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Response by Tax-Exempt Organization Scholars to Request for Information

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Dear Chairman Smith and Chairman Schweikert:

As academics who study and write about tax-exempt organizations, including their politically related activities, we would like to respond to your invitation regarding issues in connection with the advocacy activities of tax-exempt organizations. Below we note certain aspects of current law and provide an appendix with a list of our relevant scholarship. All views expressed are those of the individuals listed below and not of their institutions.

As a preliminary matter, because the committee is interested in the "Political Activities of Tax-Exempt Organizations," we emphasize the importance of the voice of tax-exempt organizations to a well-functioning civil society and democracy. As John W. Gardner has written, the nonprofit or independent sector "is the natural home of nonmajoritarian impulses, movements, and values. It comfortably harbors innovators, maverick movements, groups which feel that they must fight for their place in the sun, and critics of both liberal and conservative persuasion." John Gardner, Foundation Center, The Independent Sector, in America's Voluntary Spirit ix (1983). And, as Alexis de Tocqueville observed, the strength of American democracy is based on the inclination of its citizens to come together in associations to pursue their shared desires. Alexis de Tocqueville, Of the Use Which Americans Make of Public Associations and Civic Life, Section 2, Chapter V in Democracy in America, Volume II (1840).

We also wish to emphasize that in no case do the laws applicable to tax-exempt organizations forbid all political activity, a term almost without boundaries if "political" means related to government. The tax law delineates among a wide array of advocacy or "political" activities, some of which are limited, and others of which are not. For example, section 501(c)(3) organizations are allowed to lobby so long as lobbying activity is not a substantial part of their activities. Lobbying, however, is a technical term and does not include many activities to influence government action. Lobbying the executive branch, for example, is not considered lobbying for tax purposes and so is not subject to the lobbying limits. And while section 501(c)(3) organizations are prohibited from participating or intervening in "any political campaign on behalf of (or in opposition to) any candidate for public office," they are permitted to engage in issue advocacy, and often do. Section 501(c)(4) social welfare organizations face different constraints. They can lobby without limit regarding issues related to their exempt purpose. Under the applicable regulations, promotion of social welfare does not include direct or indirect campaign intervention on behalf of or in opposition to a candidate for public office, but such organizations can engage in such intervention so long as

they are "primarily engaged in promoting in some way the common good and general welfare of the people of the community." Treas. Reg. § 1.501(c)(4)-1(a)(2). Any consideration of political activity by exempt organizations must take care to specify the kind of political activity and type of tax-exempt organization under review.

In particular, we have all encountered a widespread misapprehension that tax law requires section 501(c)(3) organizations to be nonpartisan as a general matter, that is, to avoid taking positions with respect to legislation and public policy issues that might consistently align with one party or another. That is simply not the case. Section 501(c)(3) organizations are required to abstain only from activities that support or oppose a candidate for public office. For lobbying (to the extent permitted) and for issue advocacy, section 501(c)(3) organizations are free to take positions that are partisan in the sense that they might as a practical matter favor one party or another. The ability of nonprofits to express their opinions on the issues of the day is crucial to ensuring the pluralism and diversity of viewpoints we prize as a society.

Below please find more specific observations as to current law and citations to work we have published on the topics discussed.

1. VOTER EDUCATION, VOTER REGISTRATION, AND GOTV EFFORTS

The right to vote is essential to a well-functioning democracy. Activities of section 501(c)(3) organizations relating to the act of voting, such as providing information about candidate positions on issues, registering voters, or encouraging voters to vote do not standing alone constitute the participation or intervention in a political campaign *on behalf of or in opposition to* a particular candidate. In fact, tax law has long recognized the role of tax-exempt organizations in supporting the democratic process through voter registration, voter education, and get out the vote efforts. *See* Revenue Ruling 2007-41, https://www.irs.gov/pub/irs-tege/rr2007-41.pdf (recognizing that section 501(c)(3) organizations can engage in voter education and registration activities if they do so in a neutral or nonpartisan manner). That said, charitable organizations, qualified under section 501(c)(3), cannot engage in a voter registration drive in a manner that clearly favors or opposes one or more candidates. For example, registering voters at a state fair booth without reference to any candidate or political party (other than official voter registration forms) satisfies the requirements for neutrality in this context. *Id*. On the other hand, if the voter registration drive systematically turned away voters of one party, that would be campaign intervention. Importantly we think to your query, the percentage of voters who register with one party or another at a voter registration drive sponsored by a tax-exempt organization is not and should not be a factor in whether the effort is nonpartisan. Any test that turned on result would, as a practical matter, make it impossible for section 501(c)(3) organizations to undertake these important efforts.

2. GUIDANCE AS TO THE DEFINITION OF CAMPAIGN INTERVENTION AND THE EXTENT OF SUCH INTERVENTION PERMITTED TO TAX-EXEMPT ORGANIZATIONS, PARTICULARLY SECTION 501(c)(4) SOCIAL WELFARE ORGANIZATIONS.

Unquestionably, guidance is needed regarding the definition of campaign intervention permitted to tax-exempt organizations, especially with respect to section 501(c)(4) organizations. There is

currently no official guidance as to the extent to which section 501(c)(4) organizations can engage in campaign intervention without violating the requirement that they primarily engage in social welfare. Neither is there guidance as to how to measure such activity, whether, for example, only by dollars spent or also by including such factors as volunteer time.

Determining the percentage of permitted nonsocial welfare activity and specifying how to measure that percentage are difficult tasks, and we are not prepared at this time to make recommendations as to either. We do, however, believe these tasks should be undertaken. In general, Congress has taken the position that the government should not subsidize lobbying or campaign intervention. Thus, section 162(e) denies businesses deductions for these activities. At the same time, tax-exempt entities are permitted to engage in such activities to varying degrees. In order to carry out congressional policy and enable the IRS to enforce applicable rules while also protecting the right of exempt organizations to engage in robust dialogue essential to a strong democratic order, it is important that the rules be as clear as possible.

We note that developing better, clearer rules for permitted section 501(c)(4) activities also calls for additional guidance as to the meaning of "primarily" for purposes of defining a political organization under section 527. Section 501(c)(4) organizations cannot engage "primarily" in campaign intervention; section 527 organizations must engage primarily in campaign intervention. (Section 527 calls such activity an "exempt function," a term that is somewhat broader than campaign intervention because it includes certain appointed positions. *See* section 527(e)(2).) Section 501(c)(4) and section 527 need to be consistent in how they define and treat campaign activities.

The Treasury Department, however, may not promulgate necessary guidance under current law. Current appropriations legislation contains a rule, first imposed in 2015, that prohibits the Treasury Department from spending any funds related to guidance on the extent to which section 501(c)(4) organizations may engage in activity, such as campaign intervention, that is not deemed related to their exempt purpose. *See* Consolidated Appropriations Act, 2023, Pub. L. No. 117-328, Div. E, § 123, 136 Stat. 4459, 4659-60 (2022). Thus, under current law, the IRS may not issue guidance on this important issue. We urge Congress to lift this restriction so that the IRS can develop needed guidance with appropriate notice and comment procedures. The current state of affairs is a fraught one for both the IRS trying to properly enforce the law and for tax-exempt organizations trying to comply with that law.

3. DISCLOSURE OF MAJOR DONORS

Under current Treasury regulations, *see* T.D. 9898, noncharitable tax-exempt organizations no longer need to include the names and addresses of major donors on non-public Schedule B of Form 990, the information return filed annually with the IRS. In your Request for Information, you note that according to the Government Accountability Office, the IRS does "not review the national origin of sources of donations reported" and you ask whether the IRS should conduct such a review. The 2020 change to the regulations, however, undermines the ability of the government to identify donors who may raise concerns, including foreign donors. Thus, a foreign donor can donate substantial sums to a section 501(c)(4) organization unbeknownst to the IRS. In turn, the 501(c)(4)

may engage in substantial campaign activity, which is facilitated in amount by the lack of guidance in this area – guidance barred by the appropriation restriction mentioned above. Because a major foreign donor is not reportable on Form 990, the 2020 change to the regulations thus facilitates unlawful foreign funding of our electoral processes. We urge Congress to enact legislation that closes this loophole.

4. A NEW STUDY OF CAMPAIGN INTERVENTION BY EXEMPT ORGANIZATIONS

In the 2000s, the IRS launched the Political Activities Compliance Initiative (PACI) to address alleged violations of the political campaign intervention prohibition under sections 501(c)(3) and 170(c)(2). The IRS ended this initiative in 2008. Some twelve years later, in 2020, the GAO reported that during fiscal years 2010 through 2017 the IRS conducted and closed only 226 examinations relating to political campaign intervention, with 205 examinations involving section 501(c)(3) organizations or an average of less than twenty-six per year. *See* Report from Rebecca Gambler, Director, Homeland Security and Justice, U.S. Gov't Accountability Off. to Amy Klobuchar, Ranking Member, U.S. Senate Committee on Rules and Administration, Feb. 3, 2020, at 41, https://www.gao.gov/assets/710/705927.pdf. We agree that a new study is needed. We recommend that the GAO follow up on its 2020 Report and conduct essentially a new PACI, albeit one that does not involve actual examinations of section 501(c)(3) organizations but instead only gathers information about possible violations of the political campaign intervention prohibition.

5. AFFILIATIONS BETWEEN CHARITABLE AND NONCHARITABLE TAX-EXEMPT ORGANIZATIONS

Your Request for Information remarks that, according to news reports, some section 501(c)(3) organizations have "created spin off 501(c)(4) organizations to have greater freedom to engage in lobbying and partisan political activities." A section 501(c)(3) organization's use of affiliated entities to engage in lobbying and campaign activity is not inherently of concern, however, so long as the 501(c)(3) maintains its corporate independence and does not fund activity it could not engage in directly. As noted earlier, different categories of section 501(c) have different restrictions as to different kinds of political activities. Because section 501(c)(3) organizations face the most restrictions, it is commonplace for them to establish section 501(c)(4) affiliates, which in turn may also set up a section 527 PAC. As your letter suggests, this structure allows the 501(c)(3) a "greater freedom" to engage in these activities, albeit indirectly. This freedom to use affiliates was the basis of Justice Blackmun's concurring opinion in Regan v. Taxation with Representation of Washington, 481 U.S. 540, 551 (1983), which upheld the section 501(c)(3) limitation on lobbying in the face of a First Amendment challenge. A year later, the Supreme Court endorsed Justice Blackmun's position. F.C.C. v. League of Women Voters, 468 U.S. 364, 399-400 (1984).

Consistent with Supreme Court precedent, under current applicable guidance, a section 501(c)(3) organization can control an affiliated noncharitable entity by giving it the authority to appoint all or a majority of the latter's board. Noncharitable section 501(c) organizations, in turn, can create political action committees. These affiliated entities must follow several strictures. For example, tax-deductible contributions cannot be used to support the activities of a noncharitable entity; finances must be kept separate. *See* IRS 2000 EO CPE Text, *Affiliations among Political,*

Lobbying and Educational Organizations, https://www.irs.gov/pub/irs-tege/eotopics00.pdf. These structures also follow from the general principle of tax law expressed in Moline Properties v. Commissioner, 319 U.S. 436 (1943), of respecting corporate form. Individuals who serve on the board of both a charitable entity and its affiliated noncharitable entity will owe distinct fiduciary obligations to each and must be clear as to which organization they represent. That is, under general principles of tax law, the campaign or substantial lobbying activities of a noncharitable entity do not presumptively taint the charitable entity.

We hope this submission will prove helpful to you. Please do not hesitate to contact any of us if you have any further questions. (Affiliation for identification purposes only).

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APPENDIX

BIBLIOGRAPHY

Ellen P Aprill and Lloyd Hitoshi Mayer, *21st Century Churches and Federal Tax Law (forthcoming* 2024 UNIV. OF ILL. L. REV.), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4346286.

This article focuses on the benefits and burdens churches face as exempt organizations under section 501(c)(3). In light of recent developments, it recommends changes to the longstanding IRS approaches to defining "church" and certain church-related entities. Moreover, it recommends that GAO undertake a renewed study of campaign intervention by section 501(c)(3) organizations generally.

Ellen P. Aprill, *The Section 527 Obstacle to Meaningful Section 501(c)(4) Regulation,* 13 PITT. TAX REV. 43 (2015), https://taxreview.law.pitt.edu/ojs/taxreview/article/view/40.

This article reviews the 2013 proposed section 501(c)(4) regulations, describes section 527, and the difficulties posed by any attempt to coordinate their operation. It suggests that all organizations, including section 501(c) organizations, be permitted to engage in political

campaign intervention only through separate section 527 organizations to which contributions must be made directly.

Ellen P. Aprill, *Once and Future Gift Taxation to Section 501(c)(4) Organizations: Current Law, Constitutional Issues, and Policy Considerations,* 15 NYU J. LEGIS. & PUB. POL'Y 289 (2012), https://www.nyujlpp.org/wp-content/uploads/2012/10/Aprill-Once-and-Future-Gift-Taxation.pdf.

Written prior to the 2015 legislation exempting contributions to sections 501(c)(4), (c)(5), and (c)(6) organizations from the gift tax, this article argues that it would be constitutional to subject contributions to section 501(c)(4) organizations to gift tax but that policy considerations argue against doing so. In particular, it argues that the similarities between section 501(c)(4) organizations and section 501(c)(3) organizations, on the one hand, and section 527 organizations, on the other, calls for all three types of entities to be treated in the same way for gift tax purposes.

Ellen P. Aprill, *Regulating the Political Speech of Noncharitable Exempt Organizations after* Citizens United, 10 ELECTION LAW J. 363 (2011), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1727565.

After reviewing *Taxation with Representation* and its progeny as well as the history of section 527, this article offers a reconciliation of seemingly contradictory language *Taxation with Representation* and *Citizens United* regarding use of affiliates to conclude that *Citizens United* has not *sub silento* overruled *Taxation with Representation's* "no duty to subsidize" holding. It also proposes a number of reforms for noncharitable exempt organizations primarily engaged in lobbying and politicking, including requiring exemption for application, establishing a new category of exempt organizations primarily engaged in lobbying, and taxing the politicking expenditures of noncharitable tax-exempt organizations not conducted through a separate segregated fund.

Roger Colinvaux, *Social Welfare and Political Organizations: Ending the Plague of Inconsistency,* 21 N.Y.U. J. LEGIS. & PUB. POL'Y 481 (2018), https://nyujlpp.org/wp-content/uploads/2019/10/Colinvaux-Social-Welfare-and-Political-Organizations-21-NYUJLegis-481.pdf.

The article explains how after *Citizens United*, the inconsistency in tax law between section 501(c)(4) and section 527 groups made section 501(c)(4) an attractive vehicle for conducting campaign activity, to catastrophic effect. In particular, the ambiguity around permissible levels of campaign activity by section 501(c)(4) organizations combined with Congress's mandate that the IRS provide no guidance, opened the door to exploitation of the section 501(c)(4) tax status. The article argues that consistent disclosure and tax rules would help address the problem, as well as having fewer limits on politically related activities for non-charities.

Roger Colinvaux, *Political Activity Limits and Tax Exemption: A Gordian's Knot*, 34 VA. TAX REV. 1 (2014), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2476435.

This article explains the normative tax treatment for the politically related activities of nonprofits and the problems that arise from having different approaches for 501(c)(3)s, 501(c)(4)s, and 527s. The article argues that after *Citizens United*, the political activity limits on 501(c)(4)s are

not sustainable, but that consistent disclosure rules for all tax statuses are important to avoid abuse. The article argues that the tax on appreciated asset donations to section 527 organizations should be extended to other exempts, and that Congress should protect against abuse of money flows from section 501(c)(3) to section 501(c)(4) organizations. The article stresses that legislative solutions should minimize IRS involvement in enforcing political activity limits.

Roger Colinvaux, *The Political Speech of Charities in the Face of Citizens United: A Defense of Prohibition*, 62 CASE WESTERN RES. L. REV. 685 (2012), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1726407.

The article examines whether the section 501(c)(3) prohibition on campaign activity is constitutional in the wake of *Citizens United*, finding that it remains valid. The article also considers alternatives to prohibition and argues that present law, despite its imperfections, is preferable to the alternatives.

Roger Colinvaux, *Regulation of Political Organizations and the Red Herring of Tax-Exempt Status*, 59 NAT'L. TAX J. 531 (2007), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2265587.

The article explains that although section 527 generally should not be viewed as a tax subsidy, courts sometimes understand it as one. This affects the degree to which Congress may impose operational conditions on section 527 organizations as a condition of their tax status, as was done in the year 2000 when Congress imposed public disclosure requirements on 527s and required the IRS to administer them rather than the FEC.

Brian Galle, *The Dark Money Subsidy? Tax Policy and Donations to 501(c)(4) Organizations,* 22 AM. L. & ECON. REV. 339 (2020), https://academic.oup.com/aler/article-abstract/22/2/339/5979908.

This article presents the first empirical examination of giving to section 501(c)(4) organizations. It finds that gifts to section 501(c)(4) organizations are highly elastic to the after-tax price of charitable giving. That is, some donors appear to respond to the charitable contribution deduction as though it applied to gifts to section 501(c)(4) organizations. As a result, the charitable contribution deduction might well be encouraging meaningful amounts of untraceable donations to section 501(c)(4) organizations, in particular those engaged in considerable campaign intervention.

Brian Galle, *Charities in Politics: A Reappraisal,* 54 WM. & MARY L. REV. 1561 (2013), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3075508.

This article offers a set of policy reasons to separate politics, whether lobbying or electioneering, from charity. Combining politics with charity may impose higher agency costs, diminish "warm glow" from giving, and increase the number of recipients for which the tax incentive for donation was unneeded. Moreover, the efficiency of tax subsidies for charity depends in some part on their incidental effects on section 501(c)(4) social welfare organizations.

Philip Hackney, *Darker Money Darker? IRS Shutters Collection of Donor Data*, 25 FLA. TAX REV. 140 (2021), https://scholarship.law.pitt.edu/fac_articles/439/.

> This article evaluates the decision of the Treasury Department and the IRS to end a long-time regulatory position of requiring most tax-exempt organizations, including social welfare organizations, To disclose their substantial donors. It demonstrates that the IRS needs this donor information to enforce tax laws enacted by Congress such as the prohibition on inurement and the prohibition on excess benefit transactions under section 4958. It calls for the Treasury Department or Congress to again require these tax-exempt organizations to disclose their donors to the IRS on Form 990.

Philip Hackney, *Political Justice and Tax Policy: The Social Welfare Organizations Case,* 8 TEX. A&M L. REV. 271 (2021), https://scholarship.law.pitt.edu/fac_articles/101/.

> This article examines the democratic role played by social welfare organizations and how our tax policy interacts to either enhance or detract from democratic functioning. It argues that current policy allowing social welfare organizations an exemption from income tax for advocacy-based purposes negatively impacts our political order by giving greater benefit to the advocacy of wealthy interests. It argues Congress should impose an investment income tax and a tax on transfers of appreciated assets to social welfare organizations in the same way Congress applies these rules to section 527 organizations.

Lloyd Hitoshi Mayer, *Nonprofits, Taxes, and Speech*, 56 LOY. L.A. L. REV. (*forthcoming* 2023), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4357284.

> This article explores the limits on advocacy by tax-exempt nonprofit organizations. It concludes that the existing prohibition on political campaign intervention and the existing limit on lobbying by section 501(c)(3) organizations are constitutional and necessary to help implement Congress' decision not to allow tax deductions for spending on these activities. It also concludes that any attempt to limit other advocacy activities by section 501(c)(3) organizations would be both constitutionally suspect and inconsistent with overall tax policy. Finally, it concludes that the existing limit on political campaign intervention by non-charitable tax-exempt organizations is unwise as a policy matter and, in some circumstances, constitutionally suspect.

Lloyd Hitoshi Mayer, *When Soft Law Meets Hard Politics: Taming the Wild West of Nonprofit Political Involvement,* 45 J. LEG. 194 (2019), https://scholarship.law.nd.edu/jleg/vol45/iss2/3/.

> This article proposes a comprehensive regulatory approach to the involvement of tax-exempt nonprofits in politics, reflecting both the positive and negative aspects of that involvement. It recommends clarifying what constitutes prohibited political activity for section 501(c)(3) organizations to aid compliance and enforcement, as well as loosening the limits on political activity by noncharitable tax-exempt organizations. It also recommends refocusing public disclosure of election-related activity by tax-exempt organizations by both broadening the range of disclosed activity and increasing the dollar thresholds for triggering disclosure of donor information, while shifting responsibility for enforcing disclosure requirements from the IRS to the FEC and state election law agencies.

Lloyd Hitoshi Mayer, *The Much Maligned 527 and Institutional Choice*, 87 B.U. L. REV. 625 (2007), https://scholarship.law.nd.edu/cgi/viewcontent.cgi?article=1678&context=law_faculty_scholarship.

> This article examines the relative competency of the Federal Election Commission and the Internal Revenue Service when it comes to regulating election-related political activity. It concludes that the FEC is more accountable and effective when it comes to administering the public disclosure of information about donors to and expenditures by politically active nonprofit groups. It therefore recommends that Congress shift responsibility for the existing section 527 political organization disclosure requirements from the IRS to the FEC.