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Oregon Department of Justice Begins Issuing Disqualification Orders

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At this time of year, the Oregon Attorney General usually publishes a list of the 20 Worst Charities operating in the state in an effort to educate the public and to encourage thoughtful giving. Organizations that had the dubious honor of making the list were those that spent the least on program services. For example, the charities on the 2014 Worst Charities list spent only 6.5% - 32% of their expenses on charitable programs. This year, the list is much smaller due in no small part to the enactment of HB 2060.

HB 2060 was passed in 2013 and is now codified at ORS 128.760 – 128.769. The law authorizes the Attorney General to issue orders disqualifying charities from receiving donations that are deductible for Oregon income tax purposes if the charity does not meet certain expenditure requirements. A charity will be subject to disqualification if it does not expend a minimum of 30% of its expenses on charitable programs, averaged over a three-year period. The 30% minimum is calculated based on organizations' Form 990, Part IX Statement of Functional Expenses.

After the legislation was passed, the Department undertook the process to adopt administrative rules for the implementation and enforcement of the statute. The administrative rules were finalized and became effective on July 1, 2015; they can be found at OAR 137-010-0032. The OARs set forth the process for notice and hearings, if requested, before final disqualification orders can be issued.

With the adoption of administrative rules, the Department has begun issuing Notices of Intent to Issue Disqualification Orders. To date, the Department has issued twelve notices to organizations that met the disqualification criteria. Several organizations that have been identified in past "worst charity" lists had closed or ceased solicitations in Oregon before the Department began issuing notices. In response to the Notices, eight organizations have voluntarily agreed to cease conducting business in Oregon, including soliciting Oregon residents. The Department has issued Final Disqualification Orders to an additional three

organizations — Dakota Indian Foundation, Inc., Firefighters Support Foundation, Inc., and National Veterans Services Fund, Inc. Resolution of the remaining outstanding notice is pending.

Final Disqualification Orders are posted on the Department of Justice's website and can be found at http://www.doj.state.or.us/charigroup/Pages/disqualified.aspx. Organizations that are subject to disqualification orders must disclose their disqualified status in solicitations to Oregon residents, and failure to do so can result in substantial penalties under the Unlawful Trade Practices Act. The organizations remain disqualified until they can establish they meet the minimum expenditures standards and, in no event, will their status change in less than one year. Donations made to disqualified organizations more than 30 days after the date the disqualification order is posted to the Department's website are not deductible as charitable contributions for Oregon income tax purposes, although the donor may be able to claim the deduction if they have a written donation acknowledgement from the organization that does not include the required disclosure of the organization's disqualified status.

The Attorney General is hopeful this new law will help reduce the number of sham and disreputable charities operating in the state and that, eventually, there is will be no need for a Worst Charities list.

A Primer on 501(c)(3) Election-Related Lobbying

Christy Mason, Our Oregon, Portland, Oregon

Recently the U.S. Tax Court reminded us that private charitable foundations engage in lobbying at their peril.[1] In *Parks Foundation*, payments for radio messages related to ballot measures were deemed to be taxable expenditures. But of the two types of IRC section 501(c)(3) organizations – public charities and private foundations – only private foundations are prohibited from lobbying. Clear IRS guidelines show that public charities may support or oppose ballot measures.

Here is a short review of the basics around 501(c)(3) election-related lobbying, including a look at some relevant Oregon rules.

Lobbying

Lobbying is communication that attempts to influence specific legislation. The IRS defines nonprofit lobbying narrowly and with specificity so that it can be measured accurately by organizations who wish to engage in it. There are two kinds of lobbying -- grassroots and direct. Grassroots lobbying refers to the ways the general public may be influenced to contact their legislators about a particular piece of legislation.[2] Direct lobbying consists of communications directly with legislators themselves.[3] When the general public votes on ballot measures, they are acting as "legislators" themselves because they, and not elected officials, are making law. Direct lobbying communications must in some way relate to the specific legislation (measure or referendum) and express a view on it. It is intentional and aimed at the voter. Lobbying is not the same as general advocacy which can be carried on at anytime and anywhere by just about anyone.

1 *Parks Foundation v. Commissioner*, 145 T.C. No. 12 (issued November 17, 2015).
2 Treas. Reg. Sections 65.4911(b)(2).
3 Treas. Reg. Sections 65.4911-2(b)(1).

The Parks Foundation case highlights the differences between a direct lobbying message and a general educational statement or airing of opinion. A particular communication at issue was a radio message that criticized the state's shutdown of a state prison work program.[4] The message referred to a ballot measure about the program that had passed three years earlier and mentioned what Oregon voters may have expected as a result of that measure. The message was aired about two months before a special election in which Oregonians were to vote on a ballot measure reinstating the program. The radio piece referred to what the attorney general, the governor and "Oregon Voters" had done or thought about having prisoners work.

The Tax Court held that even though the radio message did not mention the measure by name or number, the description of the subject program in the messages was the same as that "widely used in connection with" the ballot measure around the same time and was thus deemed to be related. In addition, the "emphatic endorsement" of the program at issue reflected a view on the ballot measure. The Court made a factual determination based on the regulations around the language, timing, and tone of the communication.

During ballot measure season, public charities may engage in all of the following lobbying activities: writing ballot measures; publicly endorsing or opposing ballot measures; circulating initiative petitions for signatures; loaning or contributing money or property to measure campaigns; buying radio or newspaper ads to express support or opposition to a measure; writing newsletter pieces; and encouraging others to vote for or against ballot measures. Communications include radio and t.v. ads, letters, mailers and phone calls. Other sorts of communications never constitute lobbying: research or fact sheets that present all sides of an issue; general examinations of broad economic or social issues; or specific challenges to a measure that might change the organization's rights or its continued existence.[5]

Private Foundations

In 1969, Congress defined all 501(c)(3) organizations as "private foundations" – unless their support came from the general public or governmental sources.[6] To obtain tax-exempt status, all organizations have to be operated for public benefit, not private gain. Private foundations, funded by one individual or family or one corporation, were more strictly regulated in formal recognition of the possibility that private foundation funds might be spent on private rather than charitable purposes.[7] Lobbying on measures favored only by a few funders conflicts with the rationale of tax-exempt status in the first place. In addition to the threat of loss of tax-exempt status, Congress added a stringent system of excise taxes on expenditures supporting attempts to influence legislation.[8] Private foundations can make grants to specific projects that may include lobbying, as long as the grants are not "earmarked" for lobbying. If the grant does not exceed

4 *Parks*, 145 T.C. No. 12 at 11.

5 See Treas. Reg. Section 53.4945-2(d).

6 Churches, universities and hospitals are among the types of organizations that are not private foundations by definition.

7 1969-3 C.B. 423, 460.

8 IRC Secs. 4941, 4942 and 4945.

the non-lobbying part of the project's budget, in general, it would not violate the grantmaking rules for private foundations (or implicate the nonprofit accepting the grant).[9] And unlike much of nonprofit tax law, these private foundation rules prohibiting lobbying have been imported into Oregon statute, and are thus enforceable by the state.[10]

Public Charities

As for the other type of 501(c)(3) organization, a public charity that does (or will) pass the "public benefit" test is not a 509(a) foundation and may lobby. These organizations avoid the prohibition on lobbying "on the theory that their exposure to public scrutiny and their dependence on public support would keep them from the abuses to which private foundations were subject." [11] The organizational definition itself states that "no substantial part" of an organization's activities may be "carrying on propaganda, or otherwise attempting, to influence legislation." [12] Both direct lobbying and grassroots are permitted.[13] An organization may also be deemed to be spending on lobbying if it makes a contribution to another organization that does lobbying, but in general, only if the contribution is earmarked for lobbying.

As set out in the 501(c)(3) definition, a public charity must ensure that its lobbying does not rise to the level of a "substantial part" of its programs to retain its exempt status and/or be taxed on the expenditures. In order to determine the extent of an organization's lobbying expenditures, the IRS allows public charities to elect an expenditure test under section 501(h) to measure the spending against a bright-line standard.[14]

Under the 501(h) expenditure test, the amount an organization spends on its lobbying activity will not put its tax-exempt status into jeopardy, provided the limits are not normally exceeded annually over a four year period. [15] An organization may not spend over 20% of its first $500,000 of its exempt purpose expenditures on direct lobbying. Exempt purpose expenditures are amounts an organization spends to accomplish its exempt purposes, such as salaries, communications expenses, fundraising costs and the like. Allowed percentages decrease on additional expenditures. [16]

The 501(h) election creates a safe harbor, allowing organizations that stay within the limits to retain 501(c)(3) status, no matter how much lobbying is done. Expenditures are simply that: money going to salaries, services, transportation, signs – anything connected with the lobbying. The organization need not factor in the value of donated services or materials. As long as lobbying expenditures do not exceed 150% of the defined limitations over a four year period, the tax-exempt status is safe. [17] If the organization exceeds its lobbying expenditure dollar limit in any one year, an excise tax equal to 25% of the excess is levied.

Organizations that do not make the 501(h) election (by filling out and submitting a one-page form at any time during the tax year) remain under the more vague "insubstantial part" test, basically a study of the

9 Treas. Reg. Section 53.4945–2(a)(6)(ii)(A) and (B).
10 ORS 65.036(5); *see* also Parks v. Commissioner case.
11 *Quarrie Charitable Fund v. Commissioner*, 603 F.2d 1274, 1277 (7th Cir. 1979), aff'g 70 T.C. 182 (1978).
12 *See* Treas. Reg. Section 1.501(c)(3)-1(c)(3)(ii).
13 26 CFR 56.4911-2.
14 IRC sec. 501(h)(enacted as part of the Tax Reform Act of 1976, P.L. 94-455).
15 IRC Sec. 4911.
16 IRC sec. 501(h).
17 IRC sec. 4911.

facts and circumstances. Cases indicate that the allowable level lies somewhere between 5% and 20%. [18] Along with the lack of a numerical measuring stick, the charity must take the time to examine and place a value on a number of activities and services, in addition to actual spending. These may include numbers of volunteers involved, the relative importance of lobbying to the mission of the organization, how much time is spent lobbying versus other program activities and how long the organization has lobbied on a particular issue.[19]

Reporting Overview

Each 501(c)(3) organization must report its lobbying along with all of its other contributions and spending to the IRS each year. "Did the organization engage in lobbying activities, or have a section 501(h) election in effect during the tax year? If "Yes," complete Schedule C, Part II." [20] Note that a non-electing organization that did no lobbying during the tax year need not file a Schedule C. On that schedule, Part II-A requires entry of dollar amounts (electing), while Part II-B requires dollar amounts, numbers of personnel and other items, and a "detailed description of each lobbying activity" for each element of the (non-electing) lobbying program.

In Oregon, when a 501(c)(3) does direct lobbying for a particular ballot measure, it must report its contribution to the Secretary of State and/or to the ballot measure campaign. An independent expenditure, which is an expenditure for a communication that is not made with the cooperation, consent or at the suggestion of a ballot measure campaign, must be reported by the spending organization on the state's campaign finance reporting website, ORESTAR.[21] Money or in-kind contributions given directly to a campaign supporting or opposing a ballot measure in coordination with the campaign should be reported to the recipient – campaign or political committee – which is responsible for its proper reporting.[22] There are no restrictions at all on expressing support or opposition to a ballot measure. A nonprofit does not become a political committee itself by spending, or carrying out direct lobbying. Lobbying expenditures made in support of a campaign/political committee that is required to report that contribution on ORESTAR are accounted for by the contributing organization either under the 501(h) accounting or insubstantial-part evaluation.[23]

Note that the Oregon Government Ethics Commission, which regulates lobbyists who attempt to influence legislation through communication with elected officials, does not regulate lobbying and/or spending in connection with ballot measures.[24]

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18 *See Seasongood v. Comm'r*, 227 F.2d 907, 912 (6th Cir. 1955).

19 *Christian Echoes Nat'l Ministry, Inc. v. United States*, 470 F.2d 849 (10th Cir. 1972*; Haswell v. United States*, 500 F.2d 1133, 1146-47 (Ct. Cl. 1974).

20 Form 990, Part IV, Line 4.

21 See login and other information at http://sos.oregon.gov/elections/Pages/orestar.aspx.

22 Oregon Secretary of State, Elections Division, Campaign Finance Manual.

23 See ORS 260.005(18)(b)(A), (B).

24 Definitions for ORS 171.725 to 171.785 (State Legislative Department and Laws, Lobbying Regulation) do not include "voters" as those who can be lobbied.

Conclusion

Any number of well-known advocacy organizations, law firms and think tanks offer in-depth publications that explain in great detail the tax laws and regulations that govern 501(c)(3) lobbying. Communications, properly reported, make up an important part of what public charities can do around a ballot measure election.

Oregon Nonprofit Legislative Update

Michele Wasson, Stoel Rives, Portland, Oregon

In recent years, the legislature has enacted a number of changes to laws affecting Oregon nonprofits. The summary below highlights three of these important changes.

Low Income Housing Property Tax Exemption (HB 2690). This bill was developed by Habitat for Humanity in coordination with Reps. Gomberg and Whisnant, among others to provide a property tax exemption for nonprofit low-income housing developments. HB 2690 amends ORS 307.162 to provide a new statutory exemption from property tax for land acquired and held by a nonprofit organization, as defined in ORS 307.130, for the purpose of building residences to be sold to individuals whose income is not greater than 80 percent of the area median income as adjusted for family size. Property is exempt from property tax for a period of seven years or until the property is sold. The nonprofit can apply for a three-year extension. As discussed in committee hearings, the purpose of the exemption is to prevent taxation of the land during the pre-construction development period, which can be lengthy. If the nonprofit still holds the land after 10 years or does not timely file an extension after seven years, the full property tax for all years plus interest will be due. Applies to property tax years beginning on or after July 1, 2015.

History or Science Museums Property Tax Exemption (HB 2171, §§ 46-49). Sections 46-49 of the omnibus tax bill HB 2171 temporarily amend ORS 307.130 to provide a property tax exemption specifically for certain history or science museums, including food service facilities, museum shops if 90 percent of the inventory is museum-related, and certain parking, theater, vacant, display, storage, meeting, and educational space. Space used for commercial enterprises, hotels, chapels, and water parks is not covered by the exemption. This exemption was supported by Sen. Boquist and was sought by Evergreen Museum. Applies to property tax years July 1, 2015 through June 30, 2019.

Subjecting Nonprofit Organizations to Certain Provisions of the Public Contracting Code (HB 2214). This new legislation amends ORS 236.605 to 236.610 to include nonprofit corporations in the definition of public employer for purposes of transfers of certain public employees. Nonprofits are now subject to ORS 236.610 requiring that if the duties of the employee have been transferred from a public employer to another public employer (now including nonprofits), the public employee must be transferred to and retained by the new employer at the same salary for 12 months. After the first 12 months, the transferred employee must be placed at the closest salary for the position under the new employer's salary schedule. The source of funding is negotiable. The transferring employer must liquidate accrued compensatory time, but the employee may choose to retain sick leave and vacation. Transfers do not include the transfer of an

employee from one nonprofit to another nonprofit corporation. Sponsored by House Interim Committee on Business and Labor for AFSCME Council 75. Effective date for HB 2214 is January 1, 2016.

2016 NOLS Brown Bag Lunch Discussions

The Nonprofit Organization Law Section is pleased to offer a brown bag lunch discussion series in an effort to provide section members an opportunity to connect with peers and discuss issues they are encountering in their practice in an informal, collegial setting.

Brown bag lunch discussions have been scheduled for 2016 on the following dates:

Wednesday, February 10, 2016
Wednesday, May 11, 2016
Wednesday, August 10, 2016
Wednesday, November 9, 2016

All discussions will be held noon – 1:00 p.m. at the Law Offices of Tonkon Torp, LLP, 888 SW 5th Ave., Suite 1600, Portland, Oregon 97204.

Please note this is not a lecture format. Attendees will be encouraged to engage in the discussion, share challenges they have encountered, and practices they have found to be effective.

Save the Date

First Thursday Social. NOLS will be holding a social event for its members on February 4, 2016. We hope you will be able to stop by, meet some colleagues, and enjoy some of the art on display on First Thursday. Details to come

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