

CONFERENCE NOTES

Private Foundation Grants to Public Charities Engaged in Advocacy on Environmental Issues

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I. Overview

A. All private foundations are prohibited from funding or engaging in any "attempt to influence legislation." While this prohibition is absolute, it is also narrow and very clearly defined. In drafting the laws that restrict foundations' work in the policy arena, Congress and the IRS have taken considerable care to ensure that foundations can spend their resources on a broad array of activities that improve the quality of the legislative process. Hence, while there are certain kinds of policy-related work that foundations are strictly prohibited from supporting, there are many highly effective activities that are perfectly permissible. The purpose of this outline is to help foundations understand the rules that distinguish those activities foundations can support from those which they cannot.

B. In addition to providing a very favorable definition of "lobbying," the private foundation rules also offer several highly protective rules allowing foundations to make grants to organizations that lobby. In particular, the federal tax laws permit public charities to spend a set portion of their resources on lobbying each year. Consequently, foundations, particularly if they are actively supporting environmental groups, will frequently receive grant proposals from organizations that intend to lobby either as part of the project for which support is being requested or as part of their activities outside the project. The private foundation rules provide well defined safe harbors that will protect foundation grants from being treated as expenditures for prohibited lobbying activities.

C. Paying close attention to the rules and procedures discussed here will help private foundations take full advantage of their ability to support advocacy for improved environmental protections while complying fully with their legal obligations under the federal tax laws.

II. Limits on Private Foundation Lobbying

A. Private foundations are subject to a penalty tax under section 4945(d)(1) of the code on any "attempt to influence legislation." The penalty is 10 percent of the lobbying expenditures. Making a lobbying expenditure also triggers an obligation to "correct" the violation — that is, to recover the expenditure if possible and take whatever additional corrective action the IRS requires. Failure to meet this correction

obligation results in a second level penalty tax equal to 100 percent of the lobbying expenditure.

B. In addition, a private foundation may lose its tax-exempt status under section 501(c)(3) if attempting to influence legislation constitutes a "substantial part" of its activities during any tax year. Neither the IRS nor the courts have ever provided a precise quantitative definition of "substantial part" for these purposes. In one case during the 1960s, an organization lost its exemption under section 501(c)(3) when only 2 percent of its budget was spent on lobbying.

III. What Constitutes Lobbying: General Definitions

A. Sections 4945(d)(1) and (e) include as a taxable expenditure any amount paid or incurred by a private foundation for any attempt to influence legislation through:

1. An attempt to affect the opinion of the general public or any segment thereof (i.e., grassroots lobbying), or
2. Any communication with any member or employee of a legislative body, or with any other government official or employee who may participate in the formulation of the legislation (i.e., direct lobbying).

B. Under regulations enacted in 1990, an activity is lobbying for purposes of section 4945 only if it involves either a "direct lobbying communication" or a "grassroots lobbying communication."¹ Both of these terms have quite narrow, but rather technical, definitions. Foundations' abilities to take full advantage of the possibilities these rules provide for supporting policy-related activities depends on understanding these definitions and their application.

1. Direct lobbying

a. A direct lobbying communication is a communication with a legislator (federal, state, local, or foreign) or legislative staff member that refers to specific legislation and reflects a view on that legislation.

b. For purposes of these rules the term "specific legislation" includes the following:

- i. Federal, state, local, and foreign legislative action — e.g., acts, bills, resolutions and legislative vetos;

¹A schematic representation of the applicable tax law definition of lobbying is attached to this outline as Appendix A.

ii. Legislation that has already been introduced and specific legislative proposals that have not been introduced;

iii. Ballot initiatives and referenda; and

iv. Proposed treaties that must be submitted to the Senate for ratification — but only after negotiations have begun.

c. Specific legislation does *not* include discussion of issues of social concern and broad public policy, even though a particular issue may subsequently become, or even be the subject of specific legislation. Hence, it is not lobbying under the private foundation rules to meet with legislators or legislative staff to discuss an issue while legislation on that issue is pending, provided the meeting does not include a discussion of the legislation.

Examples: A meeting with a member of Congress to provide information about haze and degraded air quality in the Smoky Mountains while the Clean Air Act is up for reauthorization is not lobbying, so long as the discussion does not refer to the Act itself. Similarly, an open letter to legislators presenting statistical information about the condition of fisheries in the North Atlantic that did not refer to legislation would not be lobbying, even if the legislature was considering a bill to further restrict commercial fishing when the letter was mailed.

d. Specific legislation includes both legislation that has already been introduced and “specific legislative proposals” that have not yet been introduced — for example, draft legislation for which the organization is seeking sponsors. There are no clear criteria for determining at what point in the evolution of a legislative proposal it becomes sufficiently detailed to constitute “specific legislation.” However, it is clear that highly generalized proposals for policy reform do not constitute specific legislation and, therefore, that communications that make reference only to such generalized proposals are not lobbying communications.

e. *Communications with executive branch officials.* Specific legislation also does not include actions by administrative bodies — such as state and federal agencies, school boards, housing authorities and zoning boards. Consequently, most communications with executive branch officials are not lobbying for purposes of the private foundation rules. A communication with an executive branch official is direct lobbying only if.

i. The communication refers to and takes a position on legislation (not executive branch enforcement or interpretation action); and

ii. Its *primary* purpose is influencing legislation.

Examples: Meeting with a senior EPA official to discuss proposed clean air regulations is not lobbying, because implementing regulations are not legislation. But, asking the same EPA official to testify before a congressional committee in support of reauthorizing the Clean Air Act would be lobbying, because the primary purpose

of the communication to the EPA official is influencing legislation.

f. *Referenda and ballot initiatives.* Because referenda and ballot initiatives are specific legislation, communications with the general public that both refer to and take a position on a referendum or an initiative are direct lobbying under the private foundation rules.

2. Grassroots Lobbying

a. The private foundation rules define grassroots lobbying as a communication with the public that refers to specific legislation, takes a position on that legislation, and includes a “call to action.” Thus, a communication with the public, such as a radio or newspaper ad, that does not include a call to action will generally not be lobbying, even if it refers to and reflects a view on pending legislation. This aspect of the private foundation rules allows organizations to conduct effective grassroots, advocacy targeted on legislation without engaging in lobbying.

b. *Call to Action.* Under the private foundation rules, a call to action includes the following:

i. Urging the recipient to contact a legislator or staffer (e.g., “Tell Congress what you think,” “Call your Representative”);

ii. Providing the address or telephone number of a legislator;

iii. Providing a petition, tear-off postcard, etc. addressed to a legislator; or

iv. Identifying a legislator as opposing the legislation, as being undecided, as being a member of the committee considering the legislation, or as being the recipient’s representative. Identifying the sponsor of the legislation does not count as a call to action.

Example: A radio ad states that “Congress is currently considering a bill to allow logging in pristine wilderness areas in our state. This outrageous legislation would authorize the logging industry to destroy our most cherished natural areas. If this legislation is passed, you and your family will be never again be able to experience the majesty of old growth forests within our borders.” Although the message is clear that listeners should take action to oppose the bill, the ad is not grassroots lobbying because it does not include one of the four kinds of calls to action.

c. *Paid advertising.* In limited circumstances, paid mass media ads that run close to a vote on highly publicized legislation may be presumed to be grassroots lobbying even if they do not contain a call to action. Under a special rule, paid media ads are presumed to be lobbying communications if:

i. They occur within two weeks before a vote on highly publicized legislation;

ii. They reflect a view on the general subject of the legislation; and

iii. They either refer to the highly publicized legislation or encourage the public to communicate with legislators on the general subject of the legislation.

Legislation is “highly publicized” if (1) the legislation receives frequent coverage on television and radio, and in general circulation newspapers, during the two weeks preceding the vote by the legislative body or committee, and (2) the pendency of the legislation or the legislation’s general terms, purpose, or effect are known to a significant segment of the general public (as opposed to the particular interest groups directly affected) in the area in which the paid mass media advertisement appears.

3. Exceptions to the Definition of Lobbying

a. Even if an activity satisfies the basic definition of direct or grassroots lobbying, it may be permissible foundation activity because it falls within an exception to the lobbying definition.

b. Nonpartisan analysis and research. The most important exception to the definition of lobbying for many foundations involves the preparation and distribution of nonpartisan analysis and research. Under this exception, making available materials that present a sufficiently full and fair exposition of public policy issues to allow the recipient to form its own conclusions does not constitute lobbying, even if the materials both refer to and take a position on a specific legislative proposal. Although material qualifying as nonpartisan analysis must present both a developed argument for its position and the factual basis for that argument, it is not necessary to present “both sides” of an issue. To qualify for this exception, the material must be distributed to persons on both sides of the issue addressed — for example if the audience is members of Congress, then the material should be distributed to both Republicans and Democrats. In addition, if the audience is the public, the material must not explicitly encourage recipients to contact legislators (although it may identify legislators as holding a particular position on the legislation).

Example: A report documenting the health benefits of bill imposing tighter restrictions on the use of pesticides would have to include an analysis of objective data demonstrating the harmful health effects of pesticides on farm workers or consumers but would not necessarily have to present the chemical industry’s research disputing the connection between pesticide use and adverse health effects.

c. *Technical assistance.* A second important exception excludes oral or written responses to written requests for technical assistance from a legislative committee, subcommittee, or other governmental body from the definition of lobbying. In order to qualify for this exception, the written request must be an official request from the committee or subcommittee, not from an individual member asking on his own behalf. Similarly, the response must be made available to every member of the requesting body, committee, or subcommittee.

d. *Self-defense lobbying.* Third, communications *with government officials* involved in the legislative process likewise do not constitute lobbying for tax purposes if they concern legislation that could affect the foundation’s existence, powers, duties, tax-exempt status, or right to receive tax-deductible contributions. This exception does not apply to grassroots lobbying communications. In addition, the exception is only available if the legislation at issue would affect *the foundation’s* legal rights; it is not sufficient that the grantee’s rights would be affected.

e. *Jointly funded programs.* Finally, a narrow exception to the lobbying definition allows foundations (but not their grantees) to present information to government officials about a program that is, or may, be funded by both the foundation and the government, provided the communications are limited to the program.

IV. Grants to Organizations That Engage in Lobbying Activities

A. Although private foundations are prohibited from engaging in or supporting activities that constitute lobbying under the narrow definition provided above, the private foundation rules provide several highly favorable safe harbors under which grants to organizations that lobby will not be treated as expenditures for lobbying.²

1. *General Purpose Grants.* A private foundation may make a general purpose grant to a public charity engaged in lobbying activities provided that the grant is not “earmarked” to be used in an attempt to influence legislation.

- A private foundation grant is “earmarked” if the grant is given pursuant to an agreement, oral or written, that the grant will be used for specific purposes.

Example: A private foundation recognizes that a local environmental group it has supported in the past consistently achieves its environmental objectives in an efficient and highly effective manner. The organization’s activities including scientific research on the impact residential and industrial development is having on ecologically significant areas within the state, public education about this issue, organizing opportunities for volunteers to participate in environmental remediation projects, and lobbying on behalf of legislative and administrative policies that protect the environment. (All these activities are described in the organization’s annual report.) After reviewing the organization’s annual reports, mission statement, and IRS determination letter, the foundation makes a general support grant of \$100,000 to be spent within the next year. The grant agreement disclaims any ability of the foundation to control how the funds are used, and there are no other agreements between the foundation and the organization. The grant will not be an expenditure for lobbying by the foundation, even if the grantee uses some or all of the grant funds for lobbying.

²A schematic representation of the available grant making options is attached to this outline as Appendix B.

2. *Specific project grants.* A private foundation may also make a specific project grant to a public charity if three conditions are satisfied.

a. First, the grant must not be earmarked to be used in an attempt to influence legislation.

b. Second, the amount of the special project grant, together with other grants made by the same private foundation for the same project for the same year, must be less than or equal to the amount budgeted by the grantee organization for nonlobbying expenditures within the special project budget.

- If the grant is for more than one year, the preceding sentence applies to each year of the grant with the amount of the grant measured by the amount actually disbursed by the private foundation in each year or divided equally between the years, at the option of the private foundation. The same method of measuring the annual amount must be used in all years of a grant.

c. Third, the private foundation must not have any reason to doubt the accuracy of the budgetary information provided by the prospective grantee. Absent such reason to doubt the grantee, the foundation may rely on budget documents or other sufficient evidence supplied by the grantee organization (including a signed statement by an authorized officer, director, or trustee of the grantee organization) showing the proposed budget of the specific project.

Example: The public charity described in the preceding example submits a proposal seeking support for a project to protect an environmentally significant watershed. The project will include three activities: (1) researching and compiling information documenting the significance of the watershed and the risks to it; (2) running nonlobbying media advertisements educating the public about this issue; and (3) working to obtain passage of legislation restricting development in the area. The project budget indicates that total costs will be \$100,000. Of this amount, \$80,000 is allocated to activities that are not lobbying under the tax law. The foundation can make a grant for the project of up to \$80,000. Provided the foundation does not earmark its funds for lobbying and has no reason to doubt the accuracy of the grantee's materials, the grant will not be an expenditure for lobbying, even if the grantee in fact uses some or all of the grant funds to lobby.

3. Grants to Organizations that Cease to Qualify as Public Charities

a. Pursuant to the applicable regulations, a grant to a public charity that thereafter ceases to be an organization described in section 501(c)(3) by reason of its attempts to influence legislation is not a taxable expenditure for lobbying by a grantor foundation if the following conditions are satisfied:

i. The grant is a general support grant or a project grant that satisfies the requirements discussed above;

ii. The grantee organization had received a ruling, determination letter, or an advance ruling that it is a public charity within the meaning of sections 501(c)(3) and 509(a);

iii. The private foundation has not learned of the grantee's change in status because (1) notice has not been given to the public (such as by publication in the Internal Revenue Bulletin), and (2) the private foundation is unaware that the IRS has given notice to the grantee organization that it will lose its public charity status; and

iv. The private foundation does not directly or indirectly control the grantee organization. A grantee organization is controlled by a private foundation for this purpose if the private foundation and its disqualified persons can, by aggregating their votes or positions of authority, cause or prevent action on legislative issues by the grantee.

V. Lobbying Rules For Public Charities

A. In contrast to private foundations, public charities are permitted to engage in some lobbying. Public charities, other than churches and certain organizations affiliated with churches, have two options for determining the amount of lobbying they may engage in.

B. *Substantial part test.* Section 501(c)(3) provides that organizations are permitted to engage in lobbying activities so long as they do not devote a "substantial part" of their activities to attempting to influence legislation. The "substantial part test" employs a "facts and circumstances" approach to determining whether a substantial part of an organization's activities are devoted to influencing legislation. This analysis employs both qualitative and quantitative factors. Consequently, the test is vague, uncertain, and capable of subjective, and thus uneven, enforcement. The penalty for violating the substantial part test is revocation of the organization's tax-exempt status under section 501(c)(3).

C. *Section 501(h).* Recognizing that the vagueness of the substantial part test, coupled with the draconian sanction of revocation, was chilling lobbying activity by public charities, Congress enacted section 501(h). This provision sets precise expenditure limits on lobbying activities and employs a mechanical approach to determining whether an organization has complied with those limits. Organizations that exceed their lobbying limits generally are subject to a penalty tax — rather than revocation. Loss of tax exempt status is reserved as a sanction only for egregious violations. This regime provides public charities the certainty they need to participate with confidence in the legislative process.

The section 501(h) expenditure test is elective. That is, organizations only get the benefit of the mechanical expenditure test if they notify the IRS of their election to be subject to section 501(h). As noted above, churches and certain of their affiliates may not make the section 501(h) election. Whether an organization has made the section 501(h) election does not effect the rules applicable to private foundations making grants to the organization.

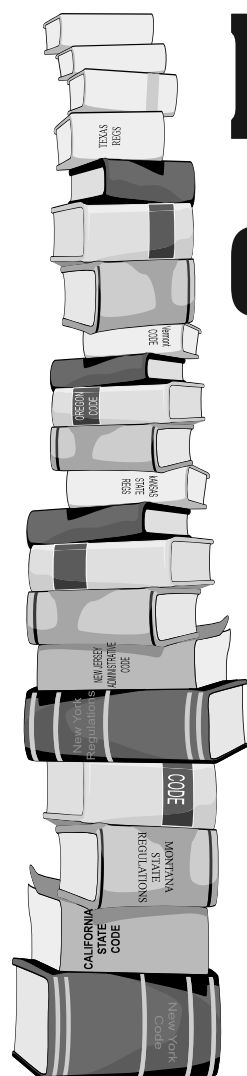
VI. Electioneering

A full discussion of the rules restricting election-related activities is beyond the scope of this outline. However, it bears emphasis that no organization exempt under section 501(c)(3) may intervene in a campaign for public office on behalf of (or in opposition to) any candidate. In general, a foundation grant will be treated as an expenditure for pro-

hibited election-related activity if it is earmarked — within the sense defined above — for such activity. Accordingly, foundation staff reviewing proposals should be on the lookout for activities that appear likely to benefit or hinder any political candidate, and clarify the permissible use of grant funds.

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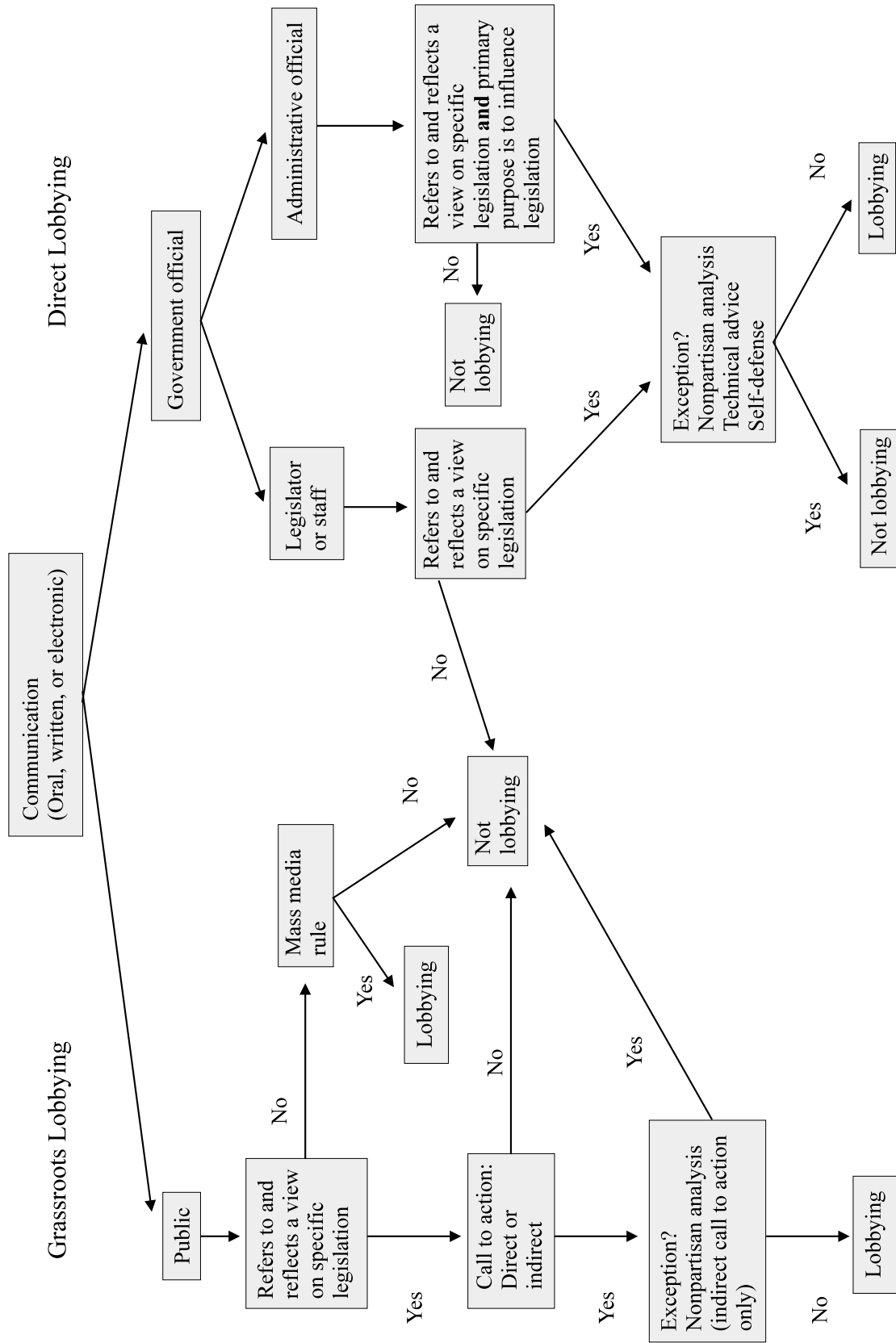
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APPENDIX A

Tax Definition of Lobbying



Permissible Grants Under the Ban on Lobbying Expenditures

