

# CLIENT ADVISORY:

## IS A NOT FOR PROFIT ORGANIZATION PERMITTED TO ENGAGE IN LOBBYING ACTIVITIES?

Lobbying provides an avenue through which charities can create change in communities and be a voice for the marginalized or disenfranchised in society. However, organizations exempt from taxation under the Internal Revenue Code (“IRC”) Section 501(c)(3) are expressly prohibited from intervening in a political campaign, and lobbying activities must remain within permissible limits in order to maintain their tax exempt status.

Lobbying may be either “direct” or “grassroots.” Direct lobbying refers to direct communications with legislators for the purposes of influencing the outcome of legislation, whereas grassroots lobbying primarily involves attempts to influence legislation through efforts aimed at affecting the opinions of the general public or any segment thereof, including encouraging members to urge nonmembers to lobby.

The IRS employs two tests in determining whether the lobbying activities of a 501(c)(3) are at permissible level. The first is the “substantial part” test in which a charity’s lobbying cannot comprise more than an “insubstantial part” of the organization’s activities. This test is difficult to apply as neither the IRC treasury regulations nor private letter rulings provide clear guidance regarding what constitutes an “insubstantial part” of an organization’s activities. The penalty for excessive lobbying under this test is an irrevocable loss of 501(c)(3) non-profit status, resulting in all of its income being subject to taxation.

The second test, created by the Tax Reform Act of 1976, is the “expenditures” test in which lobbying is restricted to a certain percentage of a tax exempt organization’s expenditures. In order to be eligible for the “expenditures” test, exempt organizations must make an “election” under IRC 501(h) by filing IRS Form 5768.

The “expenditures” test provides a “safe harbor” with a mathematical method to determine with certainty the extent to which an electing organization may engage in lobbying, and provides that an organization’s 501(c)(3) tax exempt status will be revoked only if the sum total of its lobbying expenditures or total grassroots lobbying expenditures over a four-year period exceeds 150% of the maximum permissible amount. Further, expenditures that exceed permissible limits are subject to a tax of 25% of the amount of the excessive lobbying expenditures.

The term “lobbying” refers to communications that reference and reflect a view on a specific legislative proposal or legislation that has been introduced before a legislative body. Legislation includes “action by the Congress, by any State legislature, by any local council or similar governing body, or by the public in a referendum, initiative, constitutional amendment, or similar procedure.” Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii).



Not for profit organizations that lose exempt status due to excessive lobbying may not at any time thereafter be treated as IRC 501(c)(4) organizations (a category of organizations permitted to engage in lobbying).

The expenditures test provides that an electing 501(c)(3) organization may expend the following amounts on lobbying activities:

- 20 percent of the first \$500,000 of exempt purpose expenditures, plus;
- 15 percent of the next \$500,000 of exempt purpose expenditures, plus;
- 10 percent of the next \$500,000 of exempt purpose expenditures, plus;
- 5 percent of the remaining exempt purpose expenditures;
- Up to a total cap of \$1 million.

The expenditures test further limits grassroots lobbying to 25% of an organization's total permissible lobbying expenditures.

Making the election to be treated within the safe harbor of the expenditures test has two principal benefits. First, the expenditures test provides mathematical certainty, while the substantial part test is subjective. Second, the safe harbor rule protects 501(c)(3) exempt status in the case of excessive lobbying (up to 150% of the allowable amount calculated over a four-year period).

Because lobbying activities under the "expenditures" test are measured only by expenditures, lobbying activities that do not incur expense by the organization are excluded from the calculation of lobbying activities. For example, if an organization's volunteer engages in lobbying activities, to the extent the organization does not expend funds in support of the activities of that volunteer, those activities are not considered in measuring the organization's lobbying expenditures.

The IRC defines lobbying expenditures as "expenditures for the purpose of influencing legislation." If the primary purpose of an expenditure is a non-lobbying purpose (and the "fruits" of the expenditure are used for the non-lobbying purpose), then the expenditure will not be

allocated to lobbying. Stated conversely, "an organization will not be [regarded as primarily engaging in exempt activities] if more than an insubstantial part of its activities is not in furtherance of an exempt purpose." See Treas. Reg. § 1.501(c)(3)-1(c).

The Treasury Regulations provide the following illustration of application of the primary purpose exception:

Organization B researches, prepares and prints a code of standards of minimum safety requirements in an area of common electrical wiring. Organization B sells the code of standards booklet to the public and it is widely used by professionals in the installation of electrical wiring. A number of states have codified all, or part, of the code of standards as mandatory safety standards. On occasion, B lobbies state legislators for passage of the code of standards for safety reasons. Treas. Reg. § 56.4911-2(b)(4)(i), Ex. 5.

The Regulations explain that, in the foregoing example, since the "primary purpose of preparing the code of standards was the promotion of public safety and the standards were specifically used in a profession for that purpose . . . the research, preparation, printing and public distribution of the code of standards is not expenditure for a . . . lobbying communication." *Id.* However, expenses including "transportation, photocopying, and other similar expenses, incurred in lobbying state legislators for passage of the code of standards into law" are not in furtherance of B's exempt purpose, making them lobbying expenditures. *Id.*

However, tax exempt organizations should be wary of the "subsequent use rule", in which the subsequent grassroots lobbying use of "advocacy communications or research materials" that originally contained no lobbying communications may cause the original expense incurring and developing the materials to be treated as a lobbying expenditure. For example, if a tax exempt organization initially creates a nonpartisan analysis, study, or research report without any accompanying lobbying messages, and later uses that analysis, study or report in connection with grassroots lobbying communications, the subsequent use rule will convert the original expense into a grassroots lobbying expenditure.

The following activities are excluded from the definition of lobbying:

- Making available the results of nonpartisan analysis, study, or research, IRC § 4911(d)(2)(A).
- Providing technical advice or assistance (where such advice would otherwise constitute the influencing of legislation) to a governmental body or to a committee or other subdivision thereof in response to a written request by such body or subdivision, as the case may be, IRC § 4911(d)(2)(B).
- Appearances before, or communications to, any legislative body with respect to a possible decision of such body which might affect the existence of the organization, its powers and duties, tax-exempt status, or the deduction of contributions to the organization, IRC § 4911(d)(2)(C). This is the so-called “self-defense” exclusion.
- Communications between the organization and its bona fide members with respect to legislation or proposed legislation of direct interest to the organization and such members, other than communications encouraging members to influence legislation, IRC § 4911(d)(2)(D).
- Any communication with a governmental official or employee other than:
  - A communication with a member or employee of a legislative body (where such communication would otherwise constitute the influencing of legislation), or
  - A communication the principal purpose of which is to influence legislation, IRC § 4911(d)(2)(E)(i)-(ii).

Organizations exempt from taxation under IRC 501(c)(3) must refrain from lobbying outside specified limits; otherwise, they are subject to penalties for excess lobbying expenditures, or possibly, loss of 501(c)(3) status. Due to the numerous lobbying exceptions and benefits provided by making the 501(h) election, substantial lobbying can be achieved without exceeding the permissible limits imposed by the expenditures test. Accordingly, tax exempt organizations should carefully tailor lobbying efforts to take advantage of the election.



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