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Legal Brief

What the Law Allows

An overview of the laws that govern what private foundations can and can't do regarding involvement in the public policy process.

by Robert A. Boisture and Thomas A. Troyer

Since 1969, private foundations have been subject to a penalty tax under the Internal Revenue Code on any expenditure for an attempt to influence legislation. This rule has deterred most foundations from supporting activity that appears to bear even a tangential relationship to legislation. However, as clarified by Treasury regulations adopted in 1990, foundations, in fact, have considerable freedom to fund public charity grantees actively engaged in the public policy process and, indeed, to participate directly in that process in some ways.

Foundations' substantial scope for funding activities bearing on the public policy processnotwithstanding the general ban on private foundation lobbying expendituresderives from the interplay of three aspects of the governing tax rules:

The tax rules establish a favorable definition of lobbying. Under it, efforts to influence regulations, enforcement policies and other executive branch actions, as distinguished from legislative actions, are not lobbying. Further, as discussed below, it is often possible to design effective public education campaigns on public policy issues that do not fall within the tax rules' definition of lobbying.

The tax rules provide explicit exclusions from the definition of lobbyingparticularly the exclusion for so-called nonpartisan analysis, study, or researchthat create additional scope for funding activities that bear directly on the policy formation process.

Provided that a foundation does not earmark its grant to fund lobbying activities, a grantee's lobbying activities are generally not attributed to the foundation.

The Tax Law Definition of Lobbying

Under the tax law definition, lobbying is limited to making direct and grassroots lobbying communications. Thus, unless an entity has made a direct or grassroots lobbying communication, it has not engaged in lobbying.

A direct lobbying communication is a communication with a legislator, legislative staff, or other government official that refers to, and takes a position on, specific legislation or a specific legislative proposal. For this purpose, a communication will be treated as referring to specific legislation if it provides sufficient information to permit its audience to identify one or more specific bills or proposals as the subject of the communication.

Private foundations thus may properly fund generalized public education messages that discuss, and take clear positions on, broad public policy issues, provided that the communications do not refer to the specific legislative proposals.

Generally, a grassroots lobbying communication is any communication with the general public that refers to and takes a position on specific legislation or a specific legislative proposal *and includes* a call to action encouraging recipients to do something about the legislation. Informational campaigns designed to educate the public about public policy issues do not constitute lobbying if they do not include such calls to action.

The one circumstance under which communications with the general public may be treated as lobbying communications even if they do not contain a call to action involves paid mass media advertisements on highly publicized legislation which appear within two weeks of a legislative vote. Such advertisements will generally be treated as grassroots lobbying if they reflect a view on the general subject of the highly publicized legislation and either refer to the legislation or encourage the public to communicate with legislators on the general subject of the legislation.

In considering the tax law definition of lobbying, it is important to reiterate that while lobbying includes efforts to influence federal, state, local, and foreign legislative bodies and referenda and ballot initiatives, it does not include communications with executive branch officials who focus on administrative (distinguished from legislative) actions.

Exceptions to the Definition of Lobbying

After establishing the general definition of lobbying as outlined above, the tax rules recognize four important exceptions. Foundations are free to fund activities encompassed by one or more of these exceptions even if those activities would constitute lobbying under the general definition.

Nonpartisan analysis. Most important, making available the results of nonpartisan analysis on a legislative issue is not treated as lobbying even if the research report includes specific legislative recommendations. A communication qualifies as nonpartisan analysis if it:

- presents a sufficiently full and fair exposition of the pertinent facts as to permitthe public to form an independent opinion or conclusion,
- does not include a direct call to action (that is, does not explicitly encourage recipients to contact legislators or accomplish the same objective by providing such information or materials as legislators' addresses or phone numbers or preprinted postcards to send to legislators), and
- is not distributed to persons who are interested solely in one side of the issue.

The full and fair exposition standard requires the analysis to present a rational, fact-based argument in support of the report's conclusions, but it does not require that the report devote equal space to the discussion of alternative points of view. The tax rules also make clear that grants to support the preparation and distribution of nonpartisan analysis will not be treated as lobbying expenditures even if the grantee, or others, subsequently use the analysis as part of a lobbying communication unless a foundation's primary purpose in funding the analysis was to support the grantee's lobbying or the foundation knew, or had reason to know, that the grantee's primary purpose in performing the research project was for

lobbying use.

Self-defense. A second exception protects communications with legislators, their staffs, and executive branch officials involved in the legislative process concerning legislation that might affect a private foundation's existence, powers and duties, tax-exempt status, or right to receive tax-deductible contributions. This exception permits foundations to fund communications with legislators and government officialsbut not with the general publicon a range of important issues, including, for example, proposed changes in the rules on the deductibility of gifts to foundations or proposed changes in the rules governing foundation participation in the public policy process.

Technical assistance. A further exception excludes response to written requests for technical assistance from a legislative committee or subcommittee or other governmental body. Such requests can provide organizations with broad scope for presenting legislatorsbut, again, not the general publicwith facts, analysis and recommendations on legislative issues.

Discussions of broad social issues. Finally, the regulations exclude from the definition of lobbying discussions of broad social, economic and similar problems, even if the problems are the subject of legislation already pending before a legislative body. This exception affords a further opening for foundations to fund communications on general policy issuesfor example, the importance of strong environmental protection standards or a strong national defenseprovided the communications do not address specific legislation.

Grants to public charities that lobby. Most foundation grantees qualify as public charities for federal tax purposes, and as such may elect to be subject to substantially more liberal rules on lobbying activities. Specifically, an electing public charity may make lobbying expenditures up to 20 percent of the first $500,000 of its charitable expenditures, and declining percentages thereafter, up to a maximum of $1 million each year. These permitted lobbying expenditures, combined with the favorable rules on what does, and does not, constitute lobbying, permit public charitiesparticularly those with a substantial base of non-lobbying expendituresto play a quite active role in the legislative process.

The tax rules in turn, permit private foundations to make both general support and project grants to public charities engaged in lobbying activities. General support grants are permitted so long as the funds are not earmarked for lobbyingthat is, so long as the public charity does not agree to use the funds for that purpose. Project grants are permittedeven if the project includes some lobbyingprovided that, again, the funds are not earmarked for lobbying and the amount of the grant does not exceed the grantee's budget for the non-lobbying components of the project.

Broad Flexibility

Notwithstanding the federal tax rules' prohibition on private foundation lobbying expenditures, foundations, in fact, have broad flexibility to fund activities that can have direct and significant impact on the public policy process. As outlined above, this flexibility derives from both the favorable rules protecting grantmaking foundations from attribution of their public charity grantees' lobbying expenditures and the favorable definition of lobbying. Through careful attention to the applicable tax rules, foundations

can thus play an active role in the formation of public policy without risk of adverse tax consequences.

The Rules for Community Foundations

The Treasury regulations that limit lobbying make no specific reference to community foundations. Thus, the rules generally applicable to all public charities apply to community foundations, and those rules will differ accordingly depending upon whether or not a community foundation has elected to be treated by the expenditure test.

If the community foundation elects, all actions excluded from the lobbying definition may be carried out in-house by a community foundation without fear of any legal violation, and the special exceptions to the lobbying rules will apply.

What happens, however, if a community foundation makes a general purpose grant to another charity that is active in lobbying, or for a specific project grant that includes lobbying in its budget? The private foundation rules for these circumstances are not explicitly applied to community foundations (or to other public charities) by the regulations. Yet, it is difficult to imagine the IRS or the courts applying a stricter rule to public charities (who are permitted to lobby) than the rule for private foundations (who are not).

Therefore, as a general rule, community foundations should be able to avoid incurring any lobbying penalties if they follow the rules specifically set out for private foundations. It is also comforting to remember that if the rules are not followed precisely and a community foundation grant is determined by the IRS to be lobbying, no penalty is likely to apply because community foundationsas public charitiesare permitted to lobby whether they elect the expenditure test or not.

Should Community Foundations Elect?

Any community foundation that is becoming more actively involved in public policy issues should seriously consider electing to be treated under the expenditure test created by the 1976 law and implemented by the 1990 regulations (private foundations do not have this option).

The process is simple: the foundation files a one-page IRS form 5768. Moreover, the election is not binding forever; it may be withdrawn later using the same form. Even since regulations have been clarified, the vast majority of charities have not elected. Electing provides many advantages, including:

- a single, clear spending yardstick for lobbying, not the vague substantial test.
- it does not count any efforts by volunteers (such as board members) where no expenditures occur; such activity is included under the substantial test.
- the statute and regulations are generous to an electing organization in defining what is lobbying.
- the IRS has declared that electing is a neutral factor for audit selection purposes.
- sanctions as applied to electing charities are more flexible; they measure a four-year period rather than every year standing alone.
- both electing and non-electing charities must be reported on the

Form 990. The only added requirement for electing charities is to compute direct and grassroots lobbying separately.

Excerpted from Foundations and Lobbying: Safe Ways to Affect Public Policy*, by John A. Edie. Published by the Council on Foundations in 1991. To order, call 202/467-0427.*

Three Definitions

As this issue went to press the Government Accounting Office (GAO) was finishing up a Congressionally mandated report comparing three existing definitions of lobbyingseparate tax law definitions for charities and businesses, and a third definition contained in the Lobbying Disclosure Act of 1995. GAO was asked to recommend changes to harmonize the definitions.

On behalf of Independent Sector, the Washington, D.C. law firm Caplin & Drysdale has submitted a detailed analysis to GAO on the underlying policy rationales of the three definitions, showing that harmonizing would frustrate, rather than further, Congressional intent. GAO officials have indicated the report is not likely to recommend changes in the lobbying definitions.

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