because World Family Corporation is not mandatory in any jurisdiction and the ruling does not even address lobbying activities. Furthermore, even if the ten percent standard should carry over to lobbying activities, it is unclear as to which resources it should apply.

Also in the private benefit context, the Tax Court in \textit{Orange County Agricultural Society v. Commissioner},\textsuperscript{96} provides some guidance as to how much private inurement is clearly excessive. In this case, the court ruled that one-third of an organization's revenues were distributed to the organization's key members.\textsuperscript{97} The court found that this was beyond "insubstantial."\textsuperscript{98} Although this case applied to private inurement and not lobbying activities, practitioners can be confident that this one-third figure is excessive and therefore they should avoid even coming close to it.

\begin{itemize}
\item Charitable organizations also advertise that they follow the ten-percent standard. \textit{See Lamar White Jr., \textit{What is the Louisiana Family Forum?}, NOLA DEFENDER, http://noladefender.com/content/what-louisiana-family-forum} (last visited Apr. 8, 2013). This article states in relevant part, "[s]uffice it to say that if no more than five to ten-percent of an organization's total efforts are devoted to lobbying, it is probably acting within legal limits." \textit{Id}. \textit{See also Political Speech and Non Profit Tax Issues, AM. CTR. FOR LAW & JUSTICE, http://aclj.org/churches-organizations-political-speech-non-profit-tax-issues} (last visited Apr. 8, 2013). This article cites the World Family case in settling on the ten-percent standard. \textit{Id}. \textit{See also Dana Silverman, \textit{Raising Money for a 501(c)(4): Building Your Toolbox for Civic Engagement, 31 GRASSROOTS FUNDRAISING J. 2} (Mar.-Apr. 2012), \textit{available at http://www.grassrootsfundraising.org/wp-content/uploads/2012/03/Raising_Money_C4_v31_n2_0fj.pdf}. This article is less committed to the ten-percent standard, but mentions it as a possibility, stating on page three that "501(c)(3) organizations can engage in an 'insubstantial' amount of lobbying generally agreed to be less than five or ten-percent of their overall time." \textit{Id}.
\end{itemize}

\begin{itemize}
\item \textsuperscript{96} 55 T.C.M. 1604 (1990).
\item \textsuperscript{97} \textit{Id}.
\item \textsuperscript{98} \textit{Id}.
\end{itemize}
2. The Expenditures Test

The percentage test established in Haswell v. United States focuses on the monetary expenditures an organization devotes to lobbying. In Haswell, a donor sought the charitable tax deduction for money he granted to the National Association of Railroad Passengers. The court denied this deduction on the grounds that, based on the breakdown of how the organization spent its money, it was engaged in substantial activities intended to influence legislation.

Although the court cautioned that percentage tests are not determinative, it still noted that "one measure of the relative significance of [an organization's] activities in relation to its objectives is the amount of money devoted to each category of its operations." The court then determined that, despite slight variations in calculating, the organization devoted between fifteen and twenty percent of its expenditures in two subsequent years to lobbying activities. Ultimately, the court ruled these expenditures were "substantial." In holding that fifteen and twenty percent are substantial is consistent with other case law, the Haswell ruling's main contribution is the notion that courts can look at expenditures alone to determine substantiality, even for organizations that do not make the Section 501(h) election.

3. The Facts and Circumstances Test

The facts and circumstances test set forth in Christian Echoes looks...
at all factors to determine whether an organization’s lobbying activities are “substantial.” This standard allows courts to consider not only the time and expenditures an organization devotes to lobbying, but also to factor in facility and property use, the amount of information disseminated, and the organization’s reputation within the community. In Christian Echoes, the court found that an organization had published numerous articles and delivered frequent radio broadcasts covering over twenty different political issues to be widely disseminated in an attempt to mold public opinion. In its numerous activities, the organization called for action by using such slogans as, “[y]our opinion isn’t worth a nickel without your action to back it up.” As a result of these continued efforts to mold public opinion and make calls for action, the Tenth Circuit held that the lobbying activities were “substantial” without the use of a certain percentage or defined resource expenditure method.

If an organization engages in substantial lobbying activities, it loses its tax-exemption. Further, organizations that lose the Section 501(c)(3) tax-exemption because of their substantial lobbying activities must face intermediate sanctions on the political expenditures they made. The term “expenditures” includes “any amount paid or incurred by the organization in carrying on propaganda, or otherwise attempting to influence legislation.” The organization must pay an excise tax equal to five percent of the political expenditures. In addition, the managers of the organization who willfully allowed the excessive expenditures are subject to a five percent excise tax as well.

108. Id. at 855.
109. Id.
110. Id. at 856. It is significant that, although the organization in this case also engaged in election activities, the court specifically stated that the organization engaged in substantial lobbying activities as well. Thus, this case is useful in analyzing both the campaign activities prohibition and the “substantial part” test.
111. I.R.C. § 4912(d)(1) (2008). This definition means that, even if an organization does not donate money to a political organization, the “expenditures” would include the value of services performed by the organization’s employees who engaged in research, preparation, and lobbying activities. Id. Thus, the penalty would be five-percent of the cost of the political services that are “excessive.” Id.
112. I.R.C. § 4912(a).
113. I.R.C. § 4912(b). See also I.R.C. § 4955(f)(2) (2008). This provision applies to any officer, director, or trustee of the organization (or anyone with authority similar to the aforementioned positions) and any employee of the organization with authority or responsibility of the expenditure in question. Id. See also § 4912(d)(3), which says that if more than one manager is liable, then all managers share joint and several liability.
In light of these findings, an organization must follow different tests depending on its jurisdiction. These tests are not always clearly defined. Still, an organization that fails the necessary test faces strict penalties. Not only does the organization lose its Section 501(c)(3) status and thereby become subject to income tax, but it is also required to pay penalties on its lobbying expenditures. Given these penalties, organizations are wise to avoid coming too close to the borderline. If organizations find that they frequently toe the boundary, then they should make the Section 501(h) election to obtain greater certainty.

IV. THE SECTION 501(H) EXPENDITURE ELECTION

In order to give Section 501(c)(3) organizations a clear answer regarding whether their lobbying activities are substantial, Congress passed Section 501(h) for certain groups. These groups include Section 501(c)(3) organizations that are not churches, governmental units, groups that test for public safety, or private foundations. This Section allows an organization to elect to follow a series of mechanical tests that determine whether the organization’s lobbying activities are substantial. If the organization’s lobbying expenditures do not exceed the Section 4911(c) limits, then the organization will not be taxed under Section 4911 or lose its Section 501(c) exemption.

By contrast, if the lobbying expenditures exceed Section 4911 limits, then the organization will be taxed at a rate of twenty-five percent of the excess amount. Further, if the lobbying expenditures regularly exceed one hundred and fifty percent of the Section 4911 limits, then the organization will lose its tax-exemption. In applying the Section 501(h) election, it is best to break the process down into five steps. These steps are analyzed below.

A. Step One: Determine the Exempt Purpose Expenditures for the Year

The Tax Code defines exempt purpose expenditures as amounts paid or incurred to accomplish an organization’s Section 501(c)(3) tax-

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115. See supra note 31 and accompanying text.

116. I.R.C. § 501(h). For a discussion on the benefits of certainty that the § 501(h) expenditure election provides, see infra note 121.


exempt purposes, including lobbying for exempt purposes but excluding capital and fundraising.\textsuperscript{119} Lobbying expenditures are amounts paid or costs incurred for the purpose of influencing legislation.\textsuperscript{120} If an expenditure is made to influence legislation that is unrelated to a tax-exempt purpose then it must fall under one of the six exceptions, otherwise it is considered a lobbying expenditure.\textsuperscript{121}

There are six activities that are explicitly exempted from lobbying expenditures.\textsuperscript{122} First, organizations may publish the results of a nonpartisan analysis, study, or research.\textsuperscript{123} Second, organizations may provide technical advice to a government body or committee in response to a written request.\textsuperscript{124} Third, the “self-defense” exception allows organizations to engage in direct communication with legislators on issues that affect the organization’s existence, tax-exemption, or eligibility to receive deductible contributions.\textsuperscript{125} Fourth, organizations may engage in communication with their \textit{bona fide} members on legislation of mutual interest so long as the purpose of that communication is not to directly encourage those members to lobby or urge nonmembers to lobby.\textsuperscript{126} Fifth, organizations may persuade members of the executive branch on executive matters, including

\begin{itemize}
\item \textsuperscript{119} I.R.C. § 4911(e)(1)(A). See supra notes 39-51 and accompanying text for a discussion of tax-exempt purposes.
\item \textsuperscript{120} I.R.C. § 4911(c)(1).
\item \textsuperscript{121} It is significant to note that the Section 501(h) definition of “influencing legislation” is more clearly defined here than under the “substantial part” test. Still, the case law definitions under the “substantial” test are generally similar with those under the Section 501(h) election. Therefore, groups that make the § 501(h) election do not necessarily get a more favorable definition (in terms of allowing significantly more lobbying activities to be exempt) with which to work, but they certainly do enjoy a definition that provides greater certainty.
\item \textsuperscript{122} I.R.C. § 4911(d)(2).
\item \textsuperscript{123} \textit{Id. at} § 4911(d)(2)(A).
\item \textsuperscript{124} \textit{Id. at} § 4911(d)(2)(B).
\item \textsuperscript{125} \textit{Id. at} § 4911(b)(2)(A).
\item \textsuperscript{126} \textit{Id. at} § 4911(b)(2)(D).
\end{itemize}
regulations and administrative policies, so long as the organization's purpose is not to get the executive branch officials to influence legislation.127 Finally, organizations may engage in discussions of broad social, economic, or similar problems.128 Any expenditure made to influence legislation is not included in the list of exceptions and is thus a lobbying expense.129

B. Step Two: Calculate the Maximum Combined Lobbying Amount

The maximum amount of nontaxable lobbying expenditures is the lesser of $1 million or the amount corresponding to exempt purpose expenditures ("EPEs"), as illustrated in the table below.130 Note that the twenty-five percent tax is imposed on the excess of the amount allowed in the table.131 Also, note that the maximum for combined lobbying expenditures is always $1 million.

<table>
<thead>
<tr>
<th>EPEs</th>
<th>Maximum Combined Lobbying Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not over $500k</td>
<td>20% of EPEs</td>
</tr>
<tr>
<td>Over $500k - $1M</td>
<td>$100k + 15% of EPEs over $500k</td>
</tr>
<tr>
<td>Over $1M but not over $1.5M</td>
<td>$175k + 10% of EPEs over $1M</td>
</tr>
<tr>
<td>Over $1.5M</td>
<td>$225k + 5% over $1.5M</td>
</tr>
</tbody>
</table>

C. Step Three: Categorize the Lobbying Expenditures

The organization must determine whether activities are direct or grassroots lobbying. The regulations require a fairly sophisticated analysis to determine this.132 Under the regulations, there are three forms of lobbying that generate expenditures included under Section 501(h). These forms include direct lobbying,133 grassroots lobbying,134

127. *Id.* at § 4911(b)(2)(E).
129. Also excluded from exempt purposes expenditures are: (1) expenditures that are unrelated to the organization's exempt purpose; (2) commercial activities; and (3) unrelated business activities.
130. See I.R.C. § 4911(c)(2) which provides the numbers used in the table.
131. *Id.* at § 4911(a)(1).
132. Generally speaking, direct lobbying is communication with a member of government who participates in forming legislation in an attempt to influence that legislation. Grassroots lobbying, on the other hand, is communication made with organization members or the general public in an attempt to motivate them to pressure legislators to take a particular action.
and mass media lobbying.  

First, direct lobbying occurs when organization members contact legislators and their staff on behalf of the organization to influence legislation. For Section 4911 purposes, if the piece of legislation in question is being addressed through initiative petition, then the voters are considered legislators.

Second, grassroots lobbying involves a number of like-minded people, who may not necessarily be involved in the organization, contacting legislators to influence legislation pursuant to the organization’s preferences. Identifying legislators and saying how they will likely vote on an issue falls under grassroots lobbying.

Third, mass media lobbying involves using widely distributed advertisements to influence legislation. Any advertisement by an organization regarding highly publicized legislation pending in a legislature or committee is presumed to be grassroots lobbying if it is

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134. Id. at § 56.4911-2(b)(2).
135. Id. at § 56.4911-2(b)(3)(i).
136. Id.
137. Treas. Reg. § 56.4911-2(b)(1)(i). Contacting government officials who are not legislators may be lobbying also if the purpose of the communication is to persuade the government officials to influence legislation. Id. See also Treas. Reg. § 56.4911-2(d)(3) which defines a “legislative body” as one that does not include executive, judicial, or administrative bodies. See also Treas. Reg. § 56.4911-2(d)(4) which lists school boards, housing authorities, sewer and water districts, zoning boards, and “other similar Federal, State or local special purpose bodies, whether elective or appointive” as administrative bodies.
138. Treas. Reg. § 56.4911-2(b)(1)(ii). Direct lobbying also requires that the organization: (1) refer to a specific piece of legislation; and (2) reflect a view on that legislation. Id. Contra Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii) (2008), under the “substantial” test which does not contain the nuance that classifies citizen-voters as legislators in initiative petitions.
139. Treas. Reg. § 56.4911-2(b)(2). See also Treas. Reg. § 56.4911-2(b)(2)(ii) which says that for an action to be considered grassroots lobbying, the organization must: (A) refer to specific legislation; (B) reflect views on that legislation; and (C) encourage the listener to take action. See also Treas. Reg. § 56.4911-2(b)(3)(C) which encompasses “astro-turfing,” a practice where an organization prints and distributes materials to like-minded individuals who then mail the materials to legislators.
140. Treas. Reg. § 56.4911-2(b)(2)(iv). See also Rev. Rul. 2007-41, 2007-25 I.R.B. 1421, which says that voter guides are not considered grassroots lobbying so long as they are neutral and cover a broad range of issues. Grassroots lobbying also requires that the organization: (1) refer to a specific piece of legislation; (2) reflect a view on that legislation; and (3) encourage the audience to take action. Id.
See generally Gregory L. Colvin, IRS Gives Christian Coalition a Green Light for New Voter Guides, TAX NOTES 1093 (2005). In this article, Colvin argues that the settlement with the Christian Coalition, which sets out eleven criteria for voter guides, will likely serve as a safe harbor for voter guides. Id.
published or aired within two weeks of the applicable body's voting on the legislation. In addition, the organization must reflect its views on the legislation and either refer to the specific piece of legislation or tell voters to contact legislators.\(^\text{142}\)

Still, the organization may rebut this presumption.\(^\text{143}\) Even if the advertisement satisfied the above conditions, the organization may demonstrate that it regularly makes communications similar to the advertisement or that the timing of the advertisement was unrelated to the upcoming legislative action.\(^\text{144}\)

**D. Step Four: Calculate the Grassroots Lobbying Amount**

The organization must calculate the grassroots lobbying amount. The grassroots lobbying amount must be less than or equal to twenty-five percent of the combined lobbying amount.\(^\text{145}\)

**E. Step Five: Compute the Tax on the Excess Lobbying Expenditures**

A twenty-five percent tax is imposed on the excess lobbying expenditures.\(^\text{146}\) This applies to excess combined lobbying expenditures over the combined limit\(^\text{147}\) or excess grassroots expenditures over the grassroots limit.\(^\text{148}\) The organization may lose its exemption if the excess lobbying expenditures, either total or grassroots, regularly exceed their respective lobbying limit by one hundred fifty percent.\(^\text{149}\)

As with most elections in the tax code, making the Section 501(h) election has its benefits and drawbacks. One benefit to making the election is that it provides certainty. This is due to the fact that the statutes and regulations provide clear definitions of which activities are lobbying, as well as how much lobbying is allowed. In addition, it helps small organizations that are less likely to exceed the absolute expenditure limits. Furthermore, it helps organizations that utilize volunteers as opposed to paying members for their work.\(^\text{150}\) Moreover,
the election can be made at any time during the taxable year in question, which makes it a fallback that organizations can use if they are too close for comfort under the “substantial part” test.©

The drawback of the election is that Section 501(h) requires complex administration and the sliding scale is more likely to hurt large organizations that can spend $1 million on lobbying without exceeding five-percent of total expenditures. In light of these circumstances, organizations should weigh these costs and benefits when making the election at the end of the taxable year.

V. THE SECTION 501(c)(4) ALTERNATIVE

If a Section 501(c)(3) organization cannot achieve its objectives without some political campaign activities or substantial legislative activities, as determined under the “substantial part” test or the Section 501(h) expenditure election, then it can form an affiliated Section 501(c)(4) organization to act as its political arm.© The rules of Section 501(c)(4) give tax-exempt status to civic leagues and organizations not organized for profit but for the promotion of “social welfare.”© Social welfare organizations may engage in partisan political activities, so long as those activities are not the organization’s primary purpose.© In

151. See the 2011 version of Form 5768, available at http://www.irs.gov/pub/irs-pdf/f5768.pdf. This Form is the document on which the organization makes the § 501(h) election. See that box one states: “Note: This election must be signed and postmarked within the first taxable year to which it applies.” Id. (emphasis in original). This means once the election is validly made, it remains good for the organization until it is revoked.

152. See generally Fei & Colvin, supra note 36. Note that the use of § 501(c)(4) organizations gained a lot of mainstream attention in 2010 and was again in the spotlight in 2012. See generally Editorial, The Secret Election, N.Y. TIMES, Sep. 19, 2010, available at http://www.nytimes.com/2010/09/19/opinion/19sunl.html?_r=1&. In summing up some observers’ dissatisfaction in knowing that § 501(c)(4) organizations allow for both unlimited and anonymous donations, this article states: “For all the headlines about Tea Party and blind voter anger, the most disturbing story of this year’s election is embodied in an odd combination of numbers and letters: 501(c)(4).” Id.

153. See I.R.C. § 501(c)(4) which also covers local associations of employees of a designated employer that devotes its net earnings to charitable, educational, or recreational purposes. This portion of § 501(c)(4) is beyond the scope of this Article.

154. Organizations that do engage in partisan political activities are subject to campaign finance laws with respect to those activities. For an overview of federal campaign laws, see generally FEDERAL ELECTION CAMPAIGN LAWS COMPILED BY THE FEDERAL ELECTION COMMISSION (Apr. 2008), available at http://www.fec.gov/law/feca/feca.pdf. The use of Section 501(c)(4) groups has become extremely controversial given that they are subject to reporting measures that are far less stringent than those to which Section 527 organizations must adhere. The use of § 501(c)(4) organizations has become particularly scrutinized following the United States Supreme Court’s 2010 ruling in Citizens United, where the Court held that labor unions and corporations can make unlimited direct donations to influence
addition, social welfare organizations may engage in unlimited lobbying, so long as the lobbying is germane to the Section 501(c)(3) organization’s exempt purpose.

The Section 501(c)(3) organization can give funds to the Section 501(c)(4) organization, but those funds cannot be used for campaign activities. In addition, the Section 501(c)(4) organization can raise money on its own. However, both organizations must follow significant formalities to remain separate to prevent the IRS from attributing the elections. The result is that labor unions and corporations are now giving unlimited political donations to the Section 501(c)(4) organizations, pursuant to the ruling in Citizens United, while still enjoying anonymity that has long been available to § 501(c)(4) organizations. For a discussion on this practice, see Chris Good, Don’t Blame Citizens United, THE ATLANTIC, (Oct. 20, 2010, 6:15 PM ET), http://www.theatlantic.com/politics/archive/2010/10/dont-blame-citizens-united/64906/.


For an example of a Section 501(c)(4) organization, Crossroads Grassroots Policy Strategies which is run by Karl Rove, was investigated on the grounds that it was engaged in excessive partisan political activities, see generally Brody Mullins & Jacob Gershman, IRS Probes Nonprofit Political Groups, WALL ST. J., June 28, 2012, at A4. That organization later lost its exemption because of its 2012 campaign activities. See generally Jonathan D. Salant, IRS Denial of Tax Exemption to U.S. Political Group Spurs Alarms, BLOOMBERG NEWS (June 8, 2012, 12:01 AM ET), http://www.bloomberg.com/news/2012-06-08/irs-denial-of-tax-exemption-to-u-s-political-group-spurs-alarms.html.

Also note that the IRS does little to police Section 501(c)(4) organizations because Section 501(c)(4) organizations have traditionally not accounted for much revenue, and the IRS is a tax collection agency not an elections regulator. For more on this discussion, see Michael Luo & Stephanie Strom, Donor Names Remain Secret as Rules Shift, N.Y. TIMES, Sept. 20, 2010, available at http://www.nytimes.com/2010/09/21/us/politics/21money.html?_r=1&pagewanted=all.

155. Rev. Rul. 81-95, 1981-1 C.B. 332. In this revenue ruling, an organization provided financial assistance and in-kind services for political campaigns. See supra notes 39-51 and accompanying text for a list of possible exempt purposes. The IRS pointed out that § 501(c)(4) requires an organization to operate primarily for social welfare purposes and, although the treasury regulations for 501(c)(4) do not say that political activities promote social welfare, they also do not ban political activities. Id. In light of these findings, the IRS ruled that “an organization may carry on lawful political activities and remain exempt under Section 501(c)(4) as long as it is primarily engaged in activities that promote social welfare.” Id.

156. See supra notes 39-51 and accompanying text for a list of possible exempt purposes. If the lobbying is not germane to the Section 501(c)(3) group’s exempt purpose, then the § 501(c)(3) could be subject to penalties.

157. This would violate the prohibition on campaign activities. “Primary purpose” is generally considered to be fifty-percent or more of the organization’s activities, but many commentators debate what should be enough activity to equal “primary purpose.” For a discussion on the status of the “primary purpose” standard, see Ellen P. Aprill, Once and Future Gift Taxation of Transfers to Section 501(c)(4) Organizations: Current Law, Constitutional Issues, and Policy Considerations, 15 J. OF LEGIS. & PUB. POL’Y 289, 302 (2011). However, like in the “substantial part” test discussed in supra Section III, the “primary purpose” test leaves open the possibility for these activities to be measured through “time and effort” spent, monetary expenditures, or through a multi-factor test. See supra Section III.
lobbying activities directly to the Section 501(c)(3) organization. Unlike contributions to a Section 501(c)(3) organization, contributions to a Section 501(c)(4) organization are not guaranteed to be deductible. It is worth noting that Section 501(c)(4) organizations, which are usually tax-exempt, are taxed on their involvement in political campaign activities. Nonetheless, it is significant that Section 501(c)(3) groups can maintain tax-exempt status by forming a Section 501(c)(4) affiliate to carry out the former’s political objectives. The Section 501(c)(3) organization can still control its affiliate through contributions it makes and by appointing and removing the Section 501(c)(4) organization’s board of directors, if this arrangement is desired and included in the Section 501(c)(4) group’s bylaws. Because the Section 501(c)(4) option is available, courts have less reason to be sympathetic to Section 501(c)(3) organizations that fail the “substantial part” test or the Section 501(h) test. In light of these circumstances, it behooves Section 501(c)(3) organizations anywhere close to the borderline to utilize the Section 501(c)(4) option.

A. Activities Germane to “Social Welfare” Purposes

The regulations define “social welfare” as bringing about “civic betterments and social improvements.” There are two primary activities that are not considered “social welfare”: (1) business activities; and (2) activities that are for the benefit of the group’s members. In

158. See generally Fei & Colvin, supra note 36. See infra Section V.2.
161. See Regan v. Taxation With Representation of Washington, 461 U.S. 540, 543-544 (1983). In this case, the Supreme Court held that a charity could not claim that its First Amendment right to free speech was unfairly limited because the group could have established a Section 501(c)(4) organization. Id. Compare the more recent ruling in Branch Ministries v. Rossotti, 211 F.3d 137, 143 (D.C. 2000).
163. Rev. Rul. 73-306, 1973-2 C.B. 179 (ruling that a nonprofit organization that assists tenants of an apartment complex in negotiations, litigation, and representation before governmental agencies does not qualify for the tax-exemption under Section 501(c)(4) because it did not benefit the community, broadly defined).
164. See also Rev. Rul. 69-280, 1969-1 C.B. 152 (ruling that a homeowners’ organization that provided outdoor maintenance to homes benefited only the group’s members, and not the community at-large).
165. See also Rev. Rul. 78-132, 1978-1 C.B. 157 (holding that an organization formed “to facilitate the exchange of personal services among members” does not serve to promote social welfare because only the organization’s members benefit). See also Am. Ass’n of Christian Schs. VEBA Welfare Plan Trust v. United States, 663 F. Supp. 275 (M.D. Ala. 1987), aff’d, 850 F.2d
contrast, any validly operating organization that fits the definition of a charitable organization under treasury regulation 1.501(c)(3)-1(d)(2), but not an action organization under treasury regulation 1.501(c)(3)-1(c)(3), will likely qualify.\footnote{1510 (11th Cir.1988) (holding that a tax-exempt association of churches that set up a trust for its employees should not receive tax-exempt status because its purpose is to benefit the organization's employees and not the community at-large). The organization argued that the trust provides benefits to the employees so that the employees can dedicate their efforts to promoting the general welfare, but the court found this argument to be unpersuasive. \textit{Id.}}

Further, case law and revenue rulings shed some light on what constitutes promoting "social welfare.” In Revenue Ruling 68-656, the IRS held that a Section 501(c)(4) organization was exempt because it informed the public about proposed legislation and lobbied for that legislation.\footnote{1515. Rev. Rul. 68-656, 1968-2 C.B. 216. Here, the organization set up through speaking engagements and circulated printed materials on a presently-illegal activity in attempt to legalize it. \textit{Id.} The illegal activity was germane to the organization’s purpose. \textit{Id.} The IRS ruled in favor of the organization because it found that its activities “educated” the citizenry. \textit{Id.}} The IRS ruled favorably on the grounds that this organization educated the public and “society benefits from an informed citizenry.”\footnote{1516. Rev. Rul. 68-656, 1968-2 C.B. 216. Here, the organization set up through speaking engagements and circulated printed materials on a presently-illegal activity in attempt to legalize it. \textit{Id.} The illegal activity was germane to the organization’s purpose. \textit{Id.} The IRS ruled in favor of the organization because it found that its activities “educated” the citizenry. \textit{Id.}}

In Revenue Ruling 71-530, the IRS upheld the exemption for an organization that worked to improve tax policies.\footnote{1517. Rev. Rul. 71-530, 1971-2 C.B. 237. This revenue ruling states in relevant part: [through presentations by qualified witnesses on pending or proposed tax legislation, the organization is promoting the common good and general welfare of the community by assisting legislators and administrators concerned with tax policy. Such activity helps the legislators and administrators form better judgments about the legislation. The fact that the organization’s only activities may involve advocating changes in law does not preclude the organization from qualifying under § 501(c)(4) of the Code. \textit{Id.}}} To achieve this goal, the organization conducted significant research on tax issues.\footnote{1518. Id.} In addition, its members regularly testified in legislative hearings for or against legislative proposals.\footnote{1519. Id.} The IRS justified this ruling on the grounds that the public benefits from having sound tax policies in

\section*{References}

\footnotesize
\begin{enumerate}
\item Contra Rev. Rul. 72-102, 1972-1 C.B. 149 (ruling an organization that protected the appearance of homes by passing and enforcing homeowners’ covenants, as well as maintaining the common areas in a subdivision, did benefit the community and not merely the group’s members).
\item See also Rev. Rul. 80-63, 1980-1 C.B. 116 (ruling that there is no one-size-fits-all definition for “community.” Instead, the facts and circumstances of each case define what exactly is the applicable community).
\item The policy goals of Section 501(c)(3) are parallel to Section 501(c)(4). Both subsections are intended to help organizations that contribute to the community, thereby reducing the government’s burden. \textit{See supra} note 5 for a discussion on competing policy rationales for Section 501(c)(3).
\item Rev. Rul. 68-656, 1968-2 C.B. 216. Here, the organization set up through speaking engagements and circulated printed materials on a presently-illegal activity in attempt to legalize it. \textit{Id.} The illegal activity was germane to the organization’s purpose. \textit{Id.} The IRS ruled in favor of the organization because it found that its activities “educated” the citizenry. \textit{Id.}}
\end{enumerate}
place.\textsuperscript{170} 

The most eye-catching case, however, came from the Second Circuit.\textsuperscript{171} In \textit{Debs Memorial Radio Fund, Inc. v. Commissioner},\textsuperscript{172} the court held that an exemption should be granted for an organization that operated a radio station that espoused leftist political views.\textsuperscript{173} The radio station was even established by the Socialist Party specifically to express its political viewpoints as a way to memorialize the passing of fellow leftist, Eugene Victor Debs.\textsuperscript{174} Despite the fact that the station was clearly run by political actors with political motives, the court ruled that these programs were “educational, civic and cultural in nature.”\textsuperscript{175}

Thus, both the IRS and the courts consider the dissemination of political opinions to be informative. In addition, direct communication with elected representatives to discuss legislation and frequently testifying in hearings is allowed if it is for laws that can benefit the public. Thus, under current law, Section 501(c)(4) organizations may engage in what amounts to both grassroots and direct lobbying.

\section*{B. Keeping the Section 501(c)(3) Organization Separate From the Section 501(c)(4) Organization}

In order for the two organizations to be recognized as legally separate, they must satisfy formalities that indicate they are distinct from

\begin{itemize}
\item \textsuperscript{170} \textit{Id.} A strong argument can be made that the purpose of all legislation, not just the tax laws, is to benefit the public. Therefore, this ruling likely has implications that are far broader than the facts of this particular revenue ruling.
\item \textsuperscript{171} Debs Memorial Radio Fund, Inc. v. Comm'r, 148 F.2d 948 (2d Cir. 1945).
\item \textsuperscript{172} \textit{Id.}
\item \textsuperscript{173} \textit{Id.}
\item \textsuperscript{174} \textit{Id.} at 951.
\item \textsuperscript{175} \textit{Id.} at 952. This case significantly stretched the definition of “educational.” \textit{Id.} Many observers would likely consider “educational” to mean: (1) allowing for a presentation of objective facts while leaving the audience to draw their own conclusions; or (2) presenting opinions on multiple sides of a political debate and letting audience decide which they believe. \textit{Id.} After all, these definitions of “educational” are the standards to which we generally hold college professors when they address political issues in the classroom. Many commentators perceive the injecting of opinions without at least providing a counterargument to be particularly un-educational. \textit{Id.}
\end{itemize}

The authors of both of these articles stress that their “educational” experience is greatly improved when professors avoid spoon-feeding an opinion to the students, but instead teach them the analytical process to solving problems and allowing students to reach their own conclusions.
one another. These formalities generally require the Section 501(c)(3) organization and Section 501(c)(4) affiliate to maintain separate organizational status and conduct all business between each other at arm’s length.

To determine whether the two organizations are sufficiently separate, courts follow the thrust of the United States Supreme Court’s ruling in Moline Properties, Inc. v. Commissioner. As a result, courts use the following four requirements. First, the organizations must be separately organized according to the relevant state’s filing and registration procedures. Second, the organizations must keep separate records and bank accounts. Third, if the organizations have overlapping paid officers, directors or employees, their time must be sufficiently tracked and allocated to the organization for which the services were rendered. Finally, the organizations must reasonably allocate shared property and services.

Although this case law, scholarship, and practitioner advice provides some guidance as to whether two organizations are separate, it

176. Fei & Colvin, supra note 36.
177. Ward L. Thomas & Judith Kindell, Affiliations Among Political, Lobbying, and Educational Organizations, I.R.S. (2000), available at http://www.irs.gov/pub/irs-tege/eotopics00.pdf. The IRS relies heavily on these formalities to determine whether two organizations are adequately separate. See Treas. Reg. § 56.4911-2(b)(2)(v) (2008). This regulation says that a § 501(c)(3) organization can distribute educational, non-political materials in furtherance of its exempt purpose. Id. Later, the affiliated § 501(c)(4) group can distribute those same materials, so long as they are qualified “advocacy communications or research materials,” as part of its campaign and lobbying activities. Id. This sequence of events, based on these facts alone, would not result in a determination that the organizations failed to follow the necessary formalities. Id.
178. Moline, 319 U.S. at 439. This case discussed the requirements for multiple corporations to be treated as separate for tax purposes. Id. See Justice Reed’s Majority opinion, which states that entities are treated as separate if the “purpose is the equivalent of business activity or is followed by the carrying on of business by the corporation. . . .” Id. at 439.

Determining whether two entities are separate for tax purposes is identical to determining whether entities are separate with respect to “piercing the corporate veil.” For scholarship on “piercing the corporate veil,” see generally Thomas V. Harris, Washington’s Doctrine of Corporate Disregard, 56 WASH. L. REV. 253 (1981); Jane C. Schlicht, Piercing the Nonprofit Corporate Veil, 66 MARQUETTE L. REV. 134, 140-43 (1981).

180. Id.
181. Id.
182. Id.
183. Id. at 439-40.
is lacking in two ways. First, it only sheds light on how corporate entities can be considered separate. Second, it fails to articulate the facts and circumstances that can definitively determine whether the organization has gone too far. For this reason, organizations have an incentive to handle these arrangements with significant caution.

C. The Taxation of Section 501(c)(4) Organizations

Donors’ contributions to Section 501(c)(4) groups are generally not deductible under Section 170. They could be deductible under Section 162 as a trade or business expense; however, Section 162(e) prevents a deduction for political campaign activities. The simultaneous application of Section 162(a) and Section 162(e) requires the Section 501(c)(4) organization to make one of two choices: (1) it can disclose to donors the amount of their contribution that is either deductible or is subject to the applicable marginal income tax rate, and thereby avoid tax at the Section 501(c)(4) entity level; or (2) the Section 501(c)(4) entity can pay the tax, thereby eliminating the need to tell donors how much of their contribution is deductible. Either way, no donation to a Section 501(c)(4) group to use for lobbying purposes (as opposed to general use) is a deductible expense.

The Section 527(f) tax applies to Section 501(c)(4) groups that engage in campaign activities and lobbying. This tax is an amount up to thirty five percent of the lesser of: (1) investment income; or (2) amounts spent on political campaign activities.

184. There are four entity choices for exempt organizations, including a: (1) corporation; (2) community chest; (3) fund; or (4) foundation. Granted, the application of these rulings to other entities are likely comparable, so differences should not be significant. See supra notes 40-41 and accompanying text.

185. For example, it does not specify whether “reasonably” allocate requires the allocations to fall within a specified percentage range of the fair market value.


187. I.R.C. § 162(a) (2008). This is only possible if the only trade or business in which the organization is engaged is lobbying.

188. Id. at § 162(e).

189. Id. at § 527(f)(1)(A)-(B). See also id. at § 527(b); § 11(b).

190. Most Section 501(c)(4) organizations do not pay taxes because usually no donors will get the Section 162 deduction and the Section 501(c)(4) organizations know the donors will not get the deduction.


192. Id. at § 527(f)(1).

193. Id. at § 527(f)(1)(A)-(B). See also id. at § 527(b); § 11(b). See generally McGlamery & Fei, supra note 2. This article explains that the rationale for creating the Section 527(f) tax was to prevent the use of Section 501(c) political organizations, which can engage in limited campaign
Thus, if a Section 501(c)(3) organization wants to engage in political activities and lobbying while still maintaining its tax-exempt status, then it should establish a Section 501(c)(4) affiliate. Although the affiliate faces limitations on the type and volume of campaign and lobbying activities in which it may participate and will be taxed for performing non-exempt functions, the Section 501(c)(4) affiliate can assist the Section 501(c)(3) organization through political involvement in which the Section 501(c)(3) group could not participate itself.

VI. PROPOSED SOLUTIONS

As often is the case, knowing the law here is only half the battle. In order to for Section 501(c)(3) organizations to protect their tax-exemption, they must also know how to apply the law to the activities in which they are engaged. For this reason, the discussion below describes which activities are likely acceptable for Section 501(c)(3) organizations that wish to maintain their tax-exempt status.

A. Focus on Activities That Are Not “Influencing Legislation”

Organizations interested in maintaining their tax-exempt status should avoid attempts to influence federal, state, and local statutes as well as referendums, initiatives, constitutional amendments, and judicial confirmations. However, organizations can engage in activities with the executive branch so long as those activities deal with regulations and administrative processes. Because the regulations often fill in the gaps left in the statutes and determine the manner in which they are administered, the executive branch rule allows a Section 501(c)(3) organization significant ability to help mold the parameters of a statute without engaging in lobbying. Thus, if an organization opposes a piece of legislation, it can attempt to dilute the statute by seeking the executive branch’s passage of regulations.

194. See supra notes 62-64 and accompanying text. See also Andersen, supra note 75, at 130. Andersen argues that the regulations create “an extremely broad definition of the term ‘legislation.’” Quoting Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii), Andersen emphasizes the broad scope as that which “includes action by Congress, by any State legislature, by any local council or similar governing body, or by the public in a referendum initiative, constitutional amendment, or similar procedure.” Andersen, supra note 75, at 130. This inevitably works to the disadvantage of Section 501(c)(3) organizations by placing greater restrictions on the options available to them if they wish to maintain their tax-exempt status.

195. See supra note 65 and accompanying text.

196. See James L. Gattuso & Stephen Keen, Red Tape Rising: Regulation in the Obama Era
In addition, specific types of Section 501(c)(3) organizations can interact with the judicial branch through litigation. Thus, these organizations can attempt to strike down unfavorable legislation through the court system.

If an organization cannot avoid the legislative branch on a particular law, then it should ensure that its actions are not construed as “influencing” legislation. This means that the organization should avoid contacting legislators, legislative staff members, or members of the executive or judicial branch to persuade them to exert their influence on legislators to take a particular position on legislation. Nevertheless, organizations can demonstrate that they are willing to offer good testimony on a proposed law during legislative hearings. Testifying in such hearings is not considered an attempt to influence legislation, although it is clearly an opportunity for an organization to present its case to a group of legislators.

In addition, organizations can conduct nonpartisan studies and analyses. They can then disseminate the results of such studies to

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197. See supra note 66 and accompanying text. The four types of organizations are: (1) legal aid organizations; (2) human and civil rights defense organizations; (3) public interest law firms; and (4) organizations that attempt to achieve charitable goals through the instrument of litigation as plaintiff. Supra note 66 and accompanying text. The last category opens the door for virtually any charitable organization to engage in litigation so long as it can demonstrate that it is doing so in furtherance of its tax-exempt purpose (which is the same standard for any charitable organization to maintain its tax-exempt status during any of its activities). Supra note 66 and accompanying text. Thus, the litigation context neither inhibits nor expands an organization’s access to tax-exempt status. Supra note 66 and accompanying text.

198. Supra note 66 and accompanying text.

199. See supra notes 67-70 and accompanying text. Note that organizations may contact members of the executive branch in an attempt to persuade them to change regulations, but not to influence legislation as defined in Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii) (2008).

200. See Rev. Rul. 70-449, 1970-2 C.B. 112. According to the language of Rev. Rul. 70-449, organizations that are invited to speak in a legislative hearing can utilize that opportunity to suggest legislative proposals that could benefit the organization. Id. Still, it would be wise for organizations to avoid aggressively pursuing this as an end-around strategy to engage in lobbying as the IRS could find overzealous advocacy in this context to, in fact, be lobbying.

legislators and the general public. Of course, these results need to allow the audience to come to its own conclusion so as not to appear one-sided and thereby attempting to influence legislation.

Organizations need to be cognizant of interactions with the general public as well as their involvement with legislators. Unfortunately for organizations not making the Section 501(h) election, the case law on molding public opinion directly contradicts the treasury regulations. After all, the courts say that molding public opinion generally is lobbying while the regulations say that it is not. Nonetheless, even the courts and the IRS tend to respect tax-exempt activities when they are closely tied to a constitutional right and the molding of public opinion is somewhat limited in scope.

For example, a university can be confident that courts and the IRS will respect its student newspaper that is distributed only on campus. Even if the newspaper contains political opinions and is funded by the university, college campuses are marketplaces of ideas. Of course, a university would benefit from exerting little, if any, control over the content of the newspaper. Similarly, pastors have been comfortable stating political opinions to church members on free exercise grounds, but some commentators suggest that this area of law is a ticking time bomb. As a result, these commentators predict that the IRS may buckle down and start revoking more exemptions. Even if the IRS does not revoke these exemptions, it has shown that it can tarnish a church’s name, and that should be enough to deter churches. Either way, pastors should likely avoid disseminating such opinions on the church’s behalf to the mass media.

202. See id.; supra note 123 and accompanying text.

203. See Christian Echoes v. United States, 470 F.2d 849 (10th Cir. 1972), cert. denied, 414 U.S. 864 (1973); supra notes 74-75 and accompanying text.

204. Christian Echoes, 470 F.2d 849. The ruling in Christian Echoes held that attempting to mold public opinion is lobbying, whereas Treas. Reg. § 1.501(c)(3)-1(d)(2) explicitly says it is not.

205. Id.

206. See supra notes 75-79 and accompanying text.

207. See supra notes 76-79 and accompanying text.

208. See supra note 76-79 and accompanying text.

209. See supra notes 75-77. Note that some commentators argue that this practice is on thin ice and the IRS is looking for a chance to pounce soon. Other commentators actually argue that the freedom of political speech is broadening in the wake of Citizens United. Either way, according to the interpretation in Slevin, supra note 36, the IRS will get the opportunity to react. Even if the IRS does not succeed in revoking a church’s, or any other organization’s exemption, see the discussion in supra note 74, which points out the IRS can still certainly destroy the organization’s reputation.

210. See supra note 75 and accompanying text.

211. See supra note 75 and accompanying text.

212. See supra note 75 and accompanying text.
B. Ensure That Lobbying Activities Are “Insubstantial”

If an organization cannot avoid influencing legislation, then it must limit such activities to an insubstantial amount. The organization should adhere to one of three tests, depending on which jurisdiction’s rules apply to the organization. Generally an organization should expect to maintain its tax-exempt status as long as its lobbying activities do not exceed five- to ten-percent of its total activities pursuant to the jurisdiction’s test. If an organization is above that threshold, then it should seek the Section 501(h) expenditures election at the end of the year.

C. Make the Section 501(h) Expenditure Election

The Section 501(h) election makes compliance fairly straightforward. For this reason, if an organization is anywhere close to surpassing the limits in the “substantial part” test, it should consider the Section 501(h) expenditure election. Organizations should, to the extent possible, focus on performing the six excepted activities and avoid the three forms of lobbying. To the extent an organization must perform lobbying activities, it should ensure that these activities do not exceed the expenditure limits.

If the organization exceeds both the threshold and the Section 501(h) limits, then it should not make the Section 501(h) election but its exemption stands on shaky ground in the more subjective “substantial

213. See supra Section III.2.
214. See supra note 114-116 and accompanying text. Also note that although the “substantial part” test provides significant uncertainty, as organizations are forced to rely on perhaps shaky case law, greater than ninety-percent of public charities under Section 501(c)(3) opt to remain subject to it. See The Law: IRS Rules, CTR. FOR LOBBYING IN THE PUB. INT., www.clpi.org/protect-advocacy-rights/clpipublicpolicy (last visited May 11, 2013).
216. See supra Section IV.
part” analysis. The best option at that point would be to emphasize factors beyond either “time and effort” or money to show the organization’s activities were not substantial. To do this, the organization could point out facilities and property used, information dissemination, and community reputation to demonstrate that the organization’s activities were not substantial. Given the uncertainty of this position, if an organization consistently finds itself beyond the threshold and exceeding the Section 501(h) test, then it should set up a Section 501(c)(4) organization to do its lobbying work. 217

D. Use a Section 501(c)(4) Organization for Campaign and Lobbying Activities

A Section 501(c)(3) organization can use a Section 501(c)(4) organization to perform its political work. 218 This means that Section 501(c)(4) organizations can engage in direct and grassroots lobbying, so long as the public benefits from these lobbying activities. 219 The “social welfare” activities in which Section 501(c)(4) organizations can participate include informing the public about legislation and lobbying for that legislation, researching and testifying on legislative issues, and even mass distributing partisan political propaganda. 220

The Section 501(c)(3) organizations must remain separate from the Section 501(c)(4) affiliates in order to prevent the Section 501(c)(4) organization’s activities from being attributed to the Section 501(c)(3) organization, causing the Section 501(c)(3) organization to face penalties and possibly lose its tax-exemption. 221 The organizations can prove that they are separate by forming separate legal entities, keeping separate records and bank accounts, tracking the work performed by employees who work in both organizations and definitively allocating that work to the proper organization, and allocating any shared property and services to the proper organization. 222

217. See supra Section V. Note that this area of the law is rapidly changing and is worthy of close attention because of the impact Crossroads Grassroots Policy Strategies played in the 2010 election and then in losing its tax-exempt status in 2012. See supra note 151.

Legal scholarship has not adequately kept up with the use of Section 501(c)(4) organizations, particularly in the wake of Citizens United. It is also important to note that, given the enormous attention the public has given § 501(c)(4) organizations (despite the legal scholarship’s apparent inattention to them), new legislation and regulations may be on the horizon.

218. See supra Section V.
219. See supra notes 152-159 and accompanying text.
220. See supra notes 165-175 and accompanying text.
221. See supra Section V.2.
222. See supra Section V.2.
A Section 501(c)(3) organization should avoid giving money to a Section 501(c)(4) organization for political activities, to the extent possible.\textsuperscript{223} In addition, donors should be less inclined to make donations to Section 501(c)(4) organizations for lobbying expenses because those donations are not tax-deductible.\textsuperscript{224} Any Section 501(c)(4) organization that engages in lobbying should know ahead of time that doing so will require it to pay the Section 527 tax.\textsuperscript{225}

VII. CONCLUSION

Drawing a distinct line between the charitable and political sectors is nearly impossible in America. Even charities that have the best of intentions may occasionally find themselves drifting into the lobbying arena. This is because American culture celebrates the freedom of individuals to associate with whom they please and for whatever purpose they please. With such a vast array of charitable organizations advancing their own causes and voicing their own opinions, it is impossible for them to avoid politics entirely.

Still, there are strong public policy reasons to keep the charitable sector removed from the political process as much as possible. Charities perform vital functions that benefit individual citizens, communities, and the government. For this reason, one can make a strong policy argument that charities must remain neutral to ensure they do not gain a reputation for being mere political cohorts while hiding under the guise of community service-provider. After all, this negative connotation could cause their donations to plummet and their members to stop volunteering. This in turn would have disastrous consequences for beneficiaries of charities, a class that includes nearly everyone, either directly or indirectly.

Given this tension, it is not surprising that tax-exempt organizations provide one of the most fascinating areas of the law to observe, especially during election years when lobbying activities emerge to the forefront. It is a time when Section 501(c)(3) organizations must understand their political limitations as outlined in this Article, or face harsh tax consequences for their failure to do so.

\textsuperscript{223} See supra Section V.3.
\textsuperscript{224} See supra Section V.3.
\textsuperscript{225} See supra Section V.3.
Appendix

Alpha, Beta, and Chi are all Section 501(c)(3) organizations. They have satisfied all requirements and formalities to maintain their Section 501(c)(3) status, and they are identical in all aspects unless otherwise noted below.

<table>
<thead>
<tr>
<th>Organization</th>
<th>Status</th>
<th>Step 1</th>
<th>Step 2</th>
<th>Step 3</th>
<th>Step 4</th>
<th>Step 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alpha</td>
<td>Pass</td>
<td>$1,200,000</td>
<td>$195,000</td>
<td>GLE: $20,000</td>
<td>$20,000</td>
<td>$0</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>CLE: $175,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Beta</td>
<td>Fail</td>
<td>$1,200,000</td>
<td>$195,000</td>
<td>GLE: $30,000</td>
<td>$30,000</td>
<td>.25 x</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>CLE: $175,000</td>
<td></td>
<td>$10,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>=</td>
</tr>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$2,500</td>
</tr>
<tr>
<td>Chi</td>
<td>Fail</td>
<td>$1,200,000</td>
<td>$195,000</td>
<td>GLE: $95,000</td>
<td>$95,000</td>
<td>.25 x</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>CLE: $100,000</td>
<td></td>
<td>$70,000</td>
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<td></td>
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</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$17,500</td>
</tr>
</tbody>
</table>

Note:
Grassroots lobbying expenditures = GLE
Combined lobbying expenditures = CLE

Alpha followed the statute and therefore incurred no tax. As a result, Alpha’s tax-exempt status has been fully protected.

Beta had grassroots lobbying expenditures at less than or equal to combined lobbying expenditures, but had combined lobbying expenditures $10,000 in excess of the allowed amount. As a result, Beta owes $2,500 in tax.

Chi had combined lobbying expenditures equal to the maximum amount, but had grassroots lobbying expenditures that were $70,000 in excess of the allowed amount. As a result, Chi owes $17,500 in tax.