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TEMPERING EXPECTATIONS: RESTRAINT IN A TIME OF CORPORATE POLITICAL ACTIVISM – ALLOWABLE POLITICAL ACTIVITY FOR § 501(C)(3) TAX-EXEMPT ORGANIZATIONS

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TABLE OF CONTENTS

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INTRODUCTION

Congress, through the Internal Revenue Service ("IRS") and the Internal Revenue Code ("IRC"), restricts non-profit organizations' political activities, which are divided into two categories: lobbying and campaign intervention.[1] Lobbying is limited to an insubstantial part of the overall activities of the organization. IRC § 501(c)(3) states that an organization described in the section is one that has "no substantial part" of its activities consisting of "carrying on propaganda, or otherwise attempting, to influence legislation."[2] This language is vague, and by result many non-profit organizations rightfully shy away from lobbying out of fear that they will lose their tax-exempt status. Conversely, there is a total prohibition on § 501(c)(3) organizations from engaging in campaign interventions.[3] This prohibition on campaign intervention is the restriction of greater concern for compliance as the activities that fall under the definition of campaign intervention are far more encompassing than outright endorsement or financial contribution to an individual campaign.[4]

At the same time, since the Supreme Court ruling in *Citizens United v. Federal Election Commission*, corporations in the United States have increasingly engaged in open political activity.[5] *Citizens United* infamously addressed the political activities of § 501(c)(4) organizations[6] and created new avenues for potential "dark money" to enter into American politics,[7] but it also opened

1. I.R.C. § 501(c)(3).
2. *Id.*
3. *Id.*
4. *Id.*
5. Citizens United v. Fed. Election Comm'n., 558 U.S. 310 (2010); *see generally* Douglas M. Spencer & Abby K. Wood, *Citizens United, States Divided: An Empirical Analysis of Independent Political Spending*, 89 IND. L.J. 315 (2014); *see also* James Bopp, Jr., Joseph E. La Rue, & Elizabeth M. Kosel, *The Game Changer: Citizens United's Impact on Campaign Finance Law in General and Corporate Political Speech in Particular*, 9 FIRST AMEND. L. REV. 251 (2011).
6. Citizens United, 558 U.S. 310; *see also infra* Part IV. Not all § 501(c)(4) political engagement is considered infamous. Following the holding in *Citizens United* many § 501(c)(4)s developed with the intention of addressing specific issues of public concern that are generally lauded as beneficial to American society. *See e.g.,* David Gelles, *Billionaire No More: Patagonia Founder Gives Away the Company*, N.Y TIMES, (Sept. 14, 2022), https://www.nytimes.com/2022/09/14/climate/patagonia-climate-philanthropy-chouinard.html.
7. An in-depth analysis of the First Amendment political speech rights of non-profit organizations is outside of the scope of this Article. Much scholarship exists addressing this issue. *See e.g.* Ciara Torres-Spelliscy, *Hiding Behind the Tax Code, the Dark Election of 2010 and Why Tax-Exempt Entities Should Be Subject to Robust Federal Campaign Finance*

the door for corporations to engage in open electioneering.[8] Around the same time there was the rise of Benefit Corporations ("B-Corps").[9] B-Corps developed as part of a movement of new-wave social enterprise and ethics-driven business practices.[10] B-Corps are formed with the intent of producing profits while also seeking to significantly advance one or more social or environmental goals.[11] By result, it can be tempting for § 501(c)(3) organizations to enter the arena of political discourse and engage in political activity head-on. Ultimately, this is unwise; even with the increasing trend of corporate political activity, § 501(c)(3) organizations' allowable political activities are severely limited by the IRC and its regulations.

Part I of this Article will provide a brief history of the limitations on political activities for § 501(c)(3) organizations in the United States. Part II discusses the current regulatory and legal framework surrounding § 501(c)(3) organizations. Part III analyzes potential dangers for § 501(c)(3) organizations engaging in political activity, as well as providing risk avoidance and alternative structuring suggestions. Part IV discusses two alternatives to the current legal framework, one proposed by

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Disclosure Laws, 16 CHAP. J. OF L. AND PUB. POL'Y 59 *passim* (2011); John Persinger, *Opening the Floodgates: Corporate Governance and Corporate Political Activity After Citizens United*, 26 NOTRE DAME J. OF L. ETHICS & PUB. POL'Y 340, 348-51 (2012); Tim Bakken, *Constitutional Rights and Political Power of Corporations After Citizens United: The Decline of Citizens and the Rise of Foreign Corporations and Super PACs*, 12 CARDOZO PUB. L. POL'Y & ETHICS J. 119, 119-120 (2013).

8. Michael S. Kang, *The End of Campaign Finance Law*, 98 VA. L. REV. 1, 10-12, 17 (2012). "Of course, Citizens United opened the door to corporate electioneering even further than Wisconsin Right to Life II because it allowed corporations to engage not only in sham issue advocacy but also actual express advocacy in the form of independent expenditures. Corporations could engage in explicit campaign speech without the dressing of an issue advertisement. Nonetheless, with respect to corporate electioneering, the legality of sham issue advertising offered ample opportunity to engage in exactly the type of widespread corporate electioneering that [the Bipartisan Campaign Reform Act of 2002] restrictions were intended to thwart." *Id.* at 18.

9. *See generally* Annie Collart, *Benefit Corporations: A Corporate Structure to Align Corporate Personhood with Societal Responsibility*, 44 SETON HALL L. REV. 1160, 1163 (2014); McKenzie Holden Granum, *With the Emergence of Public Benefit Corporations, Directors of Traditional For-Profit Companies Should Tread Cautiously, but Welcome the Opportunity to Invest in Social Enterprise*, 38 SEATTLE U.L. REV. 765, 765 (2015).

10. *Beyond Corporate Profits and Towards New Model Capitalism*, WORLD FIN. (Apr. 11, 2014), http://www.worldfinance.com/strategy/beyond-corporate-profits-and-towards-new-model-capitalism. ("Benefit corporation status represents a new legal structure whereby participating firms are legally obliged to consider social and environmental concerns on an equal footing to financial gains.").

11. Antony Page & Robert A. Katz, *Is Social Enterprise the New Corporate Social Responsibility?*, 34 SEATTLE U. L. REV. 1351, 1353 (2011).

Professor Benjamin Leff and the other a novel approach argued by the Author.

I. HISTORY

The IRC is the body of tax law that governs taxation in the United States.[12] IRC § 501 contains provisions related to tax-exempt organizations, which are not required to pay federal income tax on their income as long as they meet certain requirements.[13] The history of the IRC and tax-exempt organizations dates back to the early 20th century when Congress recognized the need for tax exemptions for certain organizations, such as charities and educational institutions.[14]

Over time, Congress expanded the types of organizations that could qualify for tax-exempt status and added additional requirements for maintaining that status, including pieces of the modern limitation on political activity.[15] By 1934, many of the restrictions in place today were well established.[16] These early restrictions by Congress included restrictions on "propaganda" and "substantial" lobbying; however, a total prohibition on all participation in elections was deemed too broad.[17] Twenty years later, this changed. The further addition of the Johnson Amendment in 1954, named after its sponsor then-Senator Lyndon B. Johnson, added the provision to § 501(c)(3) that prohibits certain tax-exempt organizations from endorsing or opposing political candidates.[18]

The Johnson Amendment was a response to concerns that tax-exempt organizations were engaging in political activities, such as

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12. *History: Title 26, U.S. Code*, UNITED STATES CENSUS, https://www.census.gov/history/www/reference/privacy_confidentiality/title_26_us_code_1.html (last visited Sept. 6, 2024).

13. *See generally* Oliver A. Houck, *On the Limits of Charity: Lobbying, Litigation, and Electoral Politics by Charitable Organizations Under the Internal Revenue Code and Related Laws*, 69 BROOK. L. REV. 1 (2003).

14. Hannah Lepow, *Speaking up: The Challenges to Section 501(c)(3)'s Political Activities Prohibition in a Post-Citizens United World*, 2014 COLUM. BUS. L. REV. 817, 821-23 (2014).

15. Houck, *supra* note 13, at 21-23.

16. *Id.* at 23.

17. "By retaining the restriction on 'propaganda' and by prohibiting only 'substantial' lobbying, however, the Congress left the [IRS] extremely wide discretion on whom it wished to challenge, and why," but Congress found a prohibition on "participation in electoral campaigns . . . simply [] 'too broad.'" *Id.*

18. *Id.* at 23-24.

endorsing or opposing political candidates, to influence elections.[19] Johnson argued that such activities violated the principle of separation of church and state, and that tax-exempt organizations should not be allowed to engage in partisan political activities.[20] Johnson introduced the amendment on the floor of the Senate, stating:

> Mr. President, this amendment seeks to extend the provisions of section 501 of the House bill, denying tax-exempt status to not only those people who influence legislation but also to those who intervene in any political campaign on behalf of any candidate for any public office. I have discussed the matter with the chairman of the committee, the minority ranking member of the committee, and several other members of the committee, and I understand that the amendment is acceptable to them. I

19. Roger Colinvaux, *The Political Speech of Charities in the Face of Citizens United: A Defense of Prohibition*, 62 CASE W. RSRV. L. REV. 685, 690 (2012). "The Rule's abrupt passage leads many to conclude that its rationale was mostly political: Senator Johnson was attacked by a charity during his reelection campaign and used the power of his office to change the law to prohibit such attacks. And there is little doubt that Johnson pushed the Rule through in the heat of a political battle. Indeed, after a thorough review of the legislative record, one commentator concluded that 'Johnson saw a cabal of national conservative forces, led by tax-exempt educational entities fueled by corporate donations, arrayed against him and wanted to put a stop to the meddling of these foreign interlopers.'" *Id.* at 690-91. "Notwithstanding the circumstances of the Rule's enactment, however, the broader historical record offers a more compelling story of the origin of the Rule than the reaction of a single skillful Senator to a political problem. Although the absence of direct legislative history is accurate, a view often implicit (and sometimes explicit) in some discussions of the Rule is that, in part because of the abrupt fashion in which the Rule was enacted, the rationale is uncertain, and we are, for the most part, supplying reasons for Congress' actions after the fact. Importantly, here, the implication may be that the Rule was adopted ad hoc, and therefore should be changed, or if not changed, perhaps treated with less reverence than a more fully reasoned rule." *Id.* at 691.

20. Part of Johnson's motivation included his own political needs. *See* BRUCE R. HOPKINS, THE LAW OF TAX-EXEMPT ORGANIZATIONS 608 (John Wiley & Sons, Inc., 10th ed. 2011) ("[Senator Johnson] offered the amendment out of concern that funds provided by a charitable foundation were being used to help finance the campaign of an opponent in a primary election."); JAMES J. FISHMAN & STEPHEN SCHWARZ, TAXATION OF NONPROFIT ORGANIZATIONS 261 (Thomson West, 2d ed. 2006) ("The conventional wisdom is that Senator Johnson was out to curb the activities of a Texas foundation which had provided indirect financial support to his opponent in a senatorial primary election campaign."); Houck, *supra* note 13, at 24 ("Commentators have explained that Senator Johnson was motivated by the activities of charities allied to his opponent in a recent campaign."); Patrick L. O'Daniel, *More Honored in the Breach: A Historical Perspective of the Permeable IRS Prohibition on Campaigning by Churches*, 42 B.C. L. REV. 733, 768 (2001) (noting that Senator Johnson proposed the amendment to prevent certain tax-exempt entities from intervening in political campaigns, because he "wanted to stomp out a potential threat in his own back yard").

> hope the chairman will take it to conference, and that it will be included in the final bill which Congress passes.[21]

Since its passage in 1954, the Johnson Amendment has been a controversial topic, with some arguing that it limits free speech and others arguing that it is necessary to maintain the separation of church and state.[22]

II. MODERN LEGAL AND REGULATORY FRAMEWORK

For the sake of this Article the limitations on political activity for § 501(c)(3) organizations are divided into two primary categories: lobbying efforts and campaign activities. The language of the IRC provides only limited guidance:

> Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, **no substantial part of the activities of which is 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.**[23]

Under this statutory language, § 501(c)(3) organizations are restricted from engaging in "substantial activities" that include carrying on propaganda and attempting to influence legislation.[24]

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21. 100 CONG. REC. 9604 (1954).

22. Houck, *supra* note 13, at 81 ("The Internal Revenue Code restraints on the political activities of charities have been in evolution, and in dispute, for nearly a century. They represent no grand plan, but rather a design arrived at in pieces by the impulses of the moment. They have been looking for a reason since the time they first appeared, and it was half a century before Congress even attempted one. Reading their histories, one is struck by the fact that each of the limitations, in a different climate, could have come out quite differently.").

23. I.R.C. § 501(c)(3) (emphasis added).

24. *Id.*

But there is a total prohibition on participation or intervention in any political campaign for any candidate for public office.[25] By result, § 501(c)(3) organizations are not allowed to directly participate in elections, but they are able to engage in some lobbying.[26] The more restrictive campaign activities include electioneering, campaign contributions, and public statements for or against candidates, all of which would be considered violations of the Code.[27]

There are many activities that are not considered a violation for a § 501(c)(3) organization, however, such as education activities, voter registration efforts, or advocacy conducted in a non-partisan manner.[28] There is a fine-line distinction between advocacy and lobbying. According to the Alliance for Justice, advocacy is "any action that speaks in favor of, recommends, argues for a cause, supports or defends, or pleads on behalf of others; it includes public education, regulatory work, litigation, and work before administrative bodies, lobbying, nonpartisan voter registration, nonpartisan voter education, and more."[29] Whereas, lobbying is "(1) communicating with decision makers (2) about existing legislation and (3) urging a vote for or against."[30] All three components are needed to be considered lobbying: communicating with decision-makers, actual legislation, and asking for a vote.[31] Influencing legislation is defined broadly within the IRC to include both direct lobbying and grass roots lobbying.[32] As such, § 501(c)(3) organizations must walk a fine line to remain in compliance with IRS limitations.

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25. *Id.*

26. *The Restriction of Political Campaign Intervention by Section 501(c)(3) Tax-Exempt Organizations*, INTERNAL REVENUE SERVICE, https://www.irs.gov/charities-non-profits/charitable-organizations/the-restriction-of-political-campaign-intervention-by-section-501c3-tax-exempt-organizations (last updated May 30, 2024).

27. *Id.*

28. *Id.*

29. *What is Advocacy? Definitions and Examples*, ALLIANCE FOR JUSTICE, https://mffh.org/wp-content/uploads/2016/04/AFJ_what-is-advocacy.pdf (last visited Mar. 29, 2022).

30. *Political Campaign Activities - Risks to Tax-Exempt Status*, NAT'L COUNCIL FOR NONPROFITS, https://www.councilofnonprofits.org/running-nonprofit/governance-leadership/political-campaign-activities-risks-tax-exempt-status (last visited Sept. 24, 2024).

31. *Id.*

32. I.R.C. § 4911(d)(1).

A. IRS Limitations and Definitions: Lobbying

The IRC limits lobbying activities for non-profit organizations to an insubstantial part of the overall activities of the organization.[33] IRC § 501(c)(3) states that an organization described in the section is one that has "no substantial part" of its activities consisting of "carrying on propaganda, or otherwise attempting to influence legislation."[34] This language is vague. As the IRS states on a webpage dedicated to explaining the law, "[a] 501(c)(3) organization may engage in some lobbying, but too much lobbying activity risks loss of tax-exempt status."[35] Rightfully, many non-profit organizations shy away from lobbying out of fear that they will lose their tax-exempt status. To measure if non-profit organizations comply with the regulations, the IRS sets forth two tests to measure any lobbying activities: the substantial part test and the expenditure test.

1. The Substantial Part Test

Under the substantial part test, an organization that conducts excessive political activity in any taxable year may lose its tax-exempt status, resulting in all of its income being subject to tax.[36] In addition, Section 501(c)(3) organizations that lose their tax-exempt status due to excessive political activity, other than churches and private foundations, are subject to an excise tax equal to five percent of their political activity expenditures for the year in which they cease to qualify for exemption.[37] Further, a tax equal to five percent of the political activity expenditures for the year may be imposed against organization managers, jointly and severally, who knowingly agree to such expenditures.[38]

Treasury regulations define attempting to influence legislation as when an organization "[c]ontacts, or urges the public to contact, members of a legislative body for the purpose of

33. I.R.C. § 501(c)(3).

34. *Id.*

35. *Lobbying*, INTERNAL REVENUE SERVICE, https://www.irs.gov/charities-non-profits/lobbying (last updated June 4, 2024).

36. *Measuring Lobbying: Substantial Part Test*, INTERNAL REVENUE SERVICE, https://www.irs.gov/charities-non-profits/measuring-lobbying-substantial-part-test (last updated Sep. 9, 2024).

37. *Id.*

38. I.R.C. § 4912.

proposing, supporting, or opposing legislation; or (b) [a]dvocates the adoption or rejection of legislation."[39] The IRS considers a variety of factors, including the time devoted (by both compensated and volunteer workers) and the expenditures devoted by the organization to the activity, when determining whether the political activity is substantial.[40]

Whether an organization's attempts to influence legislation constitute a substantial part of its overall activities is determined based on all the pertinent facts and circumstances in each case.[41] Such a determination is typically fact-and-circumstance specific.[42] The ambiguity of this standard should encourage caution for organizations and suggests that it is "more prudent, to take the position that the indeterminacy of the substantial part test . . . permits the [IRS] to exercise broad discretion."[43]

2. The Expenditure Test

The IRS provides a tool to remove some of the ambiguity of the substantial part test. By filing a § 501(h) election, § 501(c)(3) organizations can mitigate confusion and have clear parameters to measure their allowable political activity activities.[44] This is a free election that non-profits can use to be measurably sure they do not run afoul of the limitations on political activity established by the IRS.[45] Under the expenditure test, the extent of an organization's political activity will not jeopardize its tax-exempt status, provided its expenditures related to such activity do not normally exceed an amount specified in IRC § 4911.[46]

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39. Treas. Reg. § 1.501(c)(3)-1.

40. *Measuring Lobbying*, *supra* note 36.

41. FRANCES R. HILL & DOUGLAS M. MANCINO, TAXATION OF EXEMPT ORGANIZATIONS ¶ 5.03. (Thomson Reuters Tax & Accounting, Mar. 2024). This treatise provides expert analysis and tax guidance on the taxation of non-profit organizations and includes fact pattern specific discussions as well.

42. *Id.*

43. *Id.*

44. *Measuring Lobbying Activity: Expenditure Test*, INTERNAL REVENUE SERVICE, https://www.irs.gov/charities-non-profits/measuring-lobbying-activity-expenditure-test (last updated Oct. 18, 2024). Importantly, this option is only available to non-religious § 501(c)(3) organizations. *Id.*

45. *Id.*

46. *Id.*

If the amount of exempt purpose expenditures is:	Lobbying nontaxable amount is:
≤ $500,000	20% of the exempt purpose expenditures
>$500,00 but ≤ $1,000,000	$100,000 plus 15% of the excess of exempt purpose expenditures over $500,000
> $1,000,000 but ≤ $1,500,000	$175,000 plus 10% of the excess of exempt purpose expenditures over $1,000,000
>$1,500,000 but ≤ $17,000,000	$225,000 plus 5% of the exempt purpose expenditures over $1,500,000
>$17,000,000	$1,000,000

This table is provided by the IRS as a guideline for organizations using the expenditure test. [47]

3. Reporting Lobbying Activities

Compliance for § 501(c)(3) organizations requires careful monitoring of the activities of those who work for the non-profit organization. For § 501(c)(3) organizations that are § 501(h)-electing organizations, they only need to report political activity expenditures.[48] For non-electing organizations, they must report political activity expenditures and describe their political activity activities to ensure compliance with the IRC.[49] As a practical suggestion, effective compliance requires careful tracking of time and money spent on political activity by the organization.[50] This tracking involves the allocation of staff time and compensation, overhead costs, and administrative costs spent on political activity efforts.[51] These reporting requirements are discussed in greater detail in Part IV.[52]

47. *Id.*
48. *Id.*
49. I.R.C. § 6033(e)(1).
50. *Measuring Lobbying Activity: Expenditure Test*, *supra* note 44.
51. *Id.*
52. *See infra* Part IV.

B. IRS Limitations and Definitions: Campaign Activities

Whereas lobbying is allowed but limited, campaign activities are completely forbidden.[53] This means that a § 501(c)(3) organization cannot directly or indirectly participate in or intervene on behalf of (or in opposition to) a campaign for any candidate for elective public office.[54] This language is the aforementioned Johnson Amendment,[55] and it is significantly more restrictive than the partnered language regarding lobbying. This restriction intends to limit dark money being funneled through tax-exempt § 501(c)(3) organizations;[56] however, in the modern era of American politics the increased political division of the nation has made it increasingly difficult for § 501(c)(3)s to remain silent about specific campaigns as political candidates may run on platforms that are a direct threat to the reasons the organizations exist.[57]

III. POTENTIAL DANGERS, RISK AVOIDANCE, AND ALTERNATIVE ENTITY FORMATION

Below is a description of penalties for § 501(c)(3) organizations that violate the limitations on political activity and an analysis of practical approaches for § 501(c)(3) organizations to avoid said penalties.

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53. *The Restriction of Political Campaign Intervention by Section 501(c)(3) Tax-Exempt Organizations*, *supra* note 26.

54. I.R.C. § 501(c)(3).

55. *See supra*, Part I.

56. *See, e.g.*, Robert Paul Meier, Comment, *The Darker Side of Nonprofits: When Charities and Social Welfare Groups Become Political Slush Funds*, 147 U. PA. L. REV. 971, 993-995, 999-1000, 1008 (1999).

57. *See e.g.*, Nicole Acevedo, *Florida's Upcoming 6-Week Abortion Ban Will Disproportionately Impact Latina and Black Women, Advocates Say*, NBC NEWS (Apr. 14, 2023, 7:39 PM), https://www.nbcnews.com/news/latino/floridas-upcoming-6-week-abortion-ban-will-impact-latina-black-women-rcna79779. In this article NBC News covers the then pending impact of 6-week abortion ban in Florida. It discussed the work that was done by organizations such as Florida Access Network, a 501(c)(3) organization, to ensure abortion access in Florida. However, organizations such as this are restricted from engaging directly in the election campaigns for or against politicians seeking to ban abortion access within the state.

A. Potential Dangers: What happens when a § 501(c)(3) engages in an unallowed amount of political activity?

When a § 501(c)(3) organization violates the rules limiting political activity there is substantial legal risk and potential tax liability for the organization. The IRS requires mandatory reporting of § 501(c)(3) activity as part of their oversight of these organizations.[58] A wise § 501(c)(3) organization will use this required reporting as a tool to ensure its compliance and avoid penalties.

1. Reporting and Form 990

The IRS requires all § 501(c)(3) organizations to submit a Form 990 annually.[59] Ironically, the best tool for an organization to protect itself is reporting properly via the Form 990.[60] As part of Form 990, § 501(c)(3) organizations are required to report both lobbying and political campaign activity they have conducted within the year.[61] Under Part IV, Line 3 of Form 990 an organization must identify if it has engaged in direct or indirect political campaign activities.[62] IRS guidance suggests that organizations "[a]nswer 'Yes' whether the activity was conducted directly or indirectly through a disregarded entity or a joint venture or other arrangement treated as a partnership for federal income tax purposes and in which the organization is an owner."[63]

The form asks a similar question regarding lobbying activity on Line 4.[64] This question is limited to only § 501(c)(3) organizations, whereas Line 3 is required by all organizations that use the Form 990.[65] If a § 501(c)(3) organization reports lobbying activity they must also complete Schedule C, Part II.[66] This annual reporting requirement should be viewed as a beneficial tool for

58. I.R.C. § 6033.

59. INTERNAL REVENUE SERV., U.S. DEP'T OF THE TREASURY, CAT. NO. 11283J, INSTRUCTIONS FOR FORM 990: RETURN OF ORGANIZATION EXEMPT FROM INCOME TAX 2-3 (2023) [hereinafter INSTRUCTIONS FOR FORM 990], https://www.irs.gov/pub/irs-pdf/i990.pdf.

60. *Id.*

61. *Id.* at 12.

62. *Id.*

63. *Id.*

64. *Id.*

65. Instructions for Form 990, *supra* note 59, at 12.

66. *Id.* at 12.

§ 501(c)(3) organizations, as it allows them to track their allowable activities and remain compliant.

2. Penalties

Section 501(c)(3) organizations that violate the political activity limitations risk severe penalties and consequences.[67] Violating these rules can result in excise taxes, revocation of tax-exempt status, and intermediate sanctions for individuals responsible for the violation. Penalties for violations of allowable political participation or intervention are outlined in IRC § 4955 and violations for limitations on lobbying are established in IRC § 4911.[68]

One of the primary penalties for violating the political activity limitations is an excise tax. If a § 501(c)(3) organization engages in political campaign intervention, the IRS can impose excise taxes on the organization.[69] The tax amount is usually calculated as a percentage of the funds expended on the political activity.[70] This penalty can significantly impact an organization's finances and reputation.[71]

In addition to excise taxes, the IRS can also revoke an organization's tax-exempt status if it engages in political campaign intervention.[72] Losing tax-exempt status means the organization will be required to pay federal income tax on its earnings, and donors will no longer be able to claim a tax deduction for their

67. Benjamin M. Leff, *Fixing the Johnson Amendment Without Totally Destroying It*, 6 U. PA. J.L. & PUB. AFFS. 115, 124-25 (2020).

68. FRANCES R. HILL & DOUGLAS M. MANCINO, TAXATION OF EXEMPT ORGANIZATIONS ¶ 6.05, at 1, ¶ 5.04, at 12 (2002 & Supp. 2022).

69. *See id.* ¶ 6.05, at 2 & n.208 (citing § 4955(a)(1) (imposing an initial excise tax of 10% of any "political expenditure.")); *id.* at 2 & n.209 (citing § 4955(a)(2) (imposing an additional tax of 2.5% of the political expenditure on each manager who approved the expenditure)); *id.* at 5 & n. 233 (citing § 4955(b)(1) (providing that an organization that does not correct the expenditure must pay a tax of 100% of the expenditure)); *id.* at 5 & n.234 (citing § 4955(f)(3) (explaining that an organization that corrects the political expenditure by "recovering part or all of the expenditure to the extent recovery is possible, [and] establish[ing] safeguards to prevent future expenditures. . . .")).

70. *See* Treas. Reg. § 53.4955-1(a) (1995). ("The excise taxes imposed by section 4955 do not affect the substantive standards for tax exception under section 501(c)(3), under which an organization is described in section 501(c)(3) only if it does not participate or intervene in any political campaign on behalf of any candidate for public office.")

71. Hill & Mancino, *supra* note 68, ¶ 6.05, at 1.

72. *Id.* at 8.

contributions.[73] Such a penalty has a severe impact on an organization's operations, funding, and mission.[74]

Finally, the IRS can impose an injunction against further political expenditures.[75] These penalties can be applied based upon actions of the organization or the organization's officers, directors, or trustees.[76] For officers, directors, or trustees, penalties can also include fines, penalties, and even the loss of their positions within the organization.[77] Any of these sanctions can have a significant impact on an individual's reputation and future opportunities.[78]

B. Risk Avoidance: How can a § 501(c)(3) avoid the dangers of over-engagement?

There are two main strategies for avoiding the dangers discussed above: a total prohibition on political activity as a § 501(c)(3) organization or the formation of affiliated organizations allowed to openly participate in political activity.

1. Avoid Political Activity

This strategy is fairly straightforward, as a § 501(c)(3) organization simply does not engage in political activity. There are downsides to this however, as the organization is then unable to voice concern over elections or legislation. Some examples of organizations that are hurt by political silence include domestic violence organizations,[79] minority farmers organizations fighting federal discriminatory lending practices,[80] or even religious

73. *Id.*
74. I.R.C. § 4955.
75. Hill & Mancino, *supra* note 68, ¶ 6.05, at 1.
76. *Id.* at 3.
77. *Id.* at 5.
78. *Id.*
79. *See e.g.,* Ashley M. Blas, Note, *The Danger of Silence: How the Political Activities Prohibition Negatively Affects Nonprofit Domestic Violence Organizations*, 49 U. TOL. L. REV. 715 (2018).
80. *See generally,* Kyle Ridgeway, *Broken Promises: The Continuing Decline of Black Farm Owners and Operators in America*, 27 U.C. DAVIS SOC. JUST. L. REV. 50 (2023). This article discussed the history of discriminatory lending practices by the U.S.D.A. and a Federal attempt to remedy the loss of Black farmers within the American Rescue Plan Act (2021). Lawsuits filed by white farmer successfully blocked implementation of the debt cancellation provisions in Section 1005 of the Act. "The Federation argued that its members had compelling testimony that could bolster the defense of the $5 billion program. Law firms representing the Federation—a nonprofit association of about 20,000 mostly Black farmers and landowners—sought to enter evidence of ongoing discriminatory practices by the

organizations.[81] Non-profit organizations frequently engage in advocacy on a vast array of significant legal and policy issues. For most § 501(c)(3) organizations, not engaging in political activity is not truly an option.

2. Form an Affiliated Organization

A viable alternative for most § 501(c)(3) organizations is to form an affiliated § 501(c)(4) organization and have that entity engage in political activity.[82] A § 501(c)(4) organization does not have the same limits on its political activity and it is still a tax-exempt organization, but donors to a § 501(c)(4) organization cannot receive a tax deduction for donations.[83] This aspect can be a deterrence for some donors; however, with the most recent changes to itemized deductions, average American donors would not be able to donate enough to earn a greater deduction by itemizing as compared to the standard deduction.[84] A § 501(c)(4) organization is defined by the Code as:

> (4)(A) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are

USDA. The Federation argued that the USDA could not properly represent the interests of the socially disadvantaged farmers since the government was unwilling to discuss claims of ongoing discrimination." *Id.* at 69.

81. Keith S. Blair, *Praying for a Tax Break: Churches, Political Speech, and the Loss of Section 501(c)(3) Tax Exempt Status*, 86 DENV. U. L. REV. 405, 425 (2009).

82. Another potential affiliate organization type is found in I.R.C. § 527. A § 527 organization is also known as a political organization. The downside to a § 527 organization is they are taxable entities and can often be expensive to operate. *See* Roger Colinvaux, *Regulation of Political Organizations and the Red Herring of Tax Exempt Status*, 59 NAT'L. TAX J. 531, 541 (2006). "A political organization shall be subject to taxation under this subtitle only to the extent provided in this section. A political organization shall be considered an organization exempt from income taxes for the purpose of any law which refers to organizations exempt from income taxes." I.R.C. § 527(a). The benefit is that a 527 can engage in unlimited political activity as its primary purpose. Colinvaux, *supra* note 19, at 713-14.

83. Terence Dougherty, *The Importance of Using Affiliated § 501(c)(4) and § 501(c)(3) Organizations for Advocacy*, 21 N.Y.U. J. LEGIS. & PUB. POL'Y 615, 619 (2018).

84. Kelly Phillips Erb, *Tax-Exempt Organizations Don't Always Have to Say No to Politics*, BLOOMBERG TAX (Nov. 3, 2022, 4:45 AM), https://news.bloombergtax.com/tax-insights-and-commentary/tax-exempt-organizations-dont-always-have-to-say-no-to-politics.

> devoted exclusively to charitable, educational, or recreational purposes.
>
> (B) Subparagraph (A) shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.[85]

It is important to note that for a § 501(c)(4) organization that is affiliated with a § 501(c)(3) organization there are special limitations on the allowable sharing of funding, sharing of tangible resources, and specific consideration for the overlap of members of the board of directors.[86] A particular concern that a § 501(c)(3) organization forming an affiliated organization should keep in mind is the controversial lack of enforcement of donor reporting requirements for § 501(c)(4) organization.[87] Section 501(c)(3) organizations dependent upon donations from their community and concerned with maintaining public trust would be well advised to follow donor disclosure rules despite this lack of enforcement for affiliated § 501(c)(4) organizations.

As seen in the below graphic, there are several parallels between the allowable activities of a § 501(c)(3) organization and a § 501(c)(4) organization, but § 501(c)(4) organizations have more freedom to engage in political activities.

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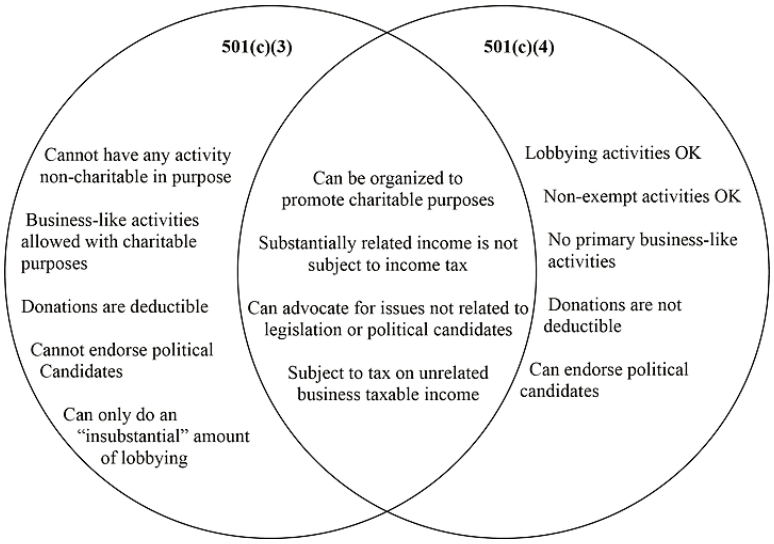
85. I.R.C. § 501(c)(4).

86. *See generally*, *The Practical Implications of Affiliated 501(c)(3)s and 501(c)(4)s*, ALLIANCE FOR JUSTICE, https://bolderadvocacy.org/wp-content/uploads/2018/06/The_Practical_Implications_of_Affiliated_501c3s_andc4s.pdf. (last visited September 20, 2024)

87. *See* Philip Hackney, *Dark Money Darker? IRS Shutters Collection of Donor Data*, 25 FLA. TAX REV. 140, 147 (2021); Matt Corley & Adam Rappaport, *The IRS Is Not Enforcing the Law on Political Nonprofit Disclosure Violations*, CITIZENS FOR RESP. & ETHICS IN WASH., https://www.citizensforethics.org/reports-investigations/crew-reports/the-irs-is-not-enforcing-the-law-on-political-nonprofit-disclosure-violations/ (Apr. 29, 2022); This lack of disclosure enforcement for 501(c)(4) organizations has given rise to a number of secretive 501(c)(4)s focused on progressing individual political candidates' campaigns. *See e.g.*, Alex Isenstadt, *A New Nonprofit Group Is Helping DeSantis Go National*, POLITICO (Feb. 20, 2023, 9:41 PM), https://www.politico.com/news/2023/02/20/nonprofit-desantis-florida-00083692.



88

Given the significant benefits of an affiliated § 501(c)(4) organization it may seem obvious that all § 501(c)(3) organizations, that can, should form one; however, this is not necessarily a viable option for all § 501(c)(3) organizations. As such, the final section of this Article is a review of possible changes to the Code.

IV. POTENTIAL CHANGES TO THE IRC

This portion of the Article leaves the descriptive and extends into the normative. As reviewed above, there are limited options for § 501(c)(3) organizations to engage in political activity under the current law. The limitations on lobbying activity are generally accepted as a well-functioning framework as currently enforced; however, there is significant scholarship addressing the question of if the Johnson Amendment is sustainable.[89] This Part

88. Alan Gassman, Karl Mill & Peter Farrell, *The 501(c)(4) Strategy*, 48 TAX MGMT. ESTS. GIFTS & TRS. J. 1, 33 (2023). Special thank you to my cohort and classmate, Peter Farrell, for this graphic as part of his work with Mr. Gassman.

89. *See e.g.*, Samuel D. Brunson, *Reigning in Charities: Using an Intermediate Penalty to Enforce the Campaigning Prohibition*, 8 PITT. TAX REV. 125, 135, 145 (2011); W. Edward Afield, *Getting Faith Out of the Gutters: Resolving the Debate Over Political Campaign Participation by Religious Organizations Through Fiscal Subsidiarity*, 12 NEV. L.J. 83, 83 (2011); Edward A. Zelinsky, *Churches' Lobbying and Campaigning: A Proposed Statutory Safe Harbor for Internal Church Communications*, 69 RUTGERS U.L. REV. 1527, 1527-1528 (2017).

highlights, in the opinion of the Author, the most convincing scholarly argument of how to change the Code to provide a more workable framework to balance the government's interest and the free speech rights of § 501(c)(3) organizations. Professor Leff, in his article *Fixing the Johnson Amendment Without Totally Destroying It*, reviews the leading proposals to fix the Johnson Amendment [a]nd proposes his own solution to balancing the free speech rights of § 501(c)(3) organizations with the government's interest in limiting the organizations' political activities.[90] This Article evaluates Professor Leff's potential changes to the IRC aimed at creating a balance, and then suggests an alternative proposal—creating a new type of tax-exempt organization.

A. Constitutional Implications

To understand the proposals below, it is necessary to discuss how the IRS is able to limit the political activities and speech rights of § 501(c)(3) organizations without violating the First or Fifth Amendments. In *Regan v. Taxation with Representation of Washington*, the U.S. Supreme Court considered these constitutional questions in regards to lobbying.[91] In this case, a nonprofit organization filed a lawsuit to obtain a ruling that it was eligible for tax-exempt status as the IRS had rejected its application.[92] The reason for the rejection was that the organization seemed primarily focused on influencing legislation, which was deemed to be a significant part of its activities.[93] The Court held that the IRC's restriction on tax-exempt nonprofit organizations engagement in significant lobbying activities did not violate the First Amendment.[94] And, that the IRC does not violate the equal protection clause of the Fifth Amendment because it was

90. *See* Leff, *supra* note 67. "This Article reviews the leading proposals to fix the Johnson Amendment and finds them all lacking. It then proposes four types of modifications that could be used to properly balance the speech interests of charities (including churches) with the government's interest in a level playing field for campaign expenditures (nonsubvention). These proposed modifications include: (i) a non-incremental expenditure tax, (ii) a reporting regime, (iii) a disclosure regime, and (iv) a governance regime. The Article concludes that in order to properly balance nonsubvention with speech interests of charities, a modification of the Johnson Amendment should include some version of all four types of interventions." *Id.* at 116.

91. Regan v. Taxation with Representation of Wash., 461 U.S. 540 (1983).

92. *Id.* at 542.

93. *Id.* at 540-42.

94. *Id.* at 542-48.

reasonable for Congress to determine that, although it would not subsidize through tax-exemption significant lobbying by charities in general, it would subsidize through tax-exemption lobbying by tax-exempt organizations dedicated to veterans' interests.[95]

The Court's ruling falls in line with the Code's limiting language for lobbying activity; however, when logically extended to the total prohibition on campaign activities a stronger conflict develops.[96] Professor Leff put it succinctly,

> [a] § 501(c)(3) organization has a constitutionally protected right to communicate its views on candidates without the government imposing a substantial burden on it. On the other hand, the government is permitted to impose restrictions on how a § 501(c)(3) organization uses the dollars it collects on a tax-deductible basis, as it has done in the Johnson Amendment.[97]

Any potential changes to the Code should balance the government's interest to not subsidize political speech, but also to not overtly infringe the speech rights of § 501(c)(3) organizations.

B. Leff's Proposal: Revise the Johnson Amendment to Allow for Some Campaign Activity for § 501(c)(3) Organizations

Leff argues that the goal of the Johnson Amendment is to maintain the integrity and independence of charities and to prevent them from being used as vehicles for political campaign contributions, which he describes as "the nonsubversion principle."[98] In terms of a revised Johnson Amendment, Leff proposes four requirements that would balance the speech interests of charities against the non-subvention principle.[99] The first requirement is to prevent incremental expenditures by § 501(c)(3) organizations to political campaign organizations or for political campaign activities, as such expenditures would violate the non-subvention principle.[100] The second requirement is to impose a financial cost on non-incremental expenditures or "no-

95. *Id.* at 548-51.
96. Leff, *supra* note 67, at 144.
97. *Id.*
98. Leff, *supra* note 67, at 120-21 (citing *Regan*, 461 U.S. 540, 549 (1983)).
99. *Id.* at 160-75.
100. *Id.* at 160-64.

cost political speech."[101] Leff proposes an excise tax of 21% on a base of 10% of the organization's total operating costs for the year to cover all no-cost political speech, regardless of how many times it occurred.[102] This excise tax would not cover incremental expenditures.[103]

The third requirement is to impose a disclosure regime to require § 501(c)(3) organizations that engage in political campaign activity to report that fact and information about how they did it or plan to do it to their stakeholders and the general public.[104] Finally, the fourth requirement is to impose governance requirements to ensure that relevant stakeholders have consented to the organization's exercise of its speech rights prior to any political campaign activity taking place.[105] Leff believes that these four requirements are necessary to best balance the speech rights of charitable organizations with the non-subvention principle, and that they do a better job of aligning policy with the interests of charities, their stakeholders, and the common good than existing proposals that limit the scope of an incremental approach by only permitting certain organizations or certain communications.[106]

Leff's argument successfully creates a more balanced legal framework that would allow for § 501(c)(3) organizations to engage in campaign activities while maintaining their preferred tax-exempt status. However, his plan does not address the potential of a § 501(c)(3) organization that wants to be intentionally removed from political discourse. Following Leff's proposal to change the Johnson Amendment could result in § 501(c)(3) organizations being pulled into political dialogue that they may want to avoid. The current version of the Johnson Amendment provides a legally justified reason for avoiding campaign-related speech. As such, the proposal presented by this Author is that there should be a new section of the Code added for tax-exempt non-profit organizations that wish to engage in political speech.

101. *Id.*
102. *Id.* at 163-71.
103. *Id.*
104. Leff, *supra* note 67, at 171-75.
105. Leff, *supra* note 67, at 168.
106. *Id.* at 175-76.

C. Create a New Tax-Exempt Organization Type: § 501(c)(30)

Rather than changing the Johnson Amendment, Congress could add a new section of the Code to create a new § 501(c)(30) organization type. This new organization type would be one that would allow for tax-exempt non-profit organizations as defined in § 501(c)(3), including religious organizations, to opt-in to limited allowable campaign activities that would be reported in a similar capacity as the Expenditure Test for lobbying. The same § 501(c)(3) rules regarding lobbying would apply to this new organization type, but it would allow tax-exempt non-profit organizations to also engage in limited campaign activity without risking their tax-exempt status. The research conducted for this Article did not uncover any scholarly argument advocating for a solution of this magnitude.[107]

This new organization type would allow for greater engagement for tax-exempt non-profit organizations that desire to participate in political activities that are currently limited, but also maintain the donor deduction benefit shared by § 501(c)(3) organizations. It would further differ from § 501(c)(4) organizations in that it would be allowed to engage in less political activity. This new § 501(c)(30) organization would be limited to less than 10% of its overall operation dedicated to political activity (both lobbying and campaign activity). Any overage of political activity would result in a 21% excise tax on all political activity related expenses and donations.

To ensure that this new organization type does not become a slush fund for dark money, mandatory reporting would be required quarterly. This reporting would require disclosure of donors, expenses, and descriptions of political activity within the quarter. If, within a reporting quarter, a § 501(c)(30) organization is found to have surpassed the 10% limitation, the excise tax of 21% would be applied to the remainder of the fiscal year and extend into the next fiscal year to the equivalent reporting quarter.[108]

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107. *Cf.* NINA J. CRIMM & LAURENCE H. WINER, POLITICS, TAXES, AND THE PULPIT: PROVOCATIVE FIRST AMENDMENT CONFLICTS 326 (2011) (Crimm and Winer proposed a new category of section 501(c) that would be available *only to houses of worship* that choose to opt into it (and out of 501(c)(3) whereas my proposal would be open to any group traditionally able to form as a 501(c)(3) organization including religious groups).

108. For example, if a § 501(c)(3) organization exceeds the 10% limitation of political activity in Q2 of 2023, it would have the 21% excise tax on all political activity related expenses and donations until Q2 of 2024.

This new organization type would provide an incentive to current § 501(c)(3) and § 501(c)(4) organizations that wish to engage in limited political activity while providing greater donor disclosures and political activity reporting to the IRS. It would provide an avenue for greater political activity for non-profit organizations without becoming an outright subsidizing of political activity by the government or becoming an additional opportunity for dark money entities to exert political influence.

V. CONCLUSION

As more American corporations have increasingly issued open statements on political issues, political candidates, and pending legislation, the temptation for § 501(c)(3) organizations to join the conversation should be tempered by well-reasoned compliance with the Code. As shown above, because of IRS limitations on the political activities of § 501(c)(3) tax-exempt organizations, those organizations should take special care to not violate the rules established by the IRC. However, changes to the Johnson Amendment, or perhaps a new section of the Code, should also be considered. Any potential changes to the IRC should increase the opportunity for free speech by § 501(c)(3) organizations. Striking a balance between the interest of the government and the free-speech interest of the organizations will better serve the public and the tax-exempt non-profit organizations. This result can be best achieved through proper reporting, a balanced legal framework, and equitably enforced oversight, rather than total prohibition.