

# The Center on Philanthropy & Public Policy

## **PRIVATE FOUNDATIONS AND POLICYMAKING**

### **Latitude Under Federal Tax Law**

**Thomas A. Troyer  
Douglas Varley**

**Research Paper - 12  
May 2002**

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## **ABOUT THE CENTER ON PHILANTHROPY AND PUBLIC POLICY**

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## ABOUT THE AUTHORS

**Thomas A. Troyer** is a member in Caplin & Drysdale's Washington, D.C. office. He is one of the leading authorities on tax-exempt organizations in the country. He has spoken and written on taxation and tax matters affecting tax-exempt organizations since the 1960's. He has built Caplin & Drysdale's exempt organizations practice and is the senior member in the practice. He has served in a long list of professionally distinguished positions, including Vice Chair for Government Relations of the ABA Tax Section, Chair of the ABA Tax Section's Exempt Organizations Committee, Chairman of the Foundation Lawyers' Group, Member of the IRS Commissioner's Advisory Group on Exempt Organizations, and Member of the Treasury Department's Advisory Committee on Private Philanthropy and Public Needs. Troyer has also served and continues to serve on the boards of many philanthropic organizations, including The Carnegie Corporation of New York, the Children's Defense Fund, and the Natural Resources Defense Council.

Mr. Troyer has advised many of the country's largest private foundations and public charities on a wide array of federal tax matters and other legal matters. His expertise spans all aspects of the federal tax rules governing tax-exempt organizations, including qualification for tax-exempt status, restrictions on private foundations, unrelated business income tax, limitations on legislative and political activities of charities, formation of affiliates and subsidiaries, intermediate sanctions, and disclosure requirements. He also is fully conversant with the rules concerning the duties of nonprofit directors and officers. Troyer earned his J.D. at the University of Michigan Law School in 1958 and his B.A. at Harvard College in 1955.

**Douglas Varley** joined the firm in 1994 as an associate working principally in the exempt organizations practice group. He became a member of the firm in February, 2000.

Mr. Varley's practice primarily focuses on advising exempt organizations, in particular, private foundations. He has guided the design of major grantmaking programs and participated in the development of national public educational campaigns targeted at a range of significant policy issues. In addition to helping a diverse array of nonprofit organizations comply with the rules governing lobbying and political activities, his areas of experience also include such tax matters as international philanthropy, restrictions on executive compensation, transactions with for-profit organizations, and minimizing unrelated business income tax. Mr. Varley has written numerous articles and other pieces on tax-exempt organizations topics and has spoken at national meetings, including the Council on Foundations Annual Conference, the ABA Tax Section's Exempt Organizations Committee and the ALI-ABA program on Tax-Exempt Charitable Organizations. Before embarking on his legal career, Mr. Varley administered grantmaking programs for college and university faculty for the National Endowment for the Humanities. Mr. Varley received his J.D. from the University of Virginia School of Law in 1994, his M.A. from the University of Chicago in 1988 and his B.A., with Highest Distinction, from the University of Virginia in 1983.

## **Executive Summary**

The federal tax law provides considerable latitude for private foundations to participate in the formation of public policy. Although special restrictions apply to influencing legislative decisions and to election-related activities, much room remains for foundations to play a significant role in the formation of public policy. Our paper will review the applicable federal laws and provide examples of the kinds of work private foundations may support or conduct themselves.

### **The “Lobbying” Restriction: Basic Rules**

All charities are subject to revocation of their tax-exempt status if a “substantial part” of their activities is “lobbying.” Private foundations, however, are subject to an additional, tighter rule that prohibits them from spending any funds on lobbying. Despite these restrictions, the law allows foundations to play a significant role in the formulation of legislative policy. How is this possible? First, the federal rules define “lobbying” very narrowly to exclude many activities that can affect legislative decisions. Second, the law contains robust safe harbors that permit foundations to make grants to public charities that lobby without having the grantee’s lobbying attributed back to the foundation.

### **What Lobbying is Not**

Whether an activity is lobbying under the foundation rules depends on the content of the communication and the identity of the recipient. Hence, the law applies an objective “magic words” test to determine whether an activity violates the no-lobbying prohibition. It is what the foundation says that matters, not the organization’s subjective intent in making the communication.

If the recipient of a communication is a government official, a communication is “lobbying” only if it “refers to” and “reflects a view” on “specific legislation.” Consequently, for example, the law allows foundations to communicate with legislators about matters of broad social concern — as distinct from specific legislation — even if those matters are, or will be, addressed in legislation. This rule has enabled private foundations and their grantees to exercise significant influence on issues as diverse as funding for medical research, criminal sentencing, and education reform.

Similarly, the lobbying restrictions in no way impede foundations’ attempts to influence decisions by judges or actions by executive and administrative agencies such as the promulgation of regulations or the prosecution of enforcement actions. Thus, for example, foundations and their grantees were able to convince the Clinton administration to protect millions of acres in our National Forests as “roadless areas.” Now that efforts are underway to reverse this policy, foundations are again relying on the latitude they have to minimize the changes. Similarly, foundations are making grants to support a national public charity’s efforts to make sure that the Department of Agriculture keeps conservation a priority when the agency implements the new provisions of this year’s Farm Bill.

In addition to the broad avenues open to foundations to participate in administrative and judicial decisions, the federal law also offers significant, though more narrowly defined, opportunities for work concerning specific legislation. Significantly, several exceptions to the general ban on foundation lobbying provide valuable tools for working with government officials to influence legislative action.

The rules are even more favorable for communications directed to the general public. In this context, foundations can conduct and support activities — including web pages, email alerts, media advertisements — espousing a particular view on specific legislation without violating the restriction on lobbying. Generally, the federal tax law permits foundations to communicate (or fund a grantee's communication) with the public about specific legislation as long as the communication does not encourage the audience to contact a government official about the legislation. Consequently, subject to one relatively minor qualification, a foundation can safely pay for a radio or television message that criticizes or endorses a piece of pending legislation without contravening the tax law, so long as the message does not include a “call to action” encouraging listeners to contact a government official about the legislation.

### **Working with grantees to influence legislation**

Because public charities are able to engage in a significant amount of lobbying, they can generally be more effective advocates for, or against, legislation than the foundations that fund them. Hence, for most foundations, the principal means of participating in the legislative process is by supporting public charities that are working to achieve changes the foundation favors. The federal rules provide two safe harbors for foundation grants to public charities that prevent attribution of the grantee's lobbying to the foundation even if the grantee, in fact, uses the foundation's funds in lobbying. These safe harbors have enabled foundations to safely fund national advocacy campaigns opposing legislation that would weaken our environmental laws and promoting amendments that reform the funding of political campaigns.

### **Nonpartisan voter education and get out the vote activities**

Federal law prohibits private foundations and other charities exempt under section 501(c)(3) from intervening in any political campaign on behalf of (or in opposition to) any candidate for public office. In contrast to the bright-line rules that distinguish lobbying from permitted advocacy, the prohibition against campaign intervention involves a vaguer “facts and circumstances” analysis. Nonetheless, the IRS has identified a number of nonpartisan voter education activities that foundations may safely support or conduct themselves. Specifically, charitable organizations, including foundations, can sponsor candidate debates, publish candidates' responses to questionnaires, and distribute candidate voting records. Detailed restrictions apply to each of these activities, intended to ensure that the event or publication is strictly neutral among the candidates. Finally, private foundations can fund nonpartisan “get out the vote drives” and, under more stringent requirements, voter registration drives.

## **PRIVATE FOUNDATIONS AND POLICYMAKING: LATITUDE UNDER FEDERAL TAX LAW**

The federal tax law provides considerable latitude for private foundations to participate in the formation of public policy. Although special restrictions apply to influencing legislative decisions and to election-related activities, much room remains for foundations to play a significant role in the formation and implementation of government policies. This paper reviews the applicable federal laws and provides examples of the kinds of work private foundations may support or conduct themselves.<sup>1</sup>

### **THE “LOBBYING” RESTRICTION**

All organizations exempt from federal income tax by reason of section 501(c)(3) of the Internal Revenue Code are prohibited from engaging in substantial attempts to influence legislation. Private foundations — a subcategory of section 501(c)(3) organization — must, however, obey a stricter rule. In contrast to public charities, which can conduct a considerable amount of legislative work, foundations are prohibited from funding or engaging in any “lobbying” at all.<sup>2</sup> Although this prohibition is absolute, it is also narrow and very clearly defined. In drafting the laws that restrict foundations’ work in this area, Congress and the Treasury Department have taken considerable care to ensure that foundations, and their charitable grantees, can spend their resources on a broad array of activities that improve the quality of the legislative process. In addition, it bears emphasis that the federal limitations on lobbying in no way impede foundations’ ability to influence actions by executive or administrative branches of governments. Nor do they restrict foundations from litigating in support of policies they favor.

Hence, while there are certain kinds of legislative activity that foundations are strictly prohibited from supporting, there is much room for advocacy work that can affect legislation and other policy outcomes. In addition, by relying on special safe harbor rules, foundations can make grants to like-minded public charities that are engaged in lobbying activities foundations could not conduct themselves. Thus, foundations frequently can have an even greater impact on the legislative process as funders than they can achieve directly. By paying close attention to the rules discussed here, foundation executives and staff, as well as their legal advisors, can help their organizations advocate government policies that advance charitable objectives while complying fully with their obligations under the federal foundation laws.

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<sup>1</sup> This paper does not address state laws that may apply to foundations that conduct or support advocacy activities. Nor does it discuss the federal Lobbying Disclosure Act, which defines “lobbying” differently from the tax law and may require foundations active in the policy-making arena to register with Congress.

<sup>2</sup> As used here, the term “private foundation” or “foundation” refers to organizations that are exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code that are not “public charities.” Public charities are section 501(c)(3) organizations that qualify for more favorable tax treatment because of the activities they conduct or the diversity of their contributors. Both private foundations and public charities are “charities” as that term is used here.

## **HISTORICAL CONTEXT**

Congress enacted the ban on foundation lobbying as part of the Tax Reform Act of 1969, which established the current regulatory regime for foundations. Prior to 1969, Congress had paid only episodic attention to foundations. In particular, policymakers gave little thought to the role of foundations in the formation of legislation. Indeed, the most comprehensive assessment of foundations during that period, the Treasury Department Report on Private Foundations,<sup>3</sup> did not mention legislative activities by foundations as an abuse that needed to be addressed. When historical circumstances came together in 1969 for passage of broadscale foundation legislation, however, Congress added the flat prohibition against foundation lobbying (along with several other restrictions) to the package of reforms the Treasury Department had recommended. The record reveals little about the precise motivation underlying this part of the legislation. Most likely the new, stricter rule for foundations simply reflected the unusually fierce hostility Congress felt toward foundations at the end of the 1960s.

Since that time, legislative activity by foundations has enjoyed the same general lack of congressional attention as before 1969. Although Congress has occasionally taken up the issue of the appropriate level of policy involvement by charities in general — most notably in 1976 when it enacted new rules to encourage public charities to participate in the legislative process — foundations have been largely ignored. Thus, while the specter of the Tax Reform Act of 1969 and the threat of congressional retaliation looms large in the minds of foundations (and their legal advisors), in fact in the more than thirty years since 1969, Congress has not once tightened the 1969 rules for foundations.

## **PENALTIES FOR FOUNDATION LOBBYING**

Private foundations are subject to a 10 percent penalty tax on any expenditure for an attempt to influence legislation at the federal, state or local level.<sup>4</sup> 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 larger second level penalty tax. As noted above, 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. As far as the authors are aware, this more draconian sanction has never been imposed on a private foundation and, since 1976, only very rarely on public charities.

## **WHAT CONSTITUTES LOBBYING: GENERAL DEFINITIONS**

Under regulations adopted in 1990, whether an activity is lobbying depends on the content of the communication and the identity of the recipient. In short, the law applies an objective “magic words” test to determine whether an activity violates the no-lobbying prohibition. Prior to the appearance of these regulations, foundations and other charities confronted considerable

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<sup>3</sup> Senate Committee on Finance Committee Print 89<sup>th</sup> Cong., 1<sup>st</sup> Sess. (1965).

<sup>4</sup> IRC § 4945(d)(1).



uncertainty about the activities they could conduct in connection with the formulation of legislation. To remove this uncertainty and, thus, provide section 501(c)(3) organizations the ability to participate in the policymaking process as Congress intended, the Treasury Department developed a set of clear, bright-line definitions that put all parties on notice about what is, and is not, lobbying.

As the law stands today, it is what the foundation *says* that matters, not its subjective intent in expressing its views. In the technical language of the regulations, an activity is lobbying for purposes of the private foundation rules only if it involves either a “direct lobbying communication” or a “grassroots lobbying communication.” Both of these terms have quite narrow and, in certain respects, rather counter-intuitive definitions. Foundations’ ability to take full advantage of the possibilities these rules provide for supporting policy-related activities depends on understanding these definitions and their application.

## **DIRECT LOBBYING**

A direct lobbying communication is a statement to a legislator or legislative staff member that (a) refers to specific legislation and (b) reflects a view on that legislation.<sup>5</sup> This definition immediately excludes from the set of prohibited activities all efforts to influence legislators’ views on matters other than specific legislation. Hence, the legal rules permit foundations to discuss policy issues with legislators or staff even if those issues are the subjects of pending legislation, provided the foundation does not refer to that legislation.<sup>6</sup> The signal benefit of this rule is that a foundation does not have to stop expressing its views to legislators on a broader policy issue just because there is a pending piece of legislation that addresses an aspect of that policy.

Example: A foundation, or its grantee, prepares a brief paper summarizing the need for scientific research on sources of renewable energy. The paper does not reflect a view on any specific legislative proposal, though there is legislation pending in Congress that would provide tax credits to encourage scientific research of the sort the foundation supports. Under the basic definition of direct lobbying, giving the report to a member of Congress would not violate the prohibition against foundation lobbying.

A similarly important aspect of the lobbying definition is that attempts to influence actions by administrative agencies are not lobbying no matter how pointedly the foundation expresses its views on the specific action in question. Accordingly, while a foundation cannot send letters to

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<sup>5</sup> Treas. Reg. § 53.4945-2(a) and § 56.4911-2(b)(1)(i). For purposes of this definition, recipients of a lobbying communication may also, under quite limited circumstances, include executive branch personnel involved in the legislative process, and the term “specific legislation” includes not only acts, bills, resolutions and legislative vetoes but also specific legislative proposals that have not been introduced; ballot initiatives and referenda; and proposed treaties that must be submitted to the Senate for ratification — but only after negotiations have begun. Treas. Reg. § 56.4911-2(d)(1).

<sup>6</sup> Treas. Reg. § 53.9945-2(c)(2).

members of Congress expressing support for a bill that would limit mining on public land, it can press officials at the Department of the Interior for regulations that would have the same effect. Since the impact of executive and agency decisions can be as far reaching as legislative action, this rule offers foundations a very significant opportunity to participate in the formation of public policy.

Example: In January of 2001, the Clinton administration issued the Roadless Area Conservation Rule, which barred virtually all road building on 58.5 million acres in national forests. This rule was the result of three years of work and hundreds of meetings where nonprofit organizations, funded in part by foundations, met with White House and agency officials to press for adoption of the rule. None of these meetings were “lobbying” because the roadless rule is not legislation.

Example continued: The timber industry filed suit in federal court to have the roadless rule set aside as illegal. Nonprofit groups, again with foundation support, met with officials at the Department of Justice to encourage the agency to defend the rule vigorously. The meetings were not lobbying because the Department’s decision is not legislation.

The legal rules provide additional protection for foundations working to affect administrative actions by stating expressly that a communication with an executive branch official will not be lobbying unless the primary purpose of the communication is to influence legislation.<sup>7</sup> Thus, under the primary purpose standard, foundations need not worry that efforts to influence nonlegislative decisions will be recharacterized as lobbying merely because legislation is mentioned in the course of exchanging information with an executive branch official.

Example: A foundation program director meets with a senior official at the Environmental Protection Agency to urge tightening of the clean air regulations. During the course of the conversation, they discuss incidentally possible legislative responses to the new regulations. Since discussing legislation is not the primary purpose of meeting, it is not lobbying.

Example continued. Later the program director meets with the same EPA official with the primary purpose of asking her to testify before a congressional committee in support of reauthorizing the Clean Air Act. The meeting is lobbying, because the primary purpose of the meeting is influencing action by Congress.

## **GRASSROOTS LOBBYING**

The foundation rules are even more generous with respect to efforts to influence public opinion on policy issues, including legislation. The law defines prohibited “grassroots lobbying” as (a) a communication with the public that: (b) refers to specific legislation; (c) reflects a view on that legislation; and (d) includes a “call to action” that encourages the recipient to contact a

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<sup>7</sup> Treas. Reg. § 56.4911-2(b)(1)(i)(B).

government official about the legislation.<sup>8</sup> Under this definition, public communications — including television and radio spots, web pages, and mass mailings — that forcefully state a position for, or against, pending legislation will not violate the ban on foundation lobbying if they do not overtly encourage contacts with legislators or other government officials who participate in the formation of legislation.

Example: A foundation makes a grant to pay for the following radio spot. “The state assembly is considering a bill that would make gun ownership illegal. If this egregious legislation passes, you and your family will be criminals if you exercise your constitutional right to protect yourselves.” The ad is not lobbying because it does not encourage listeners to contact a government official.<sup>9</sup>

There are two exceptions to the general rule that a communication with the public will not be lobbying unless it includes a call to action. The first involves paid mass media advertisements on “highly publicized legislation.”<sup>10</sup> Under a special rule, a paid ad concerning such legislation is presumed to be grassroots lobbying if it runs within two weeks of a vote on the legislation even if it does not encourage contacting government officials.

Example: Assume the radio spot on the gun bill described above runs within two weeks of a vote on the gun legislation and that the legislation is “highly publicized.” The ad will be presumed to be lobbying because it refers to the bill.

The second exception to the “call to action” arises in the narrow case of referenda and ballot initiatives. The foundation rules treat communications with voters about these measures as direct lobbying.<sup>11</sup> Accordingly, no call to action is necessary for such a communication to violate the ban on foundation lobbying. Simply expressing a view on the initiative or referendum will be sufficient.

Despite the more restrictive rules that apply in the case of referenda and ballot initiatives, there remains a significant roll for foundation-funded activities in this area. First, as for any communications with members of a legislative body, it is perfectly permissible for foundations to

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<sup>8</sup> Treas. Reg. § 56.4911-2(b)(2). Under these rules, a communication includes a “call to action” only if it: (1) tells the recipient to contact a government official about the legislation; (2) provides the address or telephone number of a legislator (or employee of a legislative body); (3) provides a petition, tear-off postcard, etc. addressed to a government official; or (4) specifically identifies a legislator who will vote on the legislation 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 is not a call to action. Treas. Reg. § 56.4911-2(b)(2)(iii).

<sup>9</sup> Based on Treas. Reg. § 56.4911-2(b)(5)(iv), Example (4).

<sup>10</sup> Whether legislation is highly publicized depends on the level of media coverage it receives and the extent to which the general public is aware of the legislation. Treas. Reg. § 56.4911-2(b)(5)(iii).

<sup>11</sup> Treas. Reg. § 56.4911-2(b)(1)(iii).

provide the public with information about the general subject of a referendum or initiative so long as there is no reference to the measure itself.

Example: In the weeks before the public votes on bonds that will provide funds for public schools, a foundation pays for television spots that emphasize the importance of education for children of all income levels. The ads do not refer the bond initiative. Therefore, they are not lobbying.

Example: A mid-sized city has placed on the ballot a measure that would authorize fluoridation in the city's water. Around the same time, a local health foundation takes out an ad in several newspapers explaining the benefits of fluoride for oral health. As long as the ads do not refer to the ballot measure, they are not lobbying.

In states where items are placed on the ballot through a petition process, it is clear under the tax rules that an initiative or referendum is not “specific legislation” until its proponents begin collecting signatures.<sup>12</sup> Consequently, foundations can be confident that activities that occur earlier in the process — such as research to design an initiative or polling to test its viability — will not be lobbying.

## **EXCEPTIONS TO THE DEFINITION OF LOBBYING**

Even if an activity satisfies the definition of direct or grassroots lobbying, it nonetheless is permissible for foundations if it falls within an exception to the basic definition. The most important exception excludes the preparation and distribution of “nonpartisan analysis and research.” This exception permits foundations, or their grantees, to offer legislators, executive branch officials, and the public materials that make forceful, substantive arguments for or against specific legislation, provided the materials present a sufficiently full and fair exposition of the legislation to allow the recipient to form his or her own conclusions.<sup>13</sup> Although the lobbying regulations do not specifically define the “full and fair” standard, the available authority indicates that the fundamental requirement is that the material provides a factual basis for its conclusions and argues for them in a reasoned fashion.<sup>14</sup> Foundations have relied on this exception to hold policy briefings on Capitol Hill, to invite legislators and staff to symposia where substantive legislative analyses are presented, and even to produce documentary films on legislative topics.

Traditionally, the exception for nonpartisan analysis and research has been the principal vehicle through which foundations have gotten their views before policymakers. As major funders of scholarly and scientific research, foundations have supported much of the primary intellectual analysis that informs the national policy debate in many areas. The nonpartisan analysis and

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<sup>12</sup> Treas. Reg. § 56.4911-2(d)(1)(ii).

<sup>13</sup> Treas. Reg. § 53.4945-2(d)(1). In addition to satisfying the “full and fair” exposition standard, nonpartisan analysis and research must also be distributed to persons on both sides of the legislation addressed.

<sup>14</sup> See Rev. Proc. 86-43, 1986-2 C.B. 729.

research exception allows foundations to package that work as forceful, reasoned briefs for the legislative outcomes they desire and give them to legislators.

A second useful, though more limited, exception to the basic lobbying definition excludes oral or written responses to written requests for technical assistance from a legislative committee, subcommittee, or other governmental body.<sup>15</sup> In order to qualify for this exception, the written request must come on behalf of the legislative body itself, not from an individual legislator asking on his or her own behalf. Where such a request solicits the foundation's views on the legislation, it grants foundation executives broad ability to state their organization's full analyses of, and conclusions on proposed legislation directly to legislators.

A third exception allows foundations to communicate with government officials involved in the legislative process about specific legislation that could affect the foundation's existence, powers, duties, tax-exempt status, or right to receive tax-deductible contributions.<sup>16</sup> Relying on this exception, foundations have pressed Congress for favorable changes to the tax code provisions that regulate them, including reductions in the tax they pay on their investment income and the ability to provide donors a deduction equal to the value of publicly traded stock. Of broader relevance, this "self-defense" exception has permitted foundations to fund advocacy against attempts to curtail the advocacy rights of charities.

Finally, a narrow exception to the lobbying definition allows foundations 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 jointly-funded program.<sup>17</sup> Although this exception is not relevant to foundations interested only in changing substantive laws, it can be enormously useful to foundations seeking government funding for particular projects. Thus, while discussions between a foundation and a legislator about appropriations legislation are generally prohibited, under this exception a foundation can ask a legislator's assistance in obtaining an appropriation for a project the foundation is supporting. Obvious examples involve foundations seeking government funding for a public facility, like a hospital or park, the foundation is supporting.

## **WORKING WITH PUBLIC CHARITY GRANTEES THAT LOBBY**

As noted above, the law allows public charities to engage in a significant amount of lobbying.<sup>18</sup> Consequently, these organizations can generally be more effective advocates for, or against,

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<sup>15</sup> Treas. Reg. § 53.4945-2(d)(2).

<sup>16</sup> Treas. Reg. § 53.4945-2(d)(3).

<sup>17</sup> Treas. Reg. § 53.4945-2(a)(3).

<sup>18</sup> Under section 501(h) of the Internal Revenue Code, public charities may spend up to 20 percent of the first \$500,000 of their program budget on lobbying. For organizations with larger budgets, the permitted lobbying percentage decreases as the size of the budget increases, reaching a maximum lobbying expenditure limit of \$1 million for organizations with charitable budgets of \$17 million or more. Lower limits apply to grassroots efforts to mobilize the public.

legislation than the foundations that fund them. Hence, while there is much foundations can do themselves, for most foundations, the principal means of participating in the legislative process is supporting public charities working to achieve changes the foundation favors.

The regulations provide two safe harbors for foundation grants to public charities that prevent attribution of the grantee's lobbying to the foundation even if the grantee, in fact, uses the foundation's funds to lobby. These rules have enabled foundations to fund advocacy campaigns that include lobbying on topics as diverse as tobacco taxes, criminal sentencing, funding for after school programs, and campaign finance reform.

The first safe harbor provides that a private foundation can make a general purpose grant to a public charity engaged in lobbying activities without risking any tax penalty. As long as the grant is not "earmarked" for lobbying, it will not be treated as a lobbying expenditure by the foundation even if the grantee uses some or all of the funds to pay for lobbying expenses.<sup>19</sup> For these purposes, a foundation grant is "earmarked" if there is an agreement between the foundation and the grantee that the funds will be used to support specific activities. The mere fact that the foundation knows the organization will be engaged in lobbying during the grant period does not constitute earmarking and will not cause a general support grant to be a lobbying expenditure for the grantor. Hence, this protective rule allows a foundation to identify public charities that advocate legislative positions it wants to see adopted and to provide those organizations general operating support thereby increasing their ability to promote the foundation's policy agenda.

In practice, foundations make relatively few general support grants, preferring instead to fund specific projects. The second safe harbor in the foundation rules addresses this kind of grant. The federal regulations state explicitly that a private foundation can make a grant to a public charity for a specific project *that will include lobbying* provided the amount of the grant is no more than the amount budgeted by the grantee for non-lobbying expenditures.<sup>20</sup> Absent earmarking, such a grant will not be a prohibited lobbying expenditure for the grantor even if the grantee spends more on lobbying than projected and uses the foundation's grant to pay these costs. Thus, the rule for project grants creates an opportunity for foundations to target their grants on activities that directly advance their legislative objectives.

Example: A public charity 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 lacking a call to action that will educate the public about this issue; and (3) meeting with legislators and staff to urge passage of legislation restricting development in the area. The budget for the project indicates that the grantee expects to spend \$80,000 on activities that will not be lobbying

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<sup>19</sup> Treas. Reg. § 53.4945-2(a)(6)(i). It is worth noting that the foundation will be protected even if the grantee loses its tax-exempt status because of excessive lobbying. Treas. Reg. § 53.4945-2(a)(7).

<sup>20</sup> Treas. Reg. § 53.4945-2(a)(6)(ii).

and \$20,000 on activities that will be lobbying. The foundation can safely make a grant for the project of up to \$80,000.<sup>21</sup>

In sum, notwithstanding the ban on foundation lobbying, the law leaves foundations able to conduct or fund an expansive set of advocacy activities. These rules are technical and complex, but once a foundation understands them, it can safely include support for legislative advocacy among the strategies it uses to achieve its charitable objectives. Given the centrality of government action in protecting and promoting the public good in our system, it is not surprising that foundations find this strategy to be among the most potent means of advancing their broader purposes.

## **A NOTE ABOUT ELECTIONEERING**

Federal law prohibits all organizations exempt under section 501(c)(3), including private foundations, from intervening in any political campaign on behalf of (or in opposition to) any candidate for public office.<sup>22</sup> The rules in this area contrast markedly from those that apply to lobbying. Most important, where the lobbying analysis is informed by bright-line definitions that clearly distinguish lobbying from permitted advocacy, the prohibition against campaign intervention involves a vaguer “facts and circumstances” analysis. There is no “magic words” test here.

Consequently, planning advocacy activities that will involve, or merely occur proximate in time to, an election frequently calls for the careful exercise of informed judgment. This difficulty is compounded by the seriousness of the potential penalties for violating the electioneering ban. In contrast to lobbying, where foundations face only a small penalty tax for activities that are “insubstantial,” the penalty for any electioneering is, theoretically at least, loss of the foundation’s tax exemption. Hence, foundations generally should seek advice of experienced tax counsel before conducting or funding activities associated with an election.

Although due caution is appropriate, the electioneering ban does not mean that foundations are prohibited from conducting advocacy and voter education activities simply because an election is near. In fact, foundations both fund and conduct a range of activities that take place around elections. For example, foundations have funded or conducted national voter education programs distributing information about candidates - the Markle Foundation’s Web White and Blue site being a notable example - paid for research into how election campaigns are financed, and supported advocacy activities designed to call attention to particular policy issues during the election season. The touchstone for distinguishing these permissible activities from prohibited electioneering is that all the foundation’s efforts must be strictly nonpartisan in both form and substance.

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<sup>21</sup> Again, loss of the grantee’s tax-exempt status will not alter the legal consequences of the grant for the foundation.

<sup>22</sup> IRC § 501(c)(3). For private foundations, this prohibition is backed up by the same penalty tax as applies to lobbying expenditures. IRC § 4945(d)(2).

In determining whether an activity meets this standard, the IRS will consider any evidence that the organization had a partisan motive in conducting the activity as well as whether the organization should reasonably have foreseen that its efforts would benefit one candidate over another. Hence, an activity may be characterized as partisan even though it does not involve an explicit endorsement of a particular candidate or party. In this way, the campaign prohibition is broader than the “express advocacy” standard that the Supreme Court has applied under the federal election laws.<sup>23</sup>

Nonetheless, the IRS has stated explicitly that the law does not require organizations to refrain from the activities they regularly carry on simply because an election is near.<sup>24</sup> In particular, the IRS does not expect charities to stop advocating for policy positions they support close to an election, provided their efforts serve a legitimate nonpartisan purpose and are not being carried out to benefit a particular candidate. Moreover, the IRS recognizes that electioneering requires more than just a positive or negative correspondence between the charity’s position on an issue and a candidate’s position. Rather, a charity violates the prohibition only if its issue ads contain an overt indication that the organization supports or opposes a particular candidate or slate of candidates. That is, the IRS is concerned about ads that use issue labels like “conservative” or “pro-choice” as code words to describe a candidate. Hence, as long as a foundation or its grantee does not link its position on issues with a particular candidate or party, its issue advocacy should not run afoul of the electioneering ban.

In addition to nonpartisan issue advocacy, the IRS has identified a number of voter education activities that foundations may safely support or conduct themselves. Specifically, charitable organizations, including foundations, can sponsor candidate debates, publish candidates’ responses to questionnaires, and distribute candidate voting records. Detailed restrictions apply to each of these activities, intended to ensure that the event or publication is strictly neutral among the candidates. Finally, private foundations can fund nonpartisan “get out the vote drives” and, under more stringent requirements, voter registration drives. A detailed recounting of the legal requirements for those activities is beyond the scope of this paper.

## CONCLUSION

Private foundations are subject to special restrictions that limit their ability to lobby and participate in election campaigns. Despite these restrictions, foundations can and do play a significant role in formation of public policy. In particular, foundations can support a wide array of activities that — while not “lobbying” under the federal foundation rules — have a direct and important impact on the legislative process. Moreover, the foundation rules include broad safe harbors that allow foundations to fund public charities conducting the relatively narrow set of lobbying activities. Finally, the special rules that bar all charities from attempting to influence

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<sup>23</sup> Foundations conducting issue advocacy around elections will want to consult their advisors about the election law reforms dealing with this topic that Congress recently enacted as part of the Bipartisan Campaign Reform Act of 2002 (effective only after the date of this fall’s congressional elections).

<sup>24</sup> Judith Kindell and John Reilly, Election Year Issues, Exempt Organizations Technical Instruction Program for FY 2002, 334, 345, IRS.



election results need not constrain foundations from promoting nonpartisan issue agendas even during the campaign season. Thus, foundations willing to invest the effort necessary to understand the legal rules that govern them can safely include seeking policy change as a potent means of furthering their charitable objectives.