



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET

DATE: 4/19/93

TO: Rossin Strong, OPD

FROM: Richard Loeb, OMB

The material concerning
contingent fees that we
discussed at the emergency
meeting. Sorry for the
delay, but I was out
all last week.

Regards

OMB FORM 38
Rev. Aug 73

(9) Assertions by the employees, former employees, or competitors of offerors, that an agreement to restrain trade exists.

(d) Identical bids shall be reported under this section if the agency has some reason to believe that the bids resulted from collusion.

(e) For offers from foreign contractors for contracts to be performed outside the United States, contracting officers may refer suspected collusive offers to the authorities of the foreign government concerned for appropriate action.

(f) Agency reports shall be addressed to the Attorney General, U.S. Department of Justice, Washington, DC 20530, Attention: Assistant Attorney General, Antitrust Division, and shall include—

(1) A brief statement describing the suspected practice and the reason for the suspicion; and

(2) The name, address, and telephone number of an individual in the agency who can be contacted for further information.

(g) Questions concerning this reporting requirement may be communicated by telephone directly to the Office of the Assistant Attorney General, Antitrust Division.

SUBPART 3.4—CONTINGENT FEES

3.400 Scope of subpart.

This subpart prescribes policies and procedures that restrict contingent fee arrangements for soliciting or obtaining Government contracts to those permitted by 10 U.S.C. 2306(b) and 41 U.S.C. 254(a).

3.401 Definitions.

“Bona fide agency,” as used in this subpart, means an established commercial or selling agency, maintained by a contractor for the purpose of securing business, that neither exerts nor proposes to exert improper influence to solicit or obtain Government contracts nor holds itself out as being able to obtain any Government contract or contracts through improper influence.

“Bona fide employee,” as used in this subpart, means a person, employed by a contractor and subject to the contractor’s supervision and control as to time, place, and manner of performance, who neither exerts nor proposes to exert improper influence to solicit or obtain Government contracts nor holds out as being able to obtain any Government contract or contracts through improper influence.

“Contingent fee,” as used in this subpart, means any commission, percentage, brokerage, or other fee that is contingent upon the success that a person or concern has in securing a Government contract.

“Improper influence,” as used in this subpart, means any influence that induces or tends to induce a Government employee or officer to give consideration or to act regarding a Government contract on any basis other than the merits of the matter.

3.402 Statutory requirements.

Contractors’ arrangements to pay contingent fees for soliciting or obtaining Government contracts have long been considered contrary to public policy because such arrangements may lead to attempted or actual exercise of improper influence. In 10 U.S.C. 2306(b) and 41 U.S.C. 254(a), Congress affirmed this public policy but permitted certain exceptions. These statutes—

(a) Require in every negotiated contract a warranty by the contractor against contingent fees;

(b) Permit, as an exception to the warranty, contingent fee arrangements between contractors and bona fide employees or bona fide agencies; and

(c) Provide that, for breach or violation of the warranty by the contractor, the Government may annul the contract without liability or deduct from the contract price or consideration, or otherwise recover, the full amount of the contingent fee.

3.403 Applicability.

This subpart applies to all contracts. Statutory requirements for negotiated contracts are, as a matter of policy, extended to sealed bid contracts.

3.404 Solicitation provision and contract clause.

(a) Prospective contractors are generally required to disclose contingent fee arrangements, other than those with full-time bona fide employees working solely for the prospective contractor, in order to permit the Government to evaluate the arrangements before award.

(b) The contracting officer shall insert the provision at 52.203-4, Contingent Fee Representation and Agreement, in solicitations, except when—

(1) The contract amount is not expected to exceed the limitation prescribed in 13.000;

(2) The solicitation is for personal services to be paid for on a time basis;

(3) The solicitation is for utility services, at rates regulated by Federal, State, or other regulatory bodies, from a public utility company that is the sole source;

(4) The award under the solicitation is to be made in a foreign country; or

(5) Any other Department of Defense contracts, individually or by class, have been designated by the Secretary for exception. Reports of such exceptions shall be filed promptly with the Administrator of the General Services Administration.

(c) The contracting officer shall insert the clause at 52.203-5, Covenant Against Contingent Fees, in all solicitations and contracts.

3.405 Review of Contingent Fee Representation and Agreement.

(a) Prospective contractors may not use any claimed professional or special relationship (other than that of a full

time bona fide employee working solely for the prospective contractor) as a basis for nondisclosure of contingent fee arrangements. The fact that a fee is for information does not exclude it from the definition of contingent fee.

(b) Contracting officers shall review each prospective contractor's offer or quotation and take the following actions:

(1) Ensure that the prospective contractor has completed both subparagraph (a)(1) and (a)(2) of the solicitation provision at 52.203-4, Contingent Fee Representation and Agreement.

(2) Consider failure to complete the representation a minor informality and afford the prospective contractor another opportunity to comply.

(3) If the prospective contractor still does not furnish the representation, reject the offer or quotation.

(4) If the prospective contractor answered subparagraphs (a)(1) and (a)(2) of the representation negatively, accept the representation, unless there is a reason to question its accuracy, and proceed with the contractual action.

(5) If the prospective contractor has answered subparagraph (a)(1) or (a)(2) affirmatively, secure a completed Standard Form 119, Statement of Contingent or Other Fees (see 53.301-119), or the statement authorized by the representation and agreement.

3.406 Award before receipt of the SF 119.

Contracting officers may award sealed bid contracts before receipt of the SF 119 or the statement. Negotiated contracts may not be awarded before receipt and evaluation of the SF 119 or statement, unless specifically approved by the chief of the contracting office.

3.407 Failure or refusal to furnish the SF 119.

If the prospective contractor fails or refuses to furnish the SF 119 or the statement in response to the contracting officer's request, the chief of the contracting office shall determine whether to make further efforts to secure the SF 119 or statement or to initiate appropriate actions under 3.409.

3.408 Evaluation of the SF 119.

3.408-1 Responsibilities.

(a) The contracting officer shall evaluate the SF 119 and all related information to determine—

(1) Whether a contingent fee arrangement exists between the prospective contractor and a person or company other than a full-time bona fide employee working solely for the prospective contractor; and

(2) When such a contingent fee arrangement does exist, whether it meets the statutory exception permit-

ting contingent fee arrangements with bona fide employees or agencies.

(b) The contracting officer's documentation of the evaluation, conclusion, and any proposed actions shall be reviewed at a level above the contracting officer in accordance with agency procedures.

3.408-2 Evaluation criteria.

(a) *Improper influence.* By definition (see 3.401), a bona fide employee or bona fide agency neither exerts nor proposes to exert improper influence to solicit or obtain Government contracts. If the contracting officer decides that there is a reasonable basis to conclude that improper influence has been or will be exerted or proposed, or that the employee or agency has held out as being able to obtain any Government contract or contracts through improper influence, the employee or agency shall not be considered bona fide.

(b) *Bona fide employee.* An employee may be bona fide but not work on a full-time basis solely for the contractor (e.g., small business concerns may need to employ persons who also represent other concerns). Prospective contractors must disclose such arrangements in the representation and agreement and submit the SF 119 or the statement. However, contingent compensation arrangements with bona fide employees, customary in the trade, are within the statutory exception and are not prohibited. In determining whether an employee is bona fide, the contracting officer shall—

(1) Compare the employment arrangement to the definition of bona fide employee in 3.401;

(2) Consider the criteria in subparagraphs (c)(1), (2), and (5) below, as appropriate; and

(3) Consider the continuity of employment. The employment must contemplate some continuity and not be solely for obtaining one or more specific Government contracts.

(c) *Bona fide agency.* The following guidelines are intended to help contracting officers determine whether an agency is a "bona fide agency," as defined in 3.401. They describe circumstances ordinarily existing in acceptable arrangements in which the agency is bona fide. However, the guidelines are not individually or collectively inviolable rules. The contracting officer must evaluate each arrangement in its totality, including attendant facts and circumstances.

(1) The fee should not be inequitable or exorbitant when compared to the services performed or to customary fees for similar services related to commercial business.

(2) The agency should have adequate knowledge of the contractor's products and business, as well as other qualifications necessary to sell the products or services on their merits.

(3) The contractor and the agency should have a continuing relationship or, in newly established relationships, should contemplate future continuity.

(4) The agency should be an established concern that has existed for a considerable period, or be a newly established going concern likely to continue in the future. The business of the agency should be conducted in the agency name and characterized by the customary indicia of the conduct of regular business.

(5) While an agency that confines its selling activities to Government contracts is not disqualified, the fact that an agency represents the contractor in Government and commercial sales should receive favorable consideration.

3.409 Misrepresentations or violations of the Covenant Against Contingent Fees.

(a) Government personnel who suspect or have evidence of attempted or actual exercise of improper influence, misrepresentation of a contingent fee arrangement, or other violation of the Covenant Against Contingent Fees shall report the matter promptly to the contracting officer or appropriate higher authority in accordance with agency procedures.

(b) When there is specific evidence or other reasonable basis to suspect one or more of the violations in paragraph (a) above, the chief of the contracting office shall review the facts and, if appropriate, take or direct one or more of the following, or other, actions:

- (1) If before award, reject the bid or proposal.
- (2) If after award, enforce the Government's right to annul the contract or to recover the fee.
- (3) Initiate suspension or debarment action under Subpart 9.4.
- (4) Refer suspected fraudulent or criminal matters to the Department of Justice, as prescribed in agency regulations.

3.410 Records.

For enforcement purposes, agencies shall preserve any representation and the original SF 119 or statement, together with all other pertinent data, including a record of actions taken. Contracting offices shall not retire or destroy these records until it is certain that they are no longer needed for enforcement purposes. If the original record is maintained in a central file, a copy must be retained in the contract file.

SUBPART 3.5—OTHER IMPROPER BUSINESS PRACTICES

3.501 Buying-in.

3.501-1 Definition.

"Buying-in" means submitting an offer below anticipated costs, expecting to—

(a) Increase the contract amount after award (e.g., through unnecessary or excessively priced change orders); or

(b) Receive follow-on contracts at artificially high prices to recover losses incurred on the buy-in contract.

3.501-2 General.

(a) Buying-in may decrease competition or result in poor contract performance. The contracting officer must take appropriate action to ensure buying-in losses are not recovered by the contractor through the pricing of (1) change orders or (2) follow-on contracts subject to cost analysis.

(b) The Government should minimize the opportunity for buying-in by seeking a price commitment covering as much of the entire program concerned as is practical by using—

(1) Multiyear contracting, with a requirement in the solicitation that a price be submitted only for the total multiyear quantity; or

(2) Priced options for additional quantities that, together with the firm contract quantity, equal the program requirements (see Subpart 17.2).

(c) Other safeguards are available to the contracting officer to preclude recovery of buying-in losses (e.g., amortization of nonrecurring costs (see 15.804-6(f)) and treatment of unreasonable price quotations (see 15.803(d)).

3.502 Subcontractor kickbacks.

3.502-1 Definitions.

"Kickback," as used in this section, means any money, fee, commission, credit, gift, gratuity, thing of value, or compensation of any kind which is provided, directly or indirectly, to any prime contractor, prime contractor employee, subcontractor, or subcontractor employee for the purpose of improperly obtaining or rewarding favorable treatment in connection with a prime contract or in connection with a subcontract relating to a prime contract.

"Person," as used in this section, means a corporation, partnership, business association of any kind, trust, joint-stock company, or individual.

"Prime contract," as used in this section, means a contract or contractual action entered into by the United States for the purpose of obtaining supplies, materials, equipment, or services of any kind.

"Prime Contractor," as used in this section, means a person who has entered into a prime contract with the United States.

"Prime Contractor employee," as used in this section, means any officer, partner, employee, or agent of a prime contractor.

"Subcontract," as used in this section, means a contract or contractual action entered into by a prime contractor or subcontractor for the purpose of obtaining supplies, materials, equipment, or services of any kind under a prime contract.

"Subcontractor," as used in this section, (a) means any person, other than the prime contractor, who offers to furnish or furnishes any supplies, materials, equipment, or services of any kind under a prime contract or a subcontract entered into in connection with such prime contract; and (b) includes any person who offers to furnish or furnishes general supplies to the prime contractor or a higher tier subcontractor.

3.502-2 General.

The Anti-Kickback Act of 1986 (41 U.S.C. 51-58) was passed to deter subcontractors from making payments and contractors from accepting payments for the purpose of improperly obtaining or rewarding favorable treatment in connection with a prime contract or a subcontract relating to a prime contract. The Act—

(a) Prohibits any person from—

(1) Providing, attempting to provide, or offering to provide any kickback;

(2) Soliciting, accepting, or attempting to accept any kickback; or

(3) Including, directly or indirectly, the amount of any kickback in the contract price charged by a subcontractor to a prime contractor or a higher tier subcontractor or in the contract price charged by a prime contractor to the United States.

(b) Imposes criminal penalties on any person who knowingly and willfully engages in the prohibited conduct addressed in paragraph (a) of this subsection.

(c) Provides for the recovery of civil penalties by the United States from any person who knowingly engages in such prohibited conduct and from any person whose employee, subcontractor, or subcontractor employee provides, accepts, or charges a kickback.

(d) Provides that—

(1) The contracting officer may offset the amount of a kickback against monies owed by the United States to the prime contractor under the prime contract to which such kickback relates;

(2) The contracting officer may direct a prime contractor to withhold from any sums owed to a subcontractor under a subcontract of the prime contract the amount of any kickback which was or may be offset against the prime contractor under subparagraph (d)(1) of this subsection; and

(3) An offset under subparagraph (d)(1) or a direction under subparagraph (d)(2) of this subsection is a claim by the Government for the purposes of the Contract Disputes Act of 1978.

(e) Authorizes contracting officers to order that sums withheld under subparagraph (d)(2) of this subsection be paid to the contracting agency, or if the sum has already been offset against the prime contractor, that it be retained by the prime contractor.

(f) Requires the prime contractor to notify the contract-

ing officer when the withholding under subparagraph (d)(2) of this subsection has been accomplished unless the amount withheld has been paid to the Government.

(g) Requires a prime contractor or subcontractor to report in writing to the inspector general of the contracting agency, the head of the contracting agency if the agency does not have an inspector general, or the Department of Justice any possible violation of the Act when the prime contractor or subcontractor has reasonable grounds to believe such violation may have occurred.

(h) Provides that, for the purpose of ascertaining whether there has been a violation of the Act with respect to any prime contract, the General Accounting Office and the inspector general of the contracting agency, or a representative of such contracting agency designated by the head of the agency if the agency does not have an inspector general, shall have access to and may inspect the facilities and audit the books and records, including any electronic data or records, of any prime contractor or subcontractor under a prime contract awarded by such agency.

(i) Requires each contracting agency to include in each prime contract a requirement that the prime contractor shall—

(1) Have in place and follow reasonable procedures designed to prevent and detect violations of the Act in its own operations and direct business relationships (e.g., company ethics rules prohibiting kickbacks by employees, agents, or subcontractors; education programs for new employees and subcontractors, explaining policies about kickbacks, related company procedures and the consequences of detection; procedures requiring subcontractors to certify they have not paid kickbacks; procurement procedures to minimize the opportunity for kickbacks; audit procedures designed to detect kickbacks; periodic surveys of subcontractors to elicit information about kickbacks; procedures to report kickbacks to law enforcement officials; annual declarations by employees of gifts or gratuities received from subcontractors; annual employee declarations that they have violated no company ethics rules; personnel practices that document unethical or illegal behavior and make such information available to prospective employers); and

(2) Cooperate fully with any Federal agency investigating a possible violation of the Act.

3.502-3 Contract clause.

The contracting officer shall insert the clause at 52.203-7, Anti-Kickback Procedures, in all solicitations and contracts.

3.503 Unreasonable restrictions on subcontractor sales.

3.503-1 Policy.

10 U.S.C. 2402 and 41 U.S.C. 253g require that subcontractors not be unreasonably precluded from making direct sales to the Government of any supplies or services made

the subcontractor under the contract (or any follow-on production contract); or

(2) otherwise act to restrict unreasonably the ability of a subcontractor to make sales to the United States described in clause (1).

(b) Rights under law

This section does not prohibit a contractor from asserting rights it otherwise has under law.

(June 30, 1949, c. 288, Title III, § 303G, formerly § 303H, as added Oct. 30, 1984, Pub.L. 98-577, Title II, § 206(a), 98 Stat. 3073, and renumbered § 303G, Nov. 8, 1985, Pub.L. 99-145, Title XIII, § 1304(c)(4)(A), 99 Stat. 742.)

HISTORICAL AND STATUTORY NOTES

Revision Notes and Legislative Reports
1984 Act. Senate Report No. 98-523, see 1984 U.S.Code Cong. and Adm.News, p. 5347.

1985 Act. House Report No. 99-81 and House Conference Report No. 99-235, see 1985 U.S.Code Cong. and Adm.News, p. 472.

Effective Dates

1984 Act. Section 206(b) of Pub.L. 98-577 provided that: "The amendment made by subsection (a) [enacting this section] shall apply with respect to solicitations made more than 180 days after the date of enactment of this Act [Oct. 30, 1984]."

WESTLAW ELECTRONIC RESEARCH

See WESTLAW guide following the Explanation pages of this volume.

§ 254. Contract requirements

(a) Contracts awarded using procedures other than sealed-bid procedures

Except as provided in subsection (b) of this section, contracts awarded after using procedures other than sealed-bid procedures may be of any type which in the opinion of the agency head will promote the best interests of the Government. Every contract awarded after using procedures other than sealed-bid procedures shall contain a suitable warranty, as determined by the agency head, by the contractor that no person or selling agency has been employed or retained to solicit or secure such contract upon an agreement or understanding for a commission, percentage, brokerage, or contingent fee, excepting bona fide employees or bona fide established commercial or selling agencies maintained by the contractor for the purpose of securing business, for the breach or violation of which warranty the Government shall have the right to annul such contract without liability or in its discretion to deduct from the contract price or consideration the full amount of such commission, percentage, brokerage, or contingent fee.

and to provide all that Government sought about expense of paying higher price, with question of whether irregularity in bid was minor and us subject to excuse being largely one of policy. *Wals American Industries, Inc. v. U.S., C.A.11 (Va.) 1989, 877 F.2d 883.*

4. Consideration of bids

Navy did not violate terms of its solicitation by awarding contract to construct nuclear-powered submarine on basis of price alone, read whole, solicitation and accompanying letter communicated message that industrial mobilization might be a factor in considering bids, that if it is a consideration it would take precedence over price, and that it would be considered, if at all, only if price was under \$780-million. *Newport News Shipbuilding and Dry Dock Co. v. General Dynamics Corp., C.A.4 (Va.) 1992, 960 F.2d 386.*

5. Rejection of bids

Unsuccessful bidder was not in any way prejudiced vis-a-vis successful bidder by Navy's schedule for submission of proposals for second phase competition for contract for hospital ship. *Prudential-Maryland Joint Venture Co. v. Lehman, D.C.D.C.1984, 590 F.Supp. 1390.*

6. Arbitrary and capricious awards

Contracting officer's determination that contractor was not responsible, and therefore unacceptable, was reasonable and not arbitrary or capricious; contractor sought to use debarred contractor as subcontractor for 100% of procurement methoscopes. *Medical Devices of Fall River, Inc. v. U.S., 1989, 19 C.I.O. 77.*

7. Modification

Where Department of Defense contracting officer clearly violated applicable procurement regulations in awarding contracts Department had aside for "small businesses" pursuant to the Small Business Act and the Armed Services Procurement Act, unsuccessful bidder would have received contracts but for such violation, successful bidder had not commenced performance of contracts in question, substitution of contractor could cause insignificant disruption of Government's procurements, and interests of public and use who bid for agency's work in agency's compliance with law outweighed higher price Government would have to pay for procurements, contracting officer would be required to award contracts to unsuccessful bidder. *Choctaw Mfg. Co. v. U.S., C.A.11 (Ala.) 1983, 761 F.2d 609.*

8. Validity

Award of contract to construct nuclear-powered submarine for Navy on basis of price alone violated Appropriations Act provision requiring contract be awarded pursuant to acquisition strategy of submarine program, where strategy required industrial mobilization award to provide for competition between two competing shipyards throughout life of submarine program. *Newport News Shipbuilding and Dry Dock Co. v. U.S. Dept. of Navy, E.D.Va.1991, 771 F.Supp. 739.*

General Accounting Office violated Armed Services Procurement Act when it awarded Army tank removal contract to competing bidder based on evaluation formula different from that in bid solicitation after determining that bids were im-

properly evaluated by including costs for returning land left uncovered by prior contractors. *Mark Dunning Industries, Inc. v. Cheney, M.D.Ala. 1989, 726 F.Supp. 810.*

There were no improper discussions between Navy and successful bidder that would have called for another round of "best and final offers," where modification which resulted from communications had no bearing on Navy's decision to award contract. *Prudential-Maryland Joint Venture Co. v. Lehman, D.C.D.C.1984, 590 F.Supp. 1390.*

28. Time for completing contracts

Navy did not violate regulation by not imposing fixed delivery date in request for proposal for contract for hospital ship. *Prudential-Maryland Joint Venture Co. v. Lehman, D.C.D.C.1984, 590 F.Supp. 1390.*

30. Jurisdiction

Contractor's claim challenging Army's termination of trash removal contract was a contractual dispute governed by jurisdictional provisions of Contract Disputes Act and Tucker Act, rather than claim of unsuccessful bidder under Arms Services Procurement Act, precluding district court from exercising jurisdiction over claim, to extent contractor sought to have termination of contract vacated. *Mark Dunning Industries, Inc. v. Cheney, M.D.Ala.1989, 726 F.Supp. 810.*

35. Persons entitled to maintain action

Subsec. (c) of this section which requires that contracts let under this chapter be awarded to the lowest responsible bidder and requiring the award of advertised government contracts to the responsible bidder whose bid conforms to the invitation are sufficient to place rejected bidder within zone of protection of this chapter so as to have standing to challenge award of bid to another. *B.K. Instrument, Inc. v. U.S., C.A.N.Y.1983, 715 F.2d 713.*

Interests of subcontractor, a nonbidder, were not within the zone of interests protected or regulated by the procurement statutes and therefore subcontractor, a manufacturer of a product which was allegedly excluded from consideration by terms of a subcontract specification in a bid solicitation issued by Navy, did not have standing to challenge the specification. *Rubber Millers, Inc. v. U.S., D.C.D.C.1984, 596 F.Supp. 210.*

48. Injunction

Evidence established that there had been de facto debarment of disappointed bidder under Department of Navy's invitation for bids; thus, awarding of subject contract would be enjoined pending debarment hearing and determinations thereon. *Leslie and Elliott Co., Inc. v. Garrett, D.D.C.1990, 732 F.Supp. 191.*

Offeror was entitled to injunctive relief in pro-award bid protest action, allowing offeror whose proposals were rejected because their demonstration model failed mandatory test to submit new demonstration models, where request for proposals did not indicate relative importance of characteristics involved and did not advise offerors that automatic exclusion would follow from test failure. *Isratex, Inc. v. U.S., C.I.O.1992, 25 C.I.O. 223.*

51. Resolicitation of bids

After it was determined that disappointed bidder on contract to construct nuclear-powered submarine for Navy was prejudiced by Navy's failure to follow previously determined competitive acquisition strategy or to adhere to factors set forth in terms of bid solicitation, proper remedy was to declare contract null and void and to order resolicitation of bids, rather than to award contract to disappointed bidder, where it could not be determined whether disappointed bidder would have received contract but for Navy's illegal actions. *Newport News Shipbuilding and Dry Dock Co. v. U.S. Dept. of Navy, E.D.Va.1991, 771 F.Supp. 739.*

§ 2305a. Renumbered § 2488

§ 2306. Kinds of contracts

(a) The cost-plus-a-percentage-of-cost system of contracting may not be used. Subject to the limitation in the preceding sentence, the other provisions of this section, and other applicable provisions of law, the head of an agency, in awarding contracts under this chapter after using procedures other than sealed-bid procedures, may enter into any kind of contract that he considers will promote the best interests of the United States.

(b) Each contract awarded under this chapter after using procedures other than sealed-bid procedures shall contain a warranty, determined to be suitable by the head of the agency, that the contractor has employed or retained no person or selling agency to solicit or obtain the contract under an understanding or agreement for a commission, percentage, brokerage, or contingent fee, except a bona fide employee or established commercial or selling agency maintained by him to obtain business. If a contractor breaks such a warranty the United States may annul the contract without liability or may deduct the commission, percentage, brokerage, or contingent fee from the contract price or consideration.

(c) No cost contract, cost-plus-a-fixed-fee contract, or incentive contract may be made under this chapter unless the head of the agency determines that such a contract is likely to be less costly to the United States than any other kind of

IRS DOCUMENTS

FINAL REGULATIONS ISSUED ON LOBBYING BY PUBLIC CHARITIES AND PRIVATE FOUNDATIONS.

(T.D. 8308)

(Section 501 - Tax Exempt Organizations)

LOBBYING BY PUBLIC CHARITIES; LOBBYING BY PRIVATE FOUNDATIONS

CC:EE-154-781 (4830-01)

Br5:JPWalshSkelly/PGAccettura
(Final draft of June 29, 1990)DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1, 7, 20, 25, 53, 56 and 602

RIN 1545-AE02

Treasury Decision 8308

AGENCY: Internal Revenue Service, Treasury

ACTION: Final regulations

SUMMARY: This document contains final regulations about lobbying expenditures by certain tax-exempt public charities and by private foundations. Changes to the tax laws governing lobbying by public charities were made by the Tax Reform Act of 1976 (the "Act"). These regulations will provide organizations the guidance needed to comply with the Act, and will affect public charities electing the expenditure test under section 501(h) of the Internal Revenue Code of 1986 ("electing public charities"). These regulations will also provide organizations with clearer guidance needed to comply with the requirements of section 4945 (relating to lobbying expenditures by private foundations). Finally, in light of the unique charitable and educational purposes shared by all organizations described in section 501(c)(3), as well as the similarity of the statutory schemes governing lobbying by private foundations and by electing public charities, the regulations ensure that the rules regarding lobbying by private foundations are consistent with the rules regarding lobbying by electing public charities. However, these regulations do not apply to lobbying by ineligible or nonelecting public charities, which continue to be covered by the "substantial part" test regarding lobbying activities. Nor does any portion of these regulations apply to section 162(e), which allows a business expense deduction for certain lobbying expenses but disallows any deduction for certain others.

DATES: The regulations are effective for taxable years beginning after August 31, 1990.

FOR FURTHER INFORMATION CONTACT: Jerome P. Walsh Skelly, 202-535-3818 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

PAPERWORK REDUCTION ACT

The collections of information contained in this final regulation have been reviewed and approved by the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act (44 U.S.C. 3504(h)) under control number 1545-0052. The estimated annual burden per respondent varies from 1/4 hour to 10

3/4 hours, depending on individual circumstances, with an estimated average of 2 1/2 hours. The estimated average annual burden per recordkeeper is 4 hours.

These estimates are an approximation of the average time expected to be necessary for the collection of information. They are based on such information as is available to the Internal Revenue Service. Individual respondents/recordkeepers may require greater or less time, depending on their particular circumstances.

Comments concerning the accuracy of these burden estimates and suggestions for reducing the burden should be directed to the Internal Revenue Service, Attn: IRS Reports Clearance Officer T:FP, Washington, D.C. 20224, and to the Office of Management and Budget, Attn: Desk officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, D.C. 20503.

OUTLINE OF IMPORTANT PORTIONS OF THIS TREASURY DECISION:

I. PREAMBLE

- A. Prior Law
- B. Summary of Expenditure Test
- C. Background on Procedural History
- D. Summary of Comments on the Three NPRMs and Explanation of Provisions in Final Regulations (including 20 separate items and a Question and Answer overview)

II. AMENDMENTS TO THE REGULATIONS

- A. Deduction for charitable gifts to organizations that lobby (Sections 170, 2055, 2522)
- B. Effect of lobbying on qualification as a tax-exempt organization (Sections 501(c) and 504)
- C. Application of "expenditure test" limits to lobbying by electing public charities (Section 501(h))
- D. Excise tax on private foundations' lobbying expenditures (Section 4945)
- E. Excise tax on electing public charities' excess lobbying expenditures, including important definitions (Section 4911)

PRIOR LAW

An organization will lose its tax exempt status under section 501(c)(3) if a substantial part of its activities is lobbying. This is known as the "substantial part test." Before the Tax Reform Act of 1976, there was uncertainty about what constituted a "substantial part" of an organization's activities. Congress was aware both of the severity of loss of tax exemption as a sanction and of the belief that the vague standards of the substantial part test tended to create uncertainty and allow subjective and selective enforcement. (Subsequent to the Tax Reform Act of 1976, in the Omnibus Budget Reconciliation Act of 1987, Congress enacted section 4912. That section imposes an excise tax on the lobbying expenditures of public charities, other than churches and certain church affiliated

organizations, whose tax exempt status is revoked for violating the "substantial part test.")

EXPENDITURE TEST

Because of its concerns about the "substantial part test," Congress enacted, in 1976, an alternative to the substantial part test. Under sections 501(h) and 4911, which were added by section 1307 of the Tax Reform Act of 1976, certain publicly supported section 501(c)(3) organizations may elect to spend up to a certain (declining) percentage of their "exempt purpose expenditures" to influence legislation without incurring tax or losing qualification for tax-exempt status. Thus, if an eligible organization elects the "expenditure test" of sections 501(h) and 4911, specific statutory dollar limits on the organization's lobbying expenditures apply. Under the expenditure test, there are limits both upon the amount of the organization's grass roots lobbying expenditures and upon the total amount of the organization's direct and grass roots lobbying expenditures. In contrast to the substantial part test, the expenditure test imposes no limit on lobbying activities that do not require expenditures, such as certain unreimbursed lobbying activities conducted by bona fide volunteers. In general, if either or both of the expenditure test limits are exceeded, section 4911 imposes a 25 percent excise tax upon the greater of: (1) the amount by which the organization's grass roots lobbying expenditures exceed its grass roots lobbying limit, or (2) the amount by which an organization's total direct and grass roots lobbying expenditures exceed its total lobbying limit. Additionally, if an organization's grass roots expenditures or total lobbying expenditures normally exceed 150 percent of the applicable limitation on its lobbying expenditures, the organization will cease to be described in section 501(c)(3), and, therefore, will no longer be exempt from income tax or be eligible to receive tax deductible charitable contributions.

For more information about the expenditure test and related issues, see item 20, Simplified Summaries, near the end of this Preamble. That item provides an easy to understand overview, in Question and Answer format, of the laws governing certain tax-exempt organizations' lobbying and political activities and expenditures.

BACKGROUND

On November 25, 1980, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under sections 162, 6001, and 6033 of the Internal Revenue Code of 1954 (relating to grass roots lobbying expenditures by business corporations) and to the regulations on Foundation and Similar Excise Taxes (26 CFR Part 53) under section 4945 of the Internal Revenue Code of 1954 (relating to lobbying expenditures by private foundations) (45 FR 78167) ("the 1980 NPRM").

On November 5, 1986, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1), Temporary Income Tax Regulations under the Tax Reform Act of 1976 (26 CFR Part 7), Estate Tax Regulations (26 CFR Part 20), Gift Tax Regulations (26 CFR Part 25), and Foundation and Similar Excise Taxes (26 CFR Part 53), and also proposed regulations on Public Charity Excise Taxes (26 CFR Part 56), under sections 170, 501(c)(3), 501(c)(4), 501(h), 504, 2055, 2522, 4911, 4945, 6001, 6011, and 6033 of the Internal Revenue Code of 1954 (51 FR 40211) ("the 1986 NPRM").

On December 23, 1988, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1), Foundation and Similar Excise Taxes (26

CFR Part 53), and also proposed regulations on Public Charity Excise Taxes (26 CFR Part 56) ("the 1988 NPRM").

The 1988 NPRM superseded that portion of the 1980 NPRM that proposed amendments to the regulations under section 4945 of the Internal Revenue Code (relating to lobbying expenditures by private foundations). The 1988 NPRM also substantially revised certain parts of the 1986 NPRM relating to proposed regulations on Public Charity Excise Taxes (26 CFR Part 56) under section 4911 of the Internal Revenue Code. The 1988 NPRM also revised portions of the 1986 NPRM that proposed amendments to the regulations under sections 501(h) and 4945.

The 1988 NPRM contained major modifications of the 1986 NPRM definitions, including the definition of grass roots lobbying. Under the changes made in the 1988 NPRM, far fewer communications by public charities that elect the expenditure test will be considered lobbying than would have been the case under the 1986 NPRM. The 1988 NPRM also modified the definitions contained in the regulations under section 4945 (relating to lobbying by private foundations) to make them consistent with the definitions for public charities that elect the expenditure test.

PUBLIC COMMENTS ON THE THREE NOTICES OF PROPOSED RULEMAKING

More than 10,000 written comments were received concerning the 1986 NPRM. Numerous written comments were also received concerning the 1980 NPRM. In addition, on May 11 and 12, 1987, the Internal Revenue Service ("Service") held public hearings concerning the 1986 NPRM.

The numerous public comments and the two days of public hearings were helpful in formulating the 1988 NPRM. In addition, possible revisions to the controversial sections of the 1986 NPRM were discussed at length with the Commissioner's Exempt Organizations Advisory Group (comprised of legal and other representatives of exempt organizations as well as academics) at public meetings held on September 17, 1987, and February 26, 1988.

The 1988 NPRM resulted from a careful balancing of the statutory mandate limiting the amount of lobbying expenditures by section 501(c)(3) organizations with the expressed desire of the affected organizations and individuals to involve themselves in the public policymaking process to the greatest extent consistent with that statutory mandate. As a result, the 1988 NPRM made extensive changes to the 1980 NPRM and the 1986 NPRM in an effort to achieve this difficult balance. For example, the 1988 NPRM contains a definition of grass roots lobbying that is less inclusive than is permitted by the broad statutory language defining grass roots lobbying.

The 1988 NPRM resulted in fewer than 100 written comments from the public (as opposed to the more than 10,000 written public comments resulting from the 1986 NPRM). The 1988 NPRM was discussed with the Commissioner's Exempt Organizations Advisory Group at a public meeting held on January 10, 1989. A formal public hearing on the 1988 NPRM, with six speakers, was held on April 3, 1989.

**SUMMARY OF COMMENTS RECEIVED ON THE
1988 NOTICE OF PROPOSED RULEMAKING AND
EXPLANATION OF PROVISIONS**

**1. THE GENERAL DEFINITION OF "GRASS ROOTS
LOBBYING"**

The most significant revision of the 1986 NPRM in the 1988 NPRM was in the general definition of grass roots lobbying. The 1988 NPRM provides that, with limited exceptions, a communication is grass roots lobbying only if it:

- 1) refers to specific legislation;
- 2) reflects a view on such legislation; AND
- 3) encourages the recipient of the communication to take action with respect to such legislation.

Most of the comments generally praised this revision, although, as described in more detail below, the comments also requested additional changes in and explanations of the terms "specific legislation," "refers to," "reflects a view" and "encourages . . . action."

Even though this general definition is very lenient and will permit many clear advocacy communications to be treated as NONlobbying, the final regulations retain the general definition in substantially unchanged form. This is part of the Service's attempt to maintain a careful balance between the statutory limits on electing public charities' lobbying expenditures and the desire of those organizations to involve themselves in the public policymaking process to the greatest extent consistent with those statutory limits.

2. DEFINITION OF "SPECIFIC LEGISLATION"

The 1988 NPRM provides that a communication is generally not considered lobbying unless it refers to specific legislation and reflects a view on that legislation. The term "specific legislation" is defined as including both legislation that has already been introduced and a specific legislative proposal that the organization either supports or opposes. Several examples in the 1988 NPRM further illustrate the meaning of the term "specific legislation" in particular fact situations.

A number of comments considered the term "specific legislation" to be vague. Also, several comments objected to the removal of certain language from the private foundation regulations. That language provided that lobbying includes attempts to influence legislation "to be submitted imminently to" a legislative body.

Deletion of the term "imminently" is justified because the term implies that a temporal standard determines whether or not an un-introduced legislative proposal is "specific legislation" that can be influenced. Given the nature of the legislative process, a temporal standard is inappropriate and underinclusive. For example, numerous specific legislative proposals are subject to extensive scrutiny, debate and controversy long before they are formally introduced as a bill. Moreover, effective lobbying could prevent a bill from ever being introduced. Therefore, the final regulations do not reintroduce the "to be submitted imminently" standard into the definition of "specific legislation".

In response to the comments regarding the vagueness of the definition of "specific legislation," the final regulations include additional examples. Like several examples already in the 1988 NPRM, these new examples further illustrate the scope of the term "specific legislation".

3. DEFINITION OF "LEGISLATION"

One comment expressed concern about the scope of the statutory and regulatory definition of "legislation." Under both the statute and the proposed regulations, the term "legislation" includes "Acts, bills, resolutions, or similar items." The final regulations do not further expand on this language, except to include examples showing that the Senate's confirmation vote on Executive branch nominees is a vote on "legislation." This position is consistent with a published Service position, Notice 88-76, 1988-2 C.B. 392.

**4. DEFINITION OF "REFERS TO" AND "REFLECTS A
VIEW"**

Under the 1988 NPRM, a communication is generally not a lobbying communication unless it refers to specific legislation and reflects a view on that specific legislation. A few comments requested more detail in defining the terms "refers to" and "reflects a view." The final regulations do not further define these terms. However, a number of the examples contained in the final regulations illustrate both terms.

**5. DEFINITION OF "ENCOURAGES RECIPIENT TO
TAKE ACTION"**

Under the 1988 NPRM, a communication is generally not a grass roots lobbying communication unless (in addition to referring to specific legislation and reflecting a view on that legislation) it encourages recipients to take action with respect to the specific legislation. The 1988 NPRM states that a communication encourages a recipient to take action when it: 1) states that the recipient should contact legislators; 2) states a legislator's address, phone number, etc; 3) provides a petition, tear-off postcard or similar material for the recipient to send to a legislator; or 4) specifically identifies one or more legislators who will vote on legislation as: opposing the communication's view on the legislation, being undecided about the legislation, being the recipient's representative in the legislature, or being a member of the legislative committee that will consider the legislation. Further, a communication with the fourth type of encouragement to take action is grass roots lobbying only if, in addition to referring to and reflecting a view on specific legislation, it is a partisan communication that can not meet the "full and fair exposition" test as nonpartisan analysis, study or research.

Some comments argued that the fourth type of encouragement to a recipient to take action was too indirect and overinclusive. One comment contended that there should be a de minimis exception that would examine the communication as a whole.

The final regulations do not substantially modify the 1988 NPRM definition of "encouraging recipients to take action." Under the standard contained in the final regulations, clear advocacy of specific legislation is not grass roots lobbying at all unless it contains an encouragement to action. Further, if an advocacy communication contains only the fourth type of encouragement to action, the communication is not grass roots lobbying unless it is partisan. The Service believes this standard, holding that certain communications that clearly advocate or oppose specific legislation are not grass roots lobbying, is very lenient. Therefore, the Service believes that any further changes would only serve to deplete a standard that already allows numerous clear advocacy communications to be treated as NONlobbying.

6. SUBSEQUENT USE OF NONLOBBYING MATERIAL

The 1988 NPRM provides that expenses incurred for nonlobbying materials or communications may, in certain circumstances, be characterized as lobbying expenditures where those materials or communications are subsequently used in a lobbying effort. Under the 1988 NPRM, this occurs only if the primary purpose of the organization in preparing the materials or communication was for use in lobbying. If the later lobbying use is by an organization that is not related to the organization that prepared the material, the organization preparing the materials will be charged with lobbying expenditures only if there is clear and convincing evidence of a lobbying purpose on the part of the preparing organization.

The 1988 NPRM provides a "safe harbor" for organizations concerned about the rule. The "safe harbor" provides that if the materials or communications are substantially distributed in a nonlobbying form prior to, or contemporaneously with, the lobbying use, the organization preparing the materials is not charged with a lobbying expenditure for the preparation of the materials or communications, regardless of later lobbying use of the materials by the preparing organization or any other organization.

Several comments stated that the clear and convincing standard for lobbying use by an unrelated organization should require conscious cooperation or collusion between the two organizations involved. Other comments objected that the subsequent use rule applies for an indefinite time period after materials are prepared. Some comments requested a safe harbor for raw, unpublished research data. Finally, several comments requested clarification of whether, for purposes of the safe harbor, the term "substantial distribution" is tested against the normal pattern of distribution of the preparing organization itself or of similar organizations.

In drafting the subsequent use rules in the 1988 NPRM, the Service attempted to meet two principal goals. The first goal was to limit potential abuses, such as where a charity creates a "nonlobbying" document advocating or opposing specific legislation, treats the preparation costs as nonlobbying, and then immediately adds an encouragement for the recipients to take action. The Service's second goal was to limit the anti-abuse rules in order to avoid treating as lobbying any research and preparation costs that were not intended to assist in lobbying efforts.

The final regulations restructure the subsequent use rule to make it easier to understand and apply. The final regulations clarify the scope of the clear and convincing evidence standard by specifying that for that standard to be met there must be evidence of cooperation or collusion between two unrelated organizations. The final regulations also clarify that the "safe harbor" distribution is tested against the normal pattern of distribution by that and similar organizations. Further, the final regulations set a time limit on the application of the subsequent use rule: if nonlobbying material is used in a lobbying campaign, the subsequent use rule applies only to expenditures paid less than six months before the first use of the nonlobbying material in the lobbying campaign.

7. NONPARTISAN ANALYSIS, STUDY OR RESEARCH

Under the statute and the 1988 NPRM, nonpartisan analysis, study or research is not lobbying. The 1988 NPRM clarifies (both for private foundations and electing public charities) that a communication that reflects a view

on specific legislation is not nonpartisan analysis, study or research if it DIRECTLY encourages the recipients to take action with respect to legislation. The 1988 NPRM provides that the term "directly encourages" includes the first three of the four methods of encouraging recipients to take action. (Those four methods are set forth in the general grass roots lobbying definition and are also listed in item 5 of this Preamble). Therefore, under the 1988 NPRM, a communication can be nonpartisan analysis, study or research even if it reflects a view on specific legislation and includes the fourth method of encouraging a recipient to action, so long as it does not include any of the first three methods of encouragement.

Several comments contended that even when a communication DIRECTLY encourages recipients to take action, the communication may be nonpartisan analysis, study or research if the direct encouragement is incidental to the nonpartisan nature of the document.

The final regulations do not modify the 1988 NPRM on this point. The Service believes that any further loosening of the standard is not appropriate because this rule does not even come into consideration unless the communication refers to and reflects a view on specific legislation.

8. REBUTTABLE PRESUMPTION FOR MASS MEDIA COMMUNICATIONS TWO WEEKS BEFORE A LEGISLATIVE VOTE ON HIGHLY PUBLICIZED LEGISLATION

The 1988 NPRM provides a special rule for a limited number of communications in the mass media. The mass media rule in the 1988 NPRM is a rebuttable presumption that a mass media communication is grass roots lobbying if it: 1) is made within two weeks before a vote by a legislative body, or committee thereof, on highly publicized legislation; 2) reflects a view on the general subject of that legislation; and 3) either refers to the legislation or encourages the public to communicate with legislators on the general subject of the legislation. The presumption is rebutted either by showing that the charity regularly makes similar mass media communications without regard to the timing of legislation or that the communication's timing was unrelated to the upcoming vote.

The mass media rule in the 1988 NPRM was intended to deal with situations where a clear encouragement for the recipients to take action is not necessary in order for the communication to influence the public to contact legislators. The Service believes that such a situation exists where a communication contains the above-described elements and is made in the mass media within two weeks before a legislative vote on highly publicized legislation. In these situations, the Service believes recipients are sufficiently aware of the legislation to not require a specific encouragement to action.

Numerous comments were received about this rebuttable presumption for certain mass media communications. Many comments objected to the two week rule. They claimed that organizations could never be sure when a communication would come under the rule since the timing of legislative votes is never certain.

The final regulations do not modify the two week rule. The Service notes that this rule can also favor charities. For example, if a vote is delayed or cancelled, the communication would not fall within the rule even if the organization fully expected that there would be a vote within two weeks of its mass media communication. This is clearly illustrated by new examples in the final regulations.

In considering charities' concerns about the two week rule, the Service considered whether the mass media presumption should apply whenever the legislation is highly publicized during the two weeks BEFORE THE ADVERTISEMENT IS PLACED. Under such a rule, a charity would know at the time it places an advertisement whether or not the mass media presumption applies.

The Service rejected this idea because such a rule would be even stricter than the 1988 NPRM. Because a given bill may be highly publicized for extended periods even in the absence of any legislative votes, such a rule could mean that all mass media communications on the general subject of that bill would be presumed grass roots lobbying (if the communication either mentions the bill or urges contact with legislators).

The Service believes that the two week rule as proposed in the 1988 NPRM strikes a reasonable balance. It focuses only on the time period when abuses are most likely to occur: when a legislative vote occurs shortly after the communication.

Several comments objected that the rule could include news reports in the mass media about an organization's lobbying. In response to these comments, the final regulations limit the rule to paid advertisements in the mass media as well as a very limited number of communications made by a charity in its own large scale mass media publication or broadcast.

A few comments noted critically that the 1988 NPRM does not apply the mass media presumption to large-scale direct mailings. Some comments said that this is unfair to charities that do not have large mailing lists. Other comments criticized this as a loophole for charities that do have large mailing lists. The final regulations do not apply the presumption to large-scale direct mailings. If significant abuses develop involving these direct mailings, the Service will consider proposing changes to the final regulations.

Several comments requested additional specificity on the meaning of the terms "highly publicized" and "general subject of the legislation." The scope of the former term is narrowed somewhat by the final regulations, and the 1988 NPRM's examples illustrating that term are retained. The final regulations do not significantly define the latter term beyond the 1988 NPRM's examples illustrating the term. The final regulations do not adopt a suggestion that the mass media presumption arises only where the mass media communication in question refers to specific legislation. Nor do the final regulations adopt a suggestion that the legislative vote, rather than the legislation, must be highly publicized in order for the mass media presumption to apply, but the final regulations do adopt a suggestion that subcommittee votes not be considered legislative votes for purposes of the mass media rule. Finally, in response to comments, changes were made in various examples illustrating the mass media rule.

The final regulations largely retain the 1988 NPRM's rebuttable presumption without substantial changes, although various technical revisions have been made. The Service believes that this rebuttable, and narrowly crafted, presumption provides an important bright line test for a very limited number of high profile communications for a very limited period of time. Any further narrowing of this rule could essentially eliminate the presumption.

9. REFERENDA AND BALLOT INITIATIVES

The 1988 NPRM includes several examples illustrating that an attempt to influence the outcome of a voter referendum or voter initiative is grass roots lobbying.

Many comments argued that expenditures to influence referenda and ballot initiatives should be considered direct lobbying expenditures rather than grass roots lobbying expenditures. Under the regulations, a communication is direct lobbying if and only if it is a communication with a legislator (or with certain other government officials) that both refers to and reflects a view on specific legislation. The comments contended that the voting public acts as the legislature with respect to a referendum or ballot initiative. Several comments also noted that, read literally, the 1988 NPRM's four categories of encouraging recipients to take action do not apply to attempts to influence referenda and ballot initiatives.

The final regulations provide that expenditures for attempts to influence referenda and ballot initiatives are considered direct lobbying expenditures. However, these final regulations do not modify the definition of direct lobbying (which requires that a communication with legislators refer to and reflect a view on specific legislation). Therefore, communications on referenda and ballot initiatives will be considered direct lobbying if they refer to and reflect a view on specific legislation, without the requirement (found in the definition of grass roots lobbying) for an encouragement to action.

There is no requirement for an encouragement to action in the definition of direct lobbying because direct lobbying communications are directed to legislators themselves, whereas grass roots lobbying communications are not directed at legislators and, to be most effective at influencing legislation, must generally encourage their recipients to contact legislators. Where the general public is the legislature, a communication directed to any member of the general public is directed to a legislator. Accordingly, in such a situation, a communication that refers to and reflects a view on specific legislation is designed to influence that recipient/legislator's vote, without regard to whether it encourages the recipient/legislator to contact others.

The final regulations also provide rules on when a referendum or ballot initiative is considered "specific legislation."

10. ALLOCATION RULES

The 1988 NPRM has two different allocation rules for communications that have both a lobbying and a bona fide nonlobbying purpose. One allocation rule simply requires a "reasonable allocation." That rule applies to an electing public charity's communications with its bona fide members.

The second allocation rule in the 1988 NPRM is for nonmembership communications. Where a nonmembership lobbying communication also has a bona fide nonlobbying purpose, the 1988 NPRM provides that an organization must include as lobbying expenditures all costs attributable to those parts of the communication that are on the same specific subject as the lobbying message. In general, the 1988 NPRM provides that part of the communication is on the "same specific subject" if it:

- * * * discusses an activity or specific issue that would be directly affected by the proposed legislation that is the subject of the lobbying message. Moreover, discussion of the background or consequences of the proposed legislation, or discussion of the background or consequences of an activity or specific issue affected by the proposed legislation, is also considered to be on the same specific subject.

Many comments urged that the scope of the term "same specific subject" be narrowed and also be further defined. Some comments urged that the "same specific subject" rule be replaced with a "reasonable allocation" rule for all lobbying communications that also have a bona fide nonlobbying purpose.

The final regulations do not modify the "same specific subject" rule, but they do add an example further illustrating the scope of the rule. The Service believes this allocation rule is necessary in light of the lenient definition of grass roots lobbying. A weakening of the allocation rule, in combination with the final regulations' lenient definition of grass roots lobbying, could virtually eliminate the statutory limitation on an electing public charity's lobbying expenditures.

11. TRANSFERS TO NONCHARITIES THAT LOBBY

The 1988 NPRM provides that transfers by an electing public charity to a noncharity that lobbies will, in certain circumstances, be a grass roots or direct lobbying expenditure by the electing public charity even if the transfer is not earmarked for lobbying. However, a transfer to a noncharity is not treated as a lobbying expenditure if the transfer is a controlled grant (the charity limits the transfer to a nonlobbying specific project of the noncharity and maintains records on the grant's use).

Most comments expressed concern about the scope of the term "transfer." That term was not defined in the 1988 NPRM. The comments expressed particular concern about whether the rule included transfers for fair market value.

The final regulations clarify and limit the meaning of the term "transfer" to situations where the charity receives less than fair market value in return for the transfer. Also, the final regulations do not apply the transfer rule if the transfer is made for less than fair market value and a significant number of members of the general public receive goods or services from the charity at the same favorable (less than fair market value) price.

12. THE PRODUCTION OF INCOME AS "EXEMPT PURPOSE EXPENDITURES"

The 1988 NPRM provides that costs for the production of income are not exempt purpose expenditures and, therefore, are not included in the base of expenditures on which the amount of permissible lobbying expenditures is calculated.

Several comments requested that the final regulations clarify that expenses for a substantially related trade or business are included as exempt purpose expenditures. Another comment requested that expenditures to manage an endowment be considered exempt purpose expenditures.

The final regulations clarify that expenditures are not exempt purpose expenditures if they are for a purpose or activity that is not substantially related (aside from the need of the organization for income or funds or the use it makes of the profits derived) to the organization's charitable, educational or other purpose that is the basis for the organization's exemption under section 501(c)(3). The final regulations also clarify that the costs of managing an endowment are not included as exempt purpose expenditures since they are incurred for the production of income.

13. FUNDRAISING COSTS

Under section 4911, amounts paid to or incurred for a separate fundraising unit are not exempt purpose

expenditures. The 1988 NPRM defines the meaning of the term "separate fundraising unit."

Several comments requested guidance on whether postage and related costs paid directly by a charity for a fundraising communication prepared by a separate fundraising unit are costs that are incurred for a separate fundraising unit.

The final regulations clarify that amounts incurred for the creation, production, copying, and distribution of a separate fundraising unit's fundraising communication are amounts paid to or incurred for a separate fundraising unit, regardless of whether the charity pays some of the costs directly rather than through the separate fundraising unit.

14. AFFILIATION RULES

The 1988 NPRM did not change the extensive affiliation rules that were contained in the 1986 NPRM. These rules implement section 4911(f).

Several comments requested the deletion of the 1986 NPRM's provision that two organizations can be affiliated on the basis of an "implication" in one organization's governing instrument that that organization is bound by the other organization's legislative positions. Two comments requested that the regulations require affiliation only among section 501(c)(3) organizations and not include non-section 501(c)(3) organizations as members of an affiliated group.

The final regulations eliminate "implication" in a governing instrument as a test for whether two organizations are affiliated. The final regulations retain the position that, in determining whether two section 501(c)(3) organizations are affiliated, non-section 501(c)(3) affiliations will be considered. The Service believes that where two section 501(c)(3) organizations are not affiliated with each other, but are both affiliated with a section 501(c)(4) organization, the two section 501(c)(3) organizations are members of an affiliated group for purposes of section 4911. However, in the actual calculation of the expenditure test, only those members of the affiliated group that have elected are considered.

15. REQUESTS FOR TECHNICAL ADVICE

The 1988 NPRM did not revise the 1986 NPRM provision that an organization is not lobbying if it testifies or presents written testimony to a legislative body or committee in response to a written request from that body or committee for technical advice.

One comment requested the elimination of the requirement that the request for technical advice be in writing. The comment also requested that the technical advice exception apply even if the request for technical advice is from an individual legislator or government official, as opposed to a legislative body or committee.

The final regulations do not substantially modify the technical advice exception. The Service believes that the requirements that the request be both in writing and from a legislative body or committee are clear statutory requirements. The Service is unable to discern any legislative intent for additional flexibility with respect to the technical advice exception.

16. SELF-DEFENSE EXCEPTION

The 1988 NPRM did not revise the 1986 NPRM provision that certain self-defense lobbying by an electing public charity is not treated as lobbying. One comment requested that this exception be revised to exclude from lobbying any lobbying by a section 501(c)(3) organization

on issues affecting that organization's section 501(c)(3) members, even if not all members of the organization are section 501(c)(3) organizations. With certain restrictions, the final regulations do generally adopt this suggestion.

17. FAIRNESS DOCTRINE

The 1986 and 1988 NPRMs included in the nonpartisan analysis, study or research exception a reference to the Fairness Doctrine. This reference first appeared in that exception as that exception was published in the regulations under section 4945.

Two comments requested that the reference to the Fairness Doctrine be deleted from the final regulations in light of uncertainty about the status of that doctrine. The comments stated that the application of the Fairness Doctrine is a matter best dealt with directly through Federal communications law and that it is inappropriate for the Fairness Doctrine to be applied indirectly through the tax law.

The final regulations delete references to the Fairness Doctrine from both the proposed regulations and the existing section 4945 regulations.

18. CONFORMING AMENDMENTS

The final regulations amend the regulations under sections 1.170A-1(h)(5)(ii), 20.2055-1(a)(2) and 25.2522(a)-1(a)(2) by inserting the words "or in opposition to" after the words "any political campaign on behalf of". This change is a technical amendment so that each of these regulations conforms to its respective statute as well as to section 501(c)(3) as amended by the Omnibus Budget Reconciliation Act of 1987.

19. MISCELLANEOUS AND TECHNICAL COMMENTS

The final regulations also contain a number of technical revisions. Most of these changes are being made in response to public comments.

20. SIMPLIFIED SUMMARIES

Each major section of the regulations is preceded by a brief and simple summary of the rules in that section. Also, the following 17 Questions and Answers should be of particular help to readers. These Q&As provide an easy to understand overview of the laws governing certain tax-exempt organizations' lobbying and political activities and expenditures. The Service hopes the Q&As and the final regulations' brief summaries will help readers more easily use the regulations.

The Q&As do not impose additional requirements or rules, nor do they amend or affect the text of the regulations. The Q&As are intended only to be a simple guide to understanding the regulations and should not be used as a substitute for reading the regulations. If there is any conflict between the Q&As and the text of the regulations, the text of the regulations controls. The chart that immediately precedes the questions and answers is designed to help illustrate the answers to some of the Q&As.

CHARITIES (SECTION 501(c)(3) ORGANIZATIONS)			
PUBLIC CHARITIES		PRIVATE FOUNDATIONS	
ELECTING	NON-ELECTING	ELECTING	NON-ELECTING

LOBBYING	YES, may lobby freely so long as lobbying expenses are within specified limits (LIM)	YES, may lobby freely so long as lobbying is not a substantial part of the organization's activities ("SUB-TEST") -- sections 501(h) and 4911.	NO, lobbying expenditures are subject to a potentially severe excise tax -- section 501(c)(3) tax -- section 4945.
INTERVENTION IN POLITICAL CAMPAIGN FOR ELECTIVE PUBLIC OFFICE	NO, intervening in a political campaign will cause loss of tax-exempt status and may also give rise to excise or other taxes -- section 501(c)(3), section 527(f), section 4945 (private foundations only), and section 4955. 24/		

TABLE CONTINUED
CERTAIN NONCHARITIES
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- Section 501(c)(4) Social Welfare Organizations.
- Section 501(c)(5) Labor Unions and
- Section 501(c)(6) Professional Societies.

LOBBYING	YES, may generally lobby in unlimited amounts as long as the lobbying is in furtherance of the noncharity's exempt purposes. 24/
INTERVENTION IN POLITICAL CAMPAIGN FOR ELECTIVE PUBLIC OFFICE	YES, does 24/ 1) the noncharity's primary purpose and/or activities may not be political campaign intervention; and 2) the noncharity may be subject to tax under section 527(f) unless it maintains a separate segregated fund (essentially, a PAC).

FOOTNOTES TO TABLE

- 24/ The section 501(h) lobbying expenditure limit and the section 4911 tax on excess lobbying expenditures apply.
- 25/ The section 501(h) lobbying expenditure limit and the section 4911 tax on excess lobbying expenditures do NOT apply. "If, however, a substantial part of the public charity's activities is lobbying, the public charity will lose both its tax-exempt status under section 501(c)(3) and its ability to receive tax-deductible charitable contributions. Also, public charities (other than churches) and their managers (in certain cases) are subject to an excise tax under section 4912 on the lobbying expenditures.
- 26/ The section 501(b) lobbying expenditure limit and the section 4911 tax on excess lobbying expenditures do NOT apply. However, section 4945 imposes a tax on ANY lobbying expenditure by a private foundation. Many definitions in the section 4911 regulations apply.
- 27/ The section 501(h) lobbying expenditure limit and the section 4911 tax on excess lobbying expenditures do NOT apply.

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Q-1: DOES THE TAX UNDER SECTION 4911 APPLY TO ALL TAX EXEMPT ORGANIZATIONS?

A-1: No, the section 4911 tax does not apply to ALL tax exempt organizations; it applies only to CERTAIN organizations that are described in section 501(c)(3). Section 501(c)(3), generally speaking, describes charitable, educational and religious organizations. Therefore, for example, the tax does not apply to such tax exempt organizations as social welfare organizations (section 501(c)(4)), labor unions (section 501(c)(5)), or business

leagues, chambers of commerce, or trade associations (section 501(c)(6)).

Q-2: TO WHICH ORGANIZATIONS DESCRIBED IN SECTION 501(c)(3) DOES THE SECTION 4911 TAX APPLY?

A-2: There are two kinds of section 501(c)(3) organizations: private foundations and public charities. (Private foundations generally are funded by a small number of individuals or corporations while public charities are generally funded by contributions from the general public and payments for services (see section 509(a)). The section 4911 tax does NOT apply to ALL organizations described in section 501(c)(3); it applies only to "electing public charities." Electing public charities are those public charities that have made a valid election to be covered by the lobbying expenditure test under sections 501(h) and 4911. The rules about making and revoking the election, including the rules about which public charities are eligible to make the election, are in section 501(h) and in section 1.501(h) of the regulations. The section 4911 tax does NOT apply to private foundations (but see Q&A-4), nor does the tax apply to NONelecting public charities (public charities that have NOT made a valid election to be covered by sections 501(h) and 4911) (but see Q&A-3).

Q-3: WHAT, IN GENERAL TERMS, IS THE EFFECT OF SECTIONS 501(h) AND 4911 ON NONELECTING PUBLIC CHARITIES?

A-3: If a public charity does not have a valid section 501(h) election in effect during a given year, that nonelecting public charity's lobbying activities and expenditures during that year are NOT covered by sections 501(h) and 4911, but are instead covered by what is known as the "substantial part test" under section 501(c)(3). In other words, sections 501(h) and 4911 do not apply to or affect NONElecting public charities. In fact, section 501(h)(7) says that nothing in sections 501(h) and 4911 (or the applicable Treasury Regulations) may be used to interpret the meaning of or the rules and definitions under the "substantial part test." (For a very brief summary of the "substantial part test," see Q&A-17).

Q-4: WHAT, IN GENERAL TERMS, IS THE EFFECT OF SECTIONS 501(h) AND 4911 ON PRIVATE FOUNDATIONS?

A-4: Private foundations' lobbying expenditures are taxed under section 4945(d) rather than under section 4911. Unlike section 4911, which taxes only EXCESSIVE lobbying expenditures, section 4945(d) taxes ANY lobbying expenditure by a private foundation. Even though the section 4911 tax does not apply to private foundations, portions of the regulations under section 4911 are nonetheless relevant to private foundations because the definition of what is and is not a lobbying expenditure is generally the same under section 4911 as under section 4945 (see sections 56.4911-2 and -3, but disregard section 56.4911-5).

Q-5: TO WHICH EXPENDITURES BY AN ELECTING PUBLIC CHARITY DOES THE SECTION 4911 TAX APPLY?

A-5: The section 4911 tax applies only to EXCESS lobbying expenditures by an electing public charity. The tax does not apply to ALL lobbying expenditures by an electing public charity, but only to that portion of the organization's lobbying expenditures that exceed one of two permitted lobbying levels for that organization for that year. One of the permitted lobbying levels is based on total lobbying expenditures; total expenditures for both direct and grass roots lobbying. The other permitted lobbying level is a separate limit based on grass roots lobbying

expenditures. See Q&A-12 for a general explanation of the difference between direct and grass roots lobbying.

Q-6: DOES THE SECTION 4911 TAX APPLY TO POLITICAL EXPENDITURES AS WELL AS LOBBYING EXPENDITURES?

A-6: No. It is important to note that the section 4911 tax applies only to LOBBYING expenditures, as opposed to POLITICAL expenditures or activities. In contrast to lobbying, all charities are ABSOLUTELY PROHIBITED from intervening in a political campaign on behalf of or in opposition to any candidate for an elective public office. As stated above, public charities may engage in some lobbying but they must not intervene in a political campaign at all. If a charity does intervene in a political campaign, it would jeopardize both its tax-exempt status and its ability to receive tax-deductible charitable contributions (under section 170). It (and in certain cases its managers) may also be liable for tax under section 4955. Finally, under certain circumstances, the charity may also be subject to tax under section 527(f).

Q-7: HOW MUCH MAY AN ELECTING PUBLIC CHARITY SPEND ON TOTAL LOBBYING WITHOUT BEING TAXED UNDER SECTION 4911?

A-7: In any given year, an electing public charity may spend up to a specified percentage of its exempt purpose expenditures on total (both direct and grass roots) lobbying without being taxed under section 4911 (see section 56.4911-1(c) for the specific declining percentages allowed for organizations of various sizes). In no case, however, may an electing public charity spend more than \$1,000,000 in any given year on lobbying without being taxed under section 4911.

Q-8: HOW MUCH MAY AN ELECTING PUBLIC CHARITY SPEND ON GRASS ROOTS LOBBYING WITHOUT BEING TAXED UNDER SECTION 4911?

A-8: In addition to the limit on an electing public charity's total lobbying expenditures, there is a separate limit for grass roots lobbying expenditures. In any given year, an electing public charity may spend up to that separate limit on grass roots lobbying without incurring any tax under section 4911. The amount of this separate limit for grass roots lobbying expenditures is 25 percent of the amount that the organization is permitted to spend during that year on total (both direct and grass roots) lobbying (see Q&A-7). In any event, \$250,000 is the maximum amount an electing public charity may spend on grass roots lobbying without incurring tax under section 4911.

Q-9: IN ADDITION TO RESULTING IN TAX UNDER SECTION 4911, CAN EXCESSIVE SPENDING ON LOBBYING HAVE OTHER ADVERSE TAX CONSEQUENCES FOR AN ELECTING PUBLIC CHARITY?

A-9: Yes. If an electing public charity normally makes excessive lobbying expenditures, it may be in danger of losing its tax-exempt status. Generally speaking, an electing public charity will lose its tax-exempt status (and its ability to receive tax-deductible charitable contributions) if the organization's lobbying expenditures over a four-year period exceed one of the two lobbying limits by more than 150 percent. See section 501(h) and the applicable Treasury Regulations for further detail.

Q-10: WHAT IS AN EXEMPT PURPOSE EXPENDITURE?

A-10: Because the amount an electing public charity may spend on lobbying (without incurring tax) is often a percentage of the organization's exempt purpose

expenditures, it is important to understand which expenditures are, and which are not exempt purpose expenditures. In general terms, an expenditure is an exempt purpose expenditure if it is paid or incurred by an electing public charity to accomplish the organization's exempt purposes. For further detail on the definition of "exempt purpose expenditure" see section 4911(e)(1) and section 56.4911-4.

Q-11: WHICH EXPENDITURES ARE LOBBYING EXPENDITURES AND WHICH ARE NOT?

A-11: To know whether an organization has spent excessive amounts on lobbying, one needs to determine which expenditures are lobbying expenditures and which are not lobbying expenditures. In general, there are two types of lobbying expenditures: expenditures for direct lobbying communications and expenditures for grass roots lobbying communications.

Q-12: HOW ARE THE TERMS "DIRECT LOBBYING COMMUNICATION" AND "GRASS ROOTS LOBBYING COMMUNICATION" DEFINED?

A-12: In very general terms (and subject to exceptions), a direct lobbying communication is an attempt to influence legislation by communicating directly with a government official, whereas a grass roots lobbying communication is an attempt to influence legislation by communicating with the general public or a segment thereof. (Note: some communications may be BOTH direct and grass roots lobbying). The terms "direct lobbying communication" and "grass roots lobbying communication" are defined at length in section 56.4911-2. That section contains a general definition of each type of lobbying communication. It also has special definitions that apply only in limited circumstances (such as a special rebuttable presumption that certain paid mass media advertisements that run shortly before a legislative vote on highly publicized legislation are grass roots lobbying communications). Section 56.4911-2(c) contains several exceptions that sometimes apply to cause communications that would otherwise be lobbying to be nonlobbying. Throughout section 56.4911-2, there are numerous examples designed to illustrate the various definitions and exceptions. (For more lenient definitions where an electing public charity makes a communication solely or primarily to its bona fide members, see section 4911(d)(3) and section 56.4911-5).

Q-13: IS LOBBYING ON REFERENDA AND BALLOT INITIATIVES CONSIDERED GRASS ROOTS OR DIRECT LOBBYING?

A-13: Lobbying on referenda, ballot initiatives and similar measures is, solely for purposes of section 4911, treated as direct rather than grass roots lobbying. See section 56.4911-2(b)(1)(iii). However, charities are not permitted to intervene in a political campaign on behalf of or in opposition to a candidate for an elective public office (as described in Q&A-6).

Q-14: ARE THERE ANY SPECIAL ACCOUNTING AND ALLOCATION RULES FOR PURPOSES OF SECTION 4911?

A-14: An electing public charity that makes a direct and/or grass roots lobbying communication must treat the expenditures for that communication as lobbying expenditures in whole or in part. See section 56.4911-3 for accounting rules regarding which expenditures are expenditures "for" the lobbying communication as well as rules regarding the allocation of expenditures that are for mixed purpose communications (for example, communications that are both direct and grass roots lobbying communications and communications that are

lobbying communications but also have a bona fide nonlobbying purpose). Section 56.4911-3 also contains rules regarding whether certain of an electing public charity's payments (such as grants) to other organizations that lobby are treated as direct and/or grass roots lobbying expenditures by the electing public charity that makes the payments.

Q-15: CAN TWO OR MORE ORGANIZATIONS EVER BE CONSIDERED ONE SINGLE ORGANIZATION FOR PURPOSES OF DETERMINING WHETHER THE ORGANIZATIONS OWE TAX UNDER SECTION 4911 ON EXCESS LOBBYING EXPENDITURES?

A-15: Yes. Under section 4911(f), certain closely affiliated organizations are sometimes treated as a single organization for purposes of determining whether the organizations owe tax under section 4911 on excess lobbying expenditures. See sections 56.4911-7 through -10.

Q-16: MUST CHARITIES THAT LOBBY KEEP RECORDS AND REPORT ON THEIR LOBBYING EXPENDITURES AND/OR ACTIVITIES?

A-16: Yes. For electing public charities, recordkeeping and return filing requirements are generally set forth in sections 56.4911-6, 56.6001-1 and 56.6011-1. Nonelecting charities must also keep records and file returns as specified in various forms and their instructions.

Q-17: IF AN ORGANIZATION IS COVERED BY THE "SUBSTANTIAL PART TEST," WHAT, IN GENERAL, ARE THE RULES THAT GOVERN THE ORGANIZATION'S LOBBYING ACTIVITIES AND EXPENDITURES?

A-17: The "substantial part test" applies to all section 501(c)(3) organizations other than electing public charities. Under the "substantial part test," no substantial part of the organization's activities may be carrying on propaganda, or otherwise attempting, to influence legislation (see section 1.501(c)(3)-1). If an organization to which the substantial part test applies engages in substantial lobbying activities during a given year, the organization will lose both its tax exempt status and its ability to receive tax-deductible charitable contributions. The organization will also be subject to an excise tax under section 4912 on its lobbying expenditures during the year. In addition, the managers of such a nonelecting public charity may in certain cases be jointly and severally liable for a tax under section 4912(b). The tax under section 4912 does not apply to electing public charities. (This is the end of the Q&As).

RULINGS REGARDING APPLICATION OF THE REGULATIONS

Under its ruling program (see Rev. Proc. 83-36, 1983-1 C.B. 763 and Rev. Proc. 88-8, 1988-4 I.R.B. 22), the Service will consider requests for private letter rulings to clarify the application of the regulations to particular fact patterns.

SPECIAL ANALYSES

It has been determined that these rules are not major rules as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. Chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations and, therefore, a final Regulatory Flexibility Analysis is not required.

DRAFTING INFORMATION

The principal author of these regulations is Jerome P. Walsh Skelly of the Office of Assistant Chief Counsel (Employee Benefits and Exempt Organizations), Internal Revenue Service. However, personnel from other offices of the Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

SUPERSESION

These regulations supersede section 7.0(c)(4) of the Temporary Income Tax Regulations under the Tax Reform Act of 1976.

LIST OF SUBJECTS

- 26 CFR 1.61-1 through 1.281-4
Deductions, Exemptions, Income taxes, Taxable income
- 26 CFR 1.501(a)-1 through 1.528-10
Cooperatives, Exempt organizations, Foundations, Homeowners associations, Nonprofit organizations, Political organizations
- 26 CFR 1.6001-1 through 1.6109-2
Administration and procedure, Filing requirements, Income taxes
- 26 CFR Part 7
Income taxes, Tax Reform Act of 1976
- 26 CFR Part 20
Estate taxes
- 26 CFR Part 25
Gift taxes
- 26 CFR Part 53
Excise taxes, Foundations, Investments, Trusts and trustees
- 26 CFR Part 56
Excise tax, Lobbying expenditures, Exempt purpose expenditures, Affiliated organizations, Administration and procedure
- 26 CFR Part 602
OMB Control Numbers under the Paperwork Reduction Act

ADOPTION OF AMENDMENTS TO THE REGULATIONS

Accordingly, 26 CFR Chapter I is amended as follows:

PART 1 - INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * sections 1.504-1 and 1.504-2 also issued under 26 U.S.C. 504(b).

Par. 2. Section 1.170A-1 is amended by revising paragraph (h)(5), adding a new paragraph (h)(11), and revising paragraph (i). These revised and added provisions read as follows:

SECTION 1.170A-1 CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS; ALLOWANCE OF DEDUCTION.

(h) EXCEPTIONS AND OTHER RULES. * * *

(5) No deduction shall be allowed under section 170 for amounts paid to an organization:

(i) Which is disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, or

(ii) Which participates in, or intervenes in (including the publishing or distributing of statements), any political campaign on behalf of or in opposition to any candidate for public office.

For purposes of determining whether an organization is attempting to influence legislation or is engaging in political activities, see sections 501(c)(3), 501(h), 4911 and the regulations thereunder.

(11) No deduction shall be allowed under section 170 for out-of-pocket expenditures on behalf of an eligible organization (within the meaning of section 1.501(h)-2(b)(1)) if the expenditure is made in connection with influencing legislation (within the meaning of section 501(c)(3) or section 56.4911-2), or in connection with the payment of the organization's tax liability under section 4911. For the treatment of similar expenditures on behalf of other organizations see paragraph (h)(6) of this section.

(i) **EFFECTIVE DATE.** In general this section applies to contributions paid in taxable years beginning after December 31, 1969. Paragraph (h)(11) of this section, however, applies only to out-of-pocket expenditures made in taxable years beginning after December 31, 1976.

Par. 3. In section 1.501(c)(3)-1, paragraph (b)(3) is amended by adding a sentence at the end of the concluding text, and paragraph (c)(3)(ii) is amended by adding a sentence at the end of the concluding text, to read:

SECTION 1.501(c)(3)-1 ORGANIZATIONS ORGANIZED AND OPERATED FOR RELIGIOUS, CHARITABLE, SCIENTIFIC, TESTING FOR PUBLIC SAFETY, LITERARY, OR EDUCATIONAL PURPOSES, OR FOR THE PREVENTION OF CRUELTY TO CHILDREN OR ANIMALS.

(b) ORGANIZATIONAL TEST. * * *

(3) **AUTHORIZATION OF LEGISLATIVE OR POLITICAL ACTIVITIES.**

* * * An organization's articles will not violate the provisions of paragraph (b)(3)(i) of this section even though the organization's articles expressly empower it to make the election provided for in section 501(b) with respect to influencing legislation and, only if it so elects, to make lobbying or grass roots expenditures that do not normally exceed the ceiling amounts prescribed by section 501(h)(2)(B) and (D).

(c) OPERATIONAL TEST. * * *

(3) **"ACTION" ORGANIZATIONS. * * ***

(ii) ***

*** An organization for which the expenditure test election of section 501(h) is in effect for a taxable year will not be considered an "action" organization by reason of this paragraph (c)(3)(ii) for that year if it is not denied exemption from taxation under section 501(a) by reason of section 501(h). *****

Par. 4. In section 1.501(c)(4)-1, paragraph (a)(2)(ii) is amended by revising the last sentence and adding a new sentence immediately thereafter. The revised and added sentences read as follows:

SECTION 1.501(c)(4)-1 CIVIC ORGANIZATIONS AND LOCAL ASSOCIATIONS OF EMPLOYEES.

(a) CIVIC ORGANIZATIONS. ***

(2) PROMOTION OF SOCIAL WELFARE. ***

(ii) POLITICAL OR SOCIAL ACTIVITIES. ***

A social welfare organization that is not, at any time after October 4, 1976, exempt from taxation as an organization described in section 501(c)(3) may qualify under section 501(c)(4) even though it is an "action" organization described in section 1.501(c)(3)-1(c)(3)(ii) or (iv), if it otherwise qualifies under this section. For rules relating to an organization that is, after October 4, 1976, exempt from taxation as an organization described in section 501(c)(3), see section 504 and section 1.504-1. *****

Par. 5. The following new sections 1.501(h)-1 through 1.501(h)-3 are added in the appropriate place:

SECTION 1.501(h)-1 APPLICATION OF THE "EXPENDITURE TEST" TO EXPENDITURES TO INFLUENCE LEGISLATION; INTRODUCTION.

(a) SCOPE -- (1) There are certain requirements an organization must meet in order to be a "charity" described in section 501(c)(3). Among other things, section 501(c)(3) states that "no substantial part of the activities of [a charity may consist of] carrying on propaganda, or otherwise attempting to influence legislation, (except as otherwise provided in subsection (h))." This requirement is called the "substantial part test."

(2) Under section 501(h), many public charities may elect the "expenditure test" as a substitute for the substantial part test. The expenditure test is described in section 501(h) and this section 1.501(h). A public charity is any charity that is not a private foundation under section 509(a). (Unlike a public charity, a private foundation may not make any lobbying expenditures: if a private foundation does make a lobbying expenditure, it is subject to an excise tax under section 4945). Section 1.501(h)-2 lists which public charities are eligible to make the expenditure test election. Section 1.501(h)-2 also provides information about how a public charity makes and revokes the election to be covered by the expenditure test.

(3) A public charity that makes the election may make lobbying expenditures within specified dollar limits. If an electing public charity's lobbying expenditures are within the dollar limits determined under section 4911(c), the electing public charity will not owe tax under section 4911 nor will it lose its tax exempt status as a charity by virtue of section 501(h). If, however, that electing public charity's lobbying expenditures exceed its section 4911 lobbying limit, the organization is subject to an excise tax on the excess lobbying expenditures. Further, under section 501(h), if an electing public charity's lobbying expenditures normally are more than 150 Percent of its

section 4911 lobbying limit, the organization will cease to be a charity described in section 501(c)(3).

(4) A public charity that elects the expenditure test may nevertheless lose its tax exempt status if it is an action organization under section 1.501(c)(3)-1(c)(3)(iii) or (iv). A public charity that does not elect the expenditure test remains subject to the substantial part test. The substantial part test is applied without regard to the provisions of section 501(h) and 4911 and the related regulations.

(b) EFFECTIVE DATE. The provisions of section 1.501(h)-1 through section 1.501(h)-3, are effective for taxable years beginning after August 31, 1990. An election made before August 31, 1990, under the provisions of section 7.0(c)(4) or the instructions to Form 5768, will be effective under these regulations without again filing Form 5768.

SECTION 1.501(h)-2 ELECTING THE EXPENDITURE TEST.

(a) IN GENERAL. The election to be governed by section 501(h) may be made by an eligible organization (as described in paragraph (b) of this section) for any taxable year of the organization beginning after December 31, 1976, other than the first taxable year for which a voluntary revocation of the election is effective (see paragraph (d) of this section). The election is made by filing a completed Form 5758, Election/Revocation of Election by an Eligible Section 501(c)(3) Organization to Make Expenditures to Influence Legislation, with the appropriate Internal Revenue Service Center listed on that form. Under section 501(h)(6), the election is effective with the beginning of the taxable year in which the form is filed. For example, if an eligible organization whose taxable year is the calendar year files Form 5768 on December 31, 1979, the organization is governed by section 501(h) for its taxable year beginning January 1, 1979. Once made, the expenditure test election is effective (without again filing Form 5768) for each succeeding taxable year for which the organization is an eligible organization and which begins before a notice of revocation is filed under paragraph (d) of this section.

(b) ORGANIZATIONS ELIGIBLE TO ELECT THE EXPENDITURE TEST -- (1) IN GENERAL. For purposes of section 501(h) and the regulations thereunder, an organization is an eligible organization for a taxable year if, for that taxable year, it is --

(i) Described in section 501(c)(3) (determined, in any year for which an election is in effect, without regard to the substantial part test of section 501(c)(3)).

(ii) Described in section 501(h)(4) and paragraph (b)(2) of this section, and

(iii) Not a disqualified organization described in section 501(h)(5) and paragraph (b)(3) of this section.

(2) CERTAIN ORGANIZATIONS LISTED. An organization is described in section 501(h)(4) and this paragraph (b)(2) if it is an organization described in --

(i) Section 170(b)(1)(A)(ii) (relating to educational institutions),

(ii) Section 170(b)(1)(A)(iii) (relating to hospitals and medical research organizations),

(iii) Section 170(b)(1)(A)(iv) (relating to organizations supporting government schools),

(iv) Section 170(b)(1)(A)(vi) (relating to organizations publicly supported by charitable contributions).

(v) Section 509(a)(2) (relating to organizations publicly supported by admissions, sales, etc.), or

(vi) Section 509(a)(3) (relating to organizations supporting public charities), except that for purposes of this paragraph (b)(2), section 509(a)(3) shall be applied without regard to the last sentence of section 509(a).

(3) **DISQUALIFIED ORGANIZATIONS.** An organization is a disqualified organization described in section 501(h)(5) and this paragraph (b)(3) if the organization is —

(i) Described in section 170(b)(1)(A)(i) (relating to churches).

(ii) An integrated auxiliary of a church or of a convention or association of churches (see section 1.6033-2(g)(5)), or

(iii) Described in section 501(c)(3) and affiliated (within the meaning of section 56.4911-7) with one or more organizations described in paragraph (b)(3)(i) or (ii) of this section.

(4) **OTHER ORGANIZATIONS INELIGIBLE TO ELECT.** Under section 501(h)(4), certain organizations, although not disqualified organizations, are not eligible to elect the expenditure test. For example, organizations described in section 509(a)(4) are not listed in section 501(h)(4) and therefore are not eligible to elect. Similarly, private foundations (within the meaning of section 509(a)) are not eligible to elect. For the treatment of expenditures by a private foundation for the purpose of carrying on propaganda, or otherwise attempting, to influence legislation, see section 53.4945-2.

(c) **NEW ORGANIZATIONS.** A newly created organization may submit Form 5768 to elect the expenditure test under section 501(h) before it is determined to be an eligible organization and may submit Form 5768 at the time it submits its application for recognition of exemption (Form 1023). If the newly created organization is determined to be an eligible organization, the election will be effective under the provisions of paragraph (a) of this section, that is, with the beginning of the taxable year in which the Form 5768 is filed by the eligible organization. However, if a newly created organization is determined by the Service not to be an eligible organization, the organization's election will not be effective and the substantial part test will apply from the effective date of its section 501(c)(3) classification.

(d) **VOLUNTARY REVOCATION OF EXPENDITURE TEST ELECTION — (1) REVOCATION EFFECTIVE.** An organization may voluntarily revoke an expenditure test election by filing a notice of voluntary revocation with the appropriate Internal Revenue Service Center listed on Form 5768. Under section 501(h)(6)(B), a voluntary revocation is effective with the beginning of the first taxable year after the taxable year in which the notice is filed. If an organization voluntarily revokes its election, the substantial part test of section 501(c)(3) will apply with respect to the organization's activities in attempting to influence legislation beginning with the taxable year for which the voluntary revocation is effective.

(2) **RE-ELECTION OF EXPENDITURE TEST.** If an organization's expenditure test election is voluntarily revoked, the organization may again make the expenditure test election, effective no earlier than for the taxable year following the first taxable year for which the revocation is effective.

(3) **EXAMPLE X.** an organization whose taxable year is the calendar year, plans to voluntarily revoke its expenditure test election effective beginning with its

taxable year 1985. X must file its notice of voluntary revocation on Form 5768 after December 31, 1983, and before January 1, 1985. If X files a notice of voluntary revocation on December 31, 1984, the revocation is effective beginning with its taxable year 1985. The organization may again elect the expenditure test by filing Form 5768. Under paragraph (d)(2) of this section, the election may not be made for taxable year 1985. Under paragraph (a) of this section, a new expenditure test election will be effective for taxable years beginning with taxable year 1986, if the Form 5768 is filed after December 31, 1985, and before January 1, 1987.

(e) **INVOLUNTARY REVOCATION OF EXPENDITURE TEST ELECTION.** If, while an election by an eligible organization is in effect, the organization ceases to be an eligible organization, its election is automatically revoked. The revocation is effective with the beginning of the first full taxable year for which it is determined that the organization is not an eligible organization. If an organization's expenditure test election is involuntarily revoked under this paragraph (e) but the organization continues to be described in section 501(c)(3), the substantial part test of section 501(c)(3) will apply with respect to the organization's activities in attempting to influence legislation beginning with the first taxable year for which the involuntary revocation is effective.

(f) **SUPERSESSON.** This section supersedes section 7.0(c)(4) of the Temporary Income Tax Regulations under the Tax Reform Act of 1976, effective August 31, 1990.

SECTION 1.501(h)-3 LOBBYING OR GRASS ROOTS EXPENDITURES NORMALLY IN EXCESS OF CEILING AMOUNT.

(a) **SCOPE.** This section provides rules under section 501(h) for determining whether an organization that has elected the expenditure test and that is not a member of an affiliated group of organizations (as defined in section 56.4911-7(e)) either normally makes lobbying expenditures in excess of its lobbying ceiling amount or normally makes grass roots expenditures in excess of its grass roots ceiling amount. Under section 501(h) and this section, an organization that has elected the expenditure test and that normally makes expenditures in excess of the corresponding ceiling amount will cease to be exempt from tax under section 501(a) as an organization described in section 501(c)(3). For similar rules relating to members of an affiliated group of organizations, see section 56.4911-9.

(b) **LOSS OF EXEMPTION — (1) IN GENERAL.** Under section 501(h)(1), an organization that has elected the expenditure test shall be denied exemption from taxation under section 501(a) as an organization described in section 501(c)(3) for the taxable year following a determination year if —

(i) The sum of the organization's lobbying expenditures for the base years exceeds 150 percent of the sum of its lobbying nontaxable amounts for the base years, or

(ii) The sum of the organization's grass roots expenditures for its base years exceeds 150 percent of the sum of its grass roots nontaxable amounts for the base years.

The organization thereafter shall not be exempt from tax under section 501(a) as an organization described in section 501(c)(3) unless, pursuant to paragraph (d) of this section, the organization reapplies for recognition of exemption and is recognized as exempt.

(2) **SPECIAL EXCEPTION FOR ORGANIZATION'S FIRST ELECTION.** For the first, second, or third

consecutive determination year for which an organization's first expenditure test election is in effect, no determination is required under paragraph (b)(1) of this section, and the organization will not be denied exemption from tax by reason of section 501(h) and this section if, taking into account as base years only those years for which the expenditure test election is in effect —

(i) The sum of the organization's lobbying expenditures for such base years does not exceed 150 percent of the sum of its lobbying nontaxable amounts for the same base years, and

(ii) The sum of the organization's grass roots expenditure for those base years does not exceed 150 percent of the sum of its grass roots nontaxable amounts for such base years. If an organization does not satisfy the requirements of this paragraph (b)(2), paragraph (b)(1) of this section will apply.

(c) DEFINITIONS, for purposes of this section —

(1) The term "lobbying expenditures" means lobbying expenditures as defined in section 4911(c)(1) or section 4911(f)(4)(A) and section 56.4911-2(a).

(2) The term "lobbying nontaxable amount" is defined in section 56.4911-1(c)(1).

(3) An organization's "lobbying ceiling amount" is 150 percent of the organization's lobbying nontaxable amount for a taxable year.

(4) The term "grass roots expenditures" means expenditures for grass roots lobbying communications as defined in section 4911(c)(3) or section 4911(f)(4)(A) and sections 56.4911-2 and 3.

(5) The term "grass roots nontaxable amount" is defined in section 56.4911-1(c)(2).

(6) An organization's "grass roots ceiling amount" is 150 percent of the organization's grass roots nontaxable amount for a taxable year.

(7) In general, the term "base years" means the determination year and the three taxable years immediately preceding the determination year. The base years, however, do not include any taxable year preceding the taxable year for which the organization is first treated as described in section 501(c)(3).

(8) A taxable year is a "determination year" if it is a year for which the expenditure test election is in effect, other than the taxable year for which the organization is first treated as described in section 501(c)(3).

(d) REAPPLICATION FOR RECOGNITION OF EXEMPTION — (1) TIME OF APPLICATION. An organization that is denied exemption from taxation under section 501(a) by reason of section 501(h) and this section may apply on Form 1023 for recognition of exemption as an organization described in section 501(c)(3) for any taxable year following the first taxable year for which exemption is so denied. See paragraphs (d)(2) and (d)(3) of this section for material to be included with an application described in the preceding sentence.

(2) SECTION 501(h) CALCULATION. An application described in paragraph (d)(1) of this section must demonstrate that the organization would not be denied exemption from taxation under section 501(a) by reason of section 501(h) if the expenditure test election had been in effect for all of its last taxable year ending before the application is made by providing the calculations, described either in paragraph (b)(1)(i) and (ii) of this section or in section 56.4911-9(b), that would have applied to the organization for that year.

(3) OPERATIONS NOT DISQUALIFYING. An application described in paragraph (d)(1) of this section must include information that demonstrates to the satisfaction of the Commissioner that the organization will not knowingly operate in a manner that would disqualify the organization for tax exemption under section 501(c)(3) by reason of attempting to influence legislation.

(4) REELECTION OF EXPENDITURE TEST. If an organization is denied exemption from tax for a taxable year by reason of section 501(h) and this section, and thereafter is again recognized as an organization described in section 501(c)(3) pursuant to this paragraph (d), it may again elect the expenditure test under section 501(h) in accordance with section 1.501(h)-2(a).

(e) EXAMPLES. The provisions of this section are illustrated by the following examples, which also illustrate the operation of the tax imposed by section 4911.

EXAMPLE (1). (1) The following table contains information used in this example concerning organization X.

Year	Exempt	Lobbying	Lobbying	
	Purpose			Nontaxable
	Expenditures	Amount	Expenditures	
	(SPE)	Calculation	(LNTA)	
			(L2)	
1979	\$ 400,000	(20% of \$400,000 =)	\$ 80,000	\$100,000
1980	300,000	(20% of \$300,000 =)	60,000	100,000
1981	400,000	(20% of \$500,000 =)	110,000	120,000
1982	550,000	(20% of \$550,000 =)	110,000	100,000
Totals: \$1,650,000			\$360,000	\$420,000

(2) Organization X, whose taxable year is the calendar year, was organized in 1971. X first made the expenditure test election under section 501(h) effective for taxable years beginning with 1979 and has not revoked the election. None of X's lobbying expenditures for its taxable years 1979 through 1982 are grass roots expenditures. Under section 4911(a) and section 56.4911-1(a), X must determine for each year for which the expenditure test election is effective whether it is liable for the 25 percent excise tax imposed by section 4911(a) on excess lobbying expenditures. X is liable for this tax for each of its taxable years 1979, 1980, and 1981, because in each year its lobbying expenditures exceeded its lobbying nontaxable amount for the year. For 1979, the tax imposed by section 4911(a) is \$5,000 (25% x (\$100,000 - \$80,000) = \$5,000). For 1980, the tax is \$10,000. For 1981, the tax is \$1,250.

(3) The taxable years 1979 through 1981 are all determination years under paragraph (c)(8) of this section. On its annual return for determination year 1979, the first year of its first election, X can demonstrate, under paragraph (b)(2) of this section, that its lobbying expenditures during 1979 (\$100,000) do not exceed 150 percent of its lobbying nontaxable amount for 1979 (\$120,000). For determination year 1980, under paragraph (b)(2), X can demonstrate that the sum of its lobbying expenditures for 1979 and 1980 (\$200,000) does not exceed 150 percent of the sum of its lobbying nontaxable amounts for 1979 and 1980 (\$210,000). For 1981, under paragraph (b)(2), X can demonstrate that the sum of its lobbying expenditures for 1979, 1980, and 1981 (\$320,000) does not exceed 150 percent of the sum of its lobbying nontaxable amounts for 1979, 1980, and 1981 (\$382,500). For each of the determination years 1979,

1980, and 1981, the first three years of its first election, X satisfies the requirements of paragraph (b)(2). Accordingly, no determination under paragraph (b)(1) of this section is required for those years, and X is not denied tax exemption by reason of section 501(h).

(4) Under paragraph (b)(1) of this section, X must determine for its determination year 1982 whether it has normally made lobbying expenditures in excess of the lobbying ceiling amount. This determination takes into account expenditures in base years 1979 through 1982. The sum of X's lobbying expenditures for the base years (\$420,000) does not exceed 150% of the sum of the lobbying nontaxable amounts for the base years (150% x \$355,000 = \$532,500). Accordingly, X is not denied tax exemption by reason of section 501(h).

EXAMPLE (2). (1) The following table contains information used in this example concerning W.

Year	Exempt Purpose Expenditures (EPE)	Calculation	Lobbying Nontaxable Amount (LNTA)	Lobbying Expenditures (LE)
1979	\$700,000	(20% of \$500,000 + 15% of \$200,000 =)	\$120,000	\$120,000
1980	\$800,000	(20% of \$500,000 + 15% of \$300,000 =)	\$145,000	\$100,000
1981	\$800,000	(20% of \$500,000 + 15% of \$300,000 =)	\$145,000	\$100,000
1982	\$800,000	(20% of \$500,000 + 15% of \$400,000 =)	\$180,000	\$190,000
Totals:	\$3,200,000		\$580,000	\$510,000

(Table continued)

Year	Grass Roots Nontaxable Amount (25% of LNTA)	Grass Roots Expenditures
1979	\$30,000	\$30,000
1980	\$36,250	\$40,000
1981	\$36,250	\$40,000
1982	\$45,000	\$45,000
Totals:	\$145,000	\$220,000

(2) Organization W, whose taxable year is the calendar year, made the expenditure test election under section 501(h) effective for taxable years beginning with 1979 and has not revoked the election. W has been treated as an organization described in section 501(c)(3) for each of its taxable years beginning with its taxable year 1974.

(3) Under section 4911(a) and section 56.4911-1(a), W must determine for each year for which the expenditure test election is effective whether it is liable for the 25 percent excise tax imposed by section 4911(a) on excess lobbying expenditures. In 1980, 1981, and 1982, W has excess lobbying expenditures because its grass roots expenditures in each of those years exceeded its grass roots nontaxable amount for the year. Therefore, W is liable for the excise tax under section 4911(a) for those years. The tax imposed by section 4911(a) for 1980 is \$5,937.50 (25%

x (\$60,000 - \$36,250) = \$5,937.50). For 1981, the tax is \$7,187.50. For 1982, the tax is \$6,250.

(4) On its annual return for its determination years 1979, 1980, and 1981, the first three years of its first election, W demonstrates that it satisfies the requirements of paragraph (b)(2) of this section. Accordingly, no determination under paragraph (b)(1) of this section is required for those years, and W is not denied tax exemption by reason of section 501(h).

(5) On its annual return for its determination year 1982, W must determine under paragraph (b)(1) whether it has normally made lobbying expenditures or grass roots expenditures in excess of the corresponding ceiling amount. This determination takes into account expenditures in base years 1979 through 1982. The sum of W's lobbying expenditures for the base years (\$470,000) does not exceed 150% of the sum of W's lobbying nontaxable amounts for those years (150% x \$380,000 = \$570,000). However, the sum of W's grass roots expenditures for the base years (\$220,000) does exceed 150% of the sum of W's grass roots nontaxable amounts for those years (150% x \$145,000 = \$217,500). Under section 501(h), W is denied tax exemption under section 501(a) as an organization described in section 501(c)(3) for its taxable year 1983. For its taxable year 1984 and any taxable year thereafter, W is exempt from tax as an organization described in section 501(c)(3) only if W applies for recognition of its exempt status under paragraph (d) of this section and is recognized as exempt from tax.

EXAMPLE (3). (1) The following table contains information used in this example concerning organization Y.

Year	Exempt Purpose Expenditures (EPE)	Calculation	Lobbying Nontaxable Amount (LNTA)	Lobbying Expenditures (LE)	Grass Roots Nontaxable Amount (25% of LNTA)	Grass Roots Expenditures
1977	\$700,000	(20% of \$500,000 + 15% of \$200,000 =)	\$120,000	\$182,000	\$30,000	\$30,000
1978	\$800,000	(20% of \$500,000 + 15% of \$300,000 =)	\$145,000	\$284,750	\$36,250	\$35,000
Totals:	\$1,500,000		\$275,000	\$466,750	\$66,250	\$65,000
1979	\$900,000	(20% of \$500,000 + 15% of \$400,000 =)	\$160,000	\$244,000	\$40,000	\$50,000
Totals:	\$2,400,000		\$435,000	\$710,750	\$106,250	\$115,000

(2) Organization Y, whose taxable year is the calendar year, was first treated as an organization described in section 501(c)(3) on February 1, 1977. Y made the expenditure test election under section 501(h) effective for taxable years beginning with 1977 and has not revoked the election.

(3) For 1977, Y has excess lobbying expenditures of \$52,000 because its lobbying expenditures (\$182,000) exceed its lobbying nontaxable amount (\$130,000) for the taxable year. Accordingly, Y is liable for the 25 percent excise tax imposed by section 4911(a). The amount of the tax is \$13,000 ($25\% \times (\$182,000 - \$130,000) = \$13,000$).

(4) For 1978, Y again has excess lobbying expenditures and is again liable for the 25 percent excise tax imposed by section 4911(a). The amount of the tax is \$19,937.50 ($25\% \times (\$224,750 - \$145,000) = \$19,937.50$).

(5) For 1979, Y's lobbying expenditures (\$264,000) exceed its lobbying nontaxable amount (\$160,000) by \$104,000, and its grass roots expenditures (\$50,000) exceed its grass roots nontaxable amount (\$40,000) by \$10,000. Under section 56.4911-1(b), Y's excess lobbying expenditures are the greater of \$104,000 or \$10,000. The amount of the tax, therefore, is \$26,000 ($25\% \times \$104,000 = \$26,000$).

(6) Under paragraph (c)(8) of this section, 1977 is not a determination year because it is the first year for which the organization is treated as described in section 501(c)(3). For 1977, Y need not determine whether it has normally made lobbying expenditures or grass roots expenditures in excess of the corresponding ceiling amount for purposes of determining whether it is denied exemption under section 501(h) for its taxable year 1978.

(7) For determination year 1978, Y must determine whether it has normally made lobbying or grass roots expenditures in excess of the corresponding ceiling amount, taking into account expenditures for the base years 1977 and 1978. For Y, the determination under paragraph (b)(2) of this section considers the same base years as the determination under paragraph (b)(1) of this section and is, therefore, redundant. Accordingly, Y proceeds to determine, under (b)(1), whether it is denied exemption. Y's grass roots expenditures for 1977 and 1978 (\$65,000) did not exceed 150 percent of the sum of its grass roots nontaxable amounts for those years (\$103,125). Y's lobbying expenditures for 1977 and 1978 (\$406,750) did not exceed 150% of its lobbying nontaxable amount for those years ($150\% \times \$275,000 = \$412,500$). Therefore, Y is not denied tax exemption under section 501(h) for its taxable year 1979.

(8) For determination year 1979, the sum of Y's grass roots expenditures in base years 1977, 1978, and 1979 does not exceed 150 percent of its grass roots nontaxable amount (calculation omitted). However, the sum of Y's lobbying expenditures for the base years (\$670,750) does exceed 150% of the sum of the lobbying nontaxable amounts for those years ($150\% \times \$435,000 = \$652,500$). Since Y was not described in section 501(c)(3) prior to 1977, only the years 1977, 1978, and 1979 may be considered in determining whether Y has normally made lobbying expenditures in excess of its lobbying ceiling. Therefore, Y determines that it has normally made lobbying expenditures in excess of its lobbying ceiling. Under section 501(h), Y is denied tax exemption under section 501(a) as an organization described in section 501(c)(3) for its taxable year 1980. For its taxable year 1981, and any taxable year thereafter, Y is exempt from tax as an organization described in section 501(c)(3) only if Y applies for recognition of its exempt status under paragraph (d) of this section and is recognized as exempt from tax.

EXAMPLE (4). Organization M made the expenditure test election under section 501(h) effective for taxable years beginning with 1977 and has not revoked the election. M has \$500,000 of exempt purpose expenditures

during each of the years 1981 through 1984. In addition, during each of those years, M spends \$75,000 for direct lobbying and \$25,000 for grass roots lobbying. Since the amount expended for M's lobbying (both total lobbying and grass roots lobbying) is within the respective nontaxable expenditure limitations, M is not liable for the 25 percent excise tax imposed under section 4911(a) upon excess lobbying expenditures, nor is M denied tax-exempt status by reason of section 501(h).

EXAMPLE (5). Assume the same facts as in Example (4), except that, on behalf of M, numerous unpaid volunteers conduct substantial lobbying activities with no reimbursement. Since the substantial lobbying activities of the unpaid volunteers are not counted towards the expenditure limitations and the amount expended for M's lobbying is within the respective nontaxable expenditure limitations, M is not liable for the 25 percent excise tax under section 4911, nor is M denied tax-exempt status by reason of section 501(h).

Par. 6. Section 1.504-1 is revised and new section 1.504-2 is added, to read as follows:

SECTION 1.504-1 ATTEMPTS TO INFLUENCE LEGISLATION; CERTAIN ORGANIZATIONS FORMERLY DESCRIBED IN SECTION 501(c)(8) DENIED EXEMPTION.

Section 504(a) and this section apply to an organization that is exempt from taxation at any time after October 4, 1976, as an organization described in section 501(c)(3), and that ceases to be described in that section because it -

(a) Is an "action" organization within the meaning of section 1.501(c)(3)-1(c)(3)(ii) or (iv), on account of activities occurring after October 4, 1976, or

(b) Is denied exemption under the provisions of section 501(h) (see section 1.501(h)-3 or section 56.4911-9).

This section does not apply, however, to an organization that was described in section 501(h)(5) and section 1.501(h)-2(b)(3) (relating generally to churches) for its taxable year immediately preceding the first taxable year for which it is no longer an organization described in section 501(c)(3). An organization to which section 504(a) and this section apply shall not be treated as described in section 501(c)(4) at any time after the organization ceases to be described in section 501(c)(3). Further, an organization denied treatment as an organization described in section 501(c)(4) under this section may not be treated as an organization described in section 501(c) other than as an organization described in section 501(c)(3). For rules relating to recognition of exemption after exemption is denied under section 501(h), see section 1.501(h)-3(d).

SECTION 1.504-2 CERTAIN TRANSFERS MADE TO AVOID SECTION 504(a).

(a) **SCOPE.** Under section 504(b), a transfer described in paragraph (b) or (c) of this section to an organization exempt from tax under section 501(a) may result in loss of exemption by the transferee unless the Commissioner determines, under paragraph (e) of this section, that the original transfer did not effect an avoidance of section 504(a). For purposes of this section, the term "transfer" includes any use by, or for the benefit of, the recipient of the transfer, but does not include any transfer made for adequate and full consideration.

(b) **TRANSFEROR AND TRANSFEREE COMMONLY CONTROLLED - (1) LOSS OF EXEMPTION.** A transfer is described in this paragraph (b) if it is described in paragraphs (b)(2) through (b)(6). The

transferee of a transfer described in this paragraph will cease to be exempt from tax under section 501(a), unless the provisions of paragraph (e) of this section apply.

(2) **TRANSFEROR ORGANIZATION.** A transfer is described in this paragraph (b)(2) only if it is from an organization that —

(i) Is or was described in section 501(c)(3), but not in section 501(h)(5), and

(ii) Is determined to be an "action" organization (as defined in section 1.501(c)(3)-1(c)(3)(ii) or (iv)), or is denied exemption from tax by reason of section 501(h) and either section 1.501(h)-3 or section 56.4911-9.

(3) **TRANSFEROR AND TRANSFEEE COMMONLY CONTROLLED.** A transfer is described in this paragraph (b)(3) only if, at the time of the transfer or at any time during the transferee's ten taxable years following the year in which the transfer was made, the transferee is controlled (directly or indirectly), as defined in paragraph (f) of this section, by the same person or persons who control the transferor.

(4) **TIME OF TRANSFER.** A transfer is described in this paragraph (b)(4) only if the transfer is made —

(i) After the date that is 24 months before the earliest of the effective date of the determination under section 501(h) that the transferor is not exempt, the effective date of the Commissioner's determination that the transferor is an "action" organization (as defined in section 1.501(c)(3)(ii) or (iv)), or the date on which the Commissioner proposes to treat it as no longer described in section 501(c)(3), and

(ii) Before the transferor again is recognized as an organization described in section 501(c)(3).

(5) **TRANSFEEE.** A transfer is described in this paragraph (b)(5) only if the transferee is exempt from tax under section 501(a) but the transferee is neither —

(i) An organization described in section 501(c)(3), nor

(ii) An organization described in section 401(a) to which the transferor contributes as an employer.

(6) **AMOUNT OF TRANSFER.** A transfer is described in this paragraph (b)(6) only if the amount of the transfer exceeds the lesser of 30 percent of the net fair market value of the transferor's assets or 50 percent of the net fair market value of the transferee's assets, computed immediately before the transfer. For purposes of this paragraph (b)(6) —

(i) The amount of a transfer by a transferor is the sum of the amounts transferred to any number of transferees in any number of transfers, all of which are described in paragraphs (b)(2) through (b)(5) of this section, and the time of the transfer is the time of the first transfer so taken into account; and

(ii) The amount of a transfer to a transferee is the sum of the amounts transferred by a transferor to the transferee in any number of transfers, all of which are described in paragraphs (b)(2) through (b)(5) of this section, and the time of the transfer is the time of the first transfer so taken into account.

(c) **OTHER TRANSFERS — (1) TRANSFERS INCLUDED.** A transfer is described in this paragraph (c) if it would be described in paragraph (b) of this section except that either —

(i) The amount of the transfer is less than the amount determined in paragraph (b)(6) of this section, or

(ii) The transferor and transferee are not commonly controlled as described in paragraph (b)(3) of this section, or

(iii) The transferee is an organization described in sections 501(c)(3) and 501(h)(4).

(2) **LOSS OF EXEMPTION.** The transferee of a transfer described in this paragraph (c) will cease to be exempt under section 501(a) if the Commissioner determines on all the facts and circumstances that the transfer effected an avoidance of section 504(a). In determining whether a transfer effected an avoidance of section 504(a), the Commissioner may consider whether the transferee engages, or has engaged, in attempts to influence legislation and may also consider any factors enumerated in paragraph (e) of this section.

(d) **DATE OF LOSS OF EXEMPT STATUS.** A transferee of a transfer described in paragraph (b), (c)(1)(ii), or (c)(1)(iii) of this section will cease to be exempt from tax under section 501(a) on the date that all requirements of paragraph (b), (c)(1)(ii), or (c)(1)(iii) (other than the determination by the Commissioner) are satisfied. A transferee of a transfer described in paragraph (c)(1)(i) of this section will cease to be exempt from tax under section 501(a) on the date of the last transfer preceding notification of the transferee that the Commissioner proposes to treat the transferee as other than an exempt organization.

(e) **TRANSFERS NOT IN AVOIDANCE OF SECTION 504(a).** Notwithstanding paragraph (b) of this section, if, based on all the facts and circumstances, the Commissioner determines that a transfer described in paragraph (b) did not effect an avoidance of section 504(a), the transferee will not be denied exemption from tax by reason of section 504(b) and this section. In making the determination called for in the preceding sentence, the Commissioner may consider all relevant factors including:

(1) Whether enforceable and effective conditions on the transfer preclude use of any of the transferred assets for any purpose that, if it were a substantial part of an organization's activities, would be inconsistent with exemption as an organization described in section 501(c)(3);

(2) In the absence of conditions described in paragraph (e)(1) of this section, whether the transferred assets are used exclusively for purposes that are consistent with the transferor's exemption as an organization described in section 501(c)(3);

(3) Whether the assets transferred would be described in section 53.4942(a)-2(c)(3) before, as well as after, the transfer if both the transferor and transferee were private foundations;

(4) Whether and to what extent the transfer would satisfy the provisions of section 1.507-2(a)(7) and (8) if the transferor were a private foundation;

(5) Whether all of the transferred assets have been expended during a period when the transferee was not controlled (directly or indirectly) by the same person or persons who controlled the transferor; and

(6) Whether the entire amount of the transferred assets were in turn transferred, before the close of the transferee's taxable year following the taxable year in which the transferred assets were received, to one or more organizations described in section 507(b)(1)(A) none of which are controlled (directly or indirectly) by the same persons who control either the original transferor or transferee.

(f) CONTROL. For purposes of section 504 and the regulations thereunder —

(1) The transferor will be presumed to control any organization with which it is affiliated within the meaning of section 56.4911-7(a), or would be if both organizations were described in section 501(c)(3), and

(2) The transferee will be treated as controlled (directly or indirectly) by the same person or persons who control the transferor if the transferee would be treated as controlled under section 53.4942(a)-3(a)(3), for which purpose the transferor shall be treated as a private foundation.

Par. 7. In section 1.6001-1(c), the last sentence is revised to read as follows:

SECTION 1.6001-1 RECORDS.

(c) EXEMPT ORGANIZATIONS. * * * See section 6033 and sections 1.6033-1 through -3.

Par. 8. Section 1.6033-2 is amended by adding paragraph (a)(2)(ii)(k). This added provision reads as follows:

SECTION 1.6033-2 RETURNS BY EXEMPT ORGANIZATIONS (TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1969) AND RETURNS BY CERTAIN NONEXEMPT ORGANIZATIONS (TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1980).

(a) IN GENERAL. * * *

(2) * * *

(ii) * * *

(k) Its lobbying expenditures, grass roots expenditures, exempt purpose expenditures, lobbying nontaxable amount, and grass roots nontaxable amount for the taxable year and for prior taxable years that are base years (within the meaning of section 1.501(h)-3(c)(7)), if the organization has an election under section 501(h) in effect for the taxable year. An organization that is a member of an affiliated group of organizations (as defined in section 56.4911-7(e)) but that is not a member of a limited affiliated group (as defined in section 56.4911-10(b)) shall report this information based on the expenditures of all members of the group during the taxable year of the group that ends with or within the member's taxable year and for prior taxable years of the group that are base years (within the meaning of section 56.4911-9(b)). For additional information required to be furnished by members of an affiliated group of organizations, and by controlling members in a limited affiliated group, see sections 56.4911-9(d) and 56.4911-10(f)(1), respectively.

PART 7 — TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1976

Par. 9. The authority citation for Part 7 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 10. In section 7.0, paragraph (c)(4) is removed and paragraph (d) is amended by removing “, (c)(4)” from the first parenthetical phrase in the first sentence.

PART 20 — ESTATE TAX REGULATIONS; ESTATES OF DECEDENTS DYING AFTER AUGUST 16, 1954

Par. 11. The authority citation for Part 20 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 12. Section 20.2055-1(a)(2) is revised to read as follows:

SECTION 20.2055-1 DEDUCTION FOR TRANSFERS FOR PUBLIC, CHARITABLE, AND RELIGIOUS USES, IN GENERAL.

(a) GENERAL RULE. * * *

(2) To or for the use of any corporation or association organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes (including the encouragement of art and for the prevention of cruelty to children or animals), if no part of the net earnings of the corporation or association inures to the benefit of any private stockholder or individual (other than as a legitimate object of such purposes), if the organization is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and if, in the case of transfers made after December 31, 1969, it 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.

PART 25 — GIFT TAX REGULATIONS; GIFTS MADE AFTER DECEMBER 31, 1954

Par. 13. The authority citation for Part 25 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 14. In section 25.2522(a)-1, paragraphs (a)(2) and (b)(2) are revised to read as follows:

SECTION 25.2522(a)-1 CHARITABLE AND SIMILAR GIFTS; CITIZENS OR RESIDENTS.

(a) * * *

(2) Any corporation, trust, community chest, fund, or foundation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, including the encouragement of art and the prevention of cruelty to children or animals, if no part of the net earnings of the organization inures to the benefit of any private shareholder or individual, if it is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and if, in the case of gifts made after December 31, 1969, it 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.

(b) * * *

(2) It must not be disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation.

PART 53 -- FOUNDATION AND SIMILAR EXCISE TAXES

Par. 15. The authority citation for Part 53 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 16. Section 53.4945-2 is amended as follows:

1. Paragraphs (a)(1), (a)(2) and (a)(5)(i) are revised to read as set forth below, and paragraph (a)(5)(iii) is removed;
2. Paragraphs (a)(6) and (a)(7) are added as set forth below;
3. Paragraphs (b) and (c) are removed and reserved.
4. Paragraph (d)(1)(i) is revised to read as set forth below.
5. Paragraph (d)(1)(ii) is revised to read as set forth below.
6. In paragraph (d)(1)(iv), the last sentence is revised to read as set forth below.
7. Paragraph (d)(1)(v), **EXAMPLES**, is redesignated as paragraph (d)(1)(vii), Examples (4) and (5) are revised, and new Examples (8) through (12) are added, to read as set forth below.
8. New paragraphs (d)(1)(v) and (d)(1)(vi) are added, to read as set forth below.
9. In paragraph (d)(2)(iii), new Examples (5) through (7) are added to read as set forth below.
10. Paragraph (d)(4) is revised to read as set forth below.

SECTION 53.4945-2 PROPAGANDA INFLUENCING LEGISLATION.

(a) **PROPAGANDA INFLUENCING LEGISLATION, ETC. -- (1) IN GENERAL.** Under section 4945(d)(1) the term "taxable expenditure" includes any amount paid or incurred by a private foundation to carry on propaganda, or otherwise to attempt, to influence legislation. An expenditure is an attempt to influence legislation if it is for a direct or grass roots lobbying communication, as defined in section 56.4911-2 (without reference to sections 56.4911-2(b)(3) and 56.4911-2(c)) and section 56.4911-3. See, however, paragraph (d) of this section for exceptions to the general rule of this paragraph (a)(1).

(2) **EXPENDITURES FOR MEMBERSHIP COMMUNICATIONS.** Section 56.4911-5, which provides special rules for electing public charities' communications with their members, does not apply to private foundations. Thus, whether a private foundation's communications with its members (assuming it has any) are lobbying communications is determined solely under section 56.4911-2 and without reference to section 56.4911-5. However, where a private foundation makes a grant to an electing public charity, section 56.4911-5 applies to the electing public charity's communications with its own members. Therefore, in the limited context of determining whether a private foundation's grant to an electing public charity is a taxable expenditure under section 4945, the section 56.4911-5 membership rules apply. For example, if the grant is specifically earmarked for a communication from the electing public charity to its members and the communication is, because of section 56.4911-5, a nonlobbying communication, the grant is not a taxable expenditure under section 4945.

* * * * *

(5) **GRANTS TO PUBLIC ORGANIZATIONS -- (1) IN GENERAL.** A grant by a private foundation to an organization described in section 509(a)(1), (2), or (3) does not constitute a taxable expenditure by the foundation under section 4945(d), other than under section 4945(d)(1), if the grant by the private foundation is not earmarked to be used for any activity described in section 4945(d)(2) or (5); is not earmarked to be used in a manner which would violate section 4945(d)(3) or (4), and there does not exist an agreement, oral or written, whereby the grantor foundation may cause the grantee to engage in any such prohibited activity or to select the recipient to which the grant is to be devoted. For purposes of this paragraph (a)(5)(i), a grant by a private foundation is earmarked if the grant is given pursuant to an agreement, oral or written, that the grant will be used for specific purposes. For the expenditure responsibility requirements with respect to organizations other than those described in section 509(a)(1), (2), or (3), see section 53.4945-5. For rules for determining whether grants to public charities are taxable expenditures under section 4945(d)(1), see paragraphs (a)(2), (a)(6) and (a)(7) of this section.

* * * * *

(6) **GRANTS TO PUBLIC ORGANIZATIONS THAT ATTEMPT TO INFLUENCE LEGISLATION -- (i) GENERAL SUPPORT GRANT.** A general support grant by a private foundation to an organization described in section 509(a)(1), (2), or (3) (a "public charity" for purposes of paragraphs (a)(6) and (7) of this section) does not constitute a taxable expenditure under section 4945(d)(1) to the extent that the grant is not earmarked, within the meaning of section 53.4945-2(a)(5)(i), to be used in an attempt to influence legislation. The preceding sentence applies without regard to whether the public charity has made the election under section 501(h).

(ii) **SPECIFIC PROJECT GRANT.** A grant by a private foundation to fund a specific project of a public charity is not a taxable expenditure by the foundation under section 4945(d)(1) to the extent that --

(A) The grant is not earmarked, within the meaning of section 53.4945-2(a)(5)(i), to be used in an attempt to influence legislation, and

(B) The amount of the grant, together with other grants by the same private foundation for the same project for the same year, does not exceed the amount budgeted, for the year of the grant, by the grantee organization for activities of the project that are not attempts to influence legislation. If the grant is for more than one year, the preceding sentence applies to each year of the grant with the amount of the grant measured by the amount actually disbursed by the private foundation in each year or divided equally between years, at the option of the private foundation. The same method of measuring the annual amount must be used in all years of a grant. This paragraph (a)(6)(ii) applies without regard to whether the public charity has made the election under section 501(h).

(iii) **RELiance UPON GRANTEE'S BUDGET.** For purposes of determining the amount budgeted by a prospective grantee for specific project activities that are not attempts to influence legislation under paragraph (a)(6)(ii) of this section, a private foundation may rely on budget documents or other sufficient evidence supplied by the grantee organization (such as a signed statement by an authorized officer, director or trustee of such grantee organization) showing the proposed budget of the specific project, unless the private foundation doubts or, in light of all the facts and circumstances, reasonably should doubt the accuracy or reliability of the documents.

(7) GRANTS TO ORGANIZATIONS THAT CEASE TO BE DESCRIBED IN 501(c)(3) - (i) NOT TAXABLE EXPENDITURE: CONDITIONS. A grant to a public charity (as defined in paragraph (a)(6)(i) of this section) that thereafter ceases to be an organization described in section 501(c)(3) by reason of its attempts to influence legislation is not a taxable expenditure if -

(A) The grant meets the requirements of paragraph (a)(6) of this section.

(B) The recipient organization had received a ruling or determination letter, or an advance ruling or determination letter, that it is described in sections 501(c)(3) and 509(a).

(C) Notice of a change in the recipient organization's status has not been made to the public (such as by publication in the Internal Revenue Bulletin), and the private foundation has not acquired knowledge that the Internal Revenue Service has given notice to the recipient organization that it will be deleted from such status; and

(D) The recipient organization is not controlled directly or indirectly by the private foundation. A recipient organization is controlled by a private foundation for this purpose if the private foundation and disqualified persons (defined in section 4946(a)(1)(A) through (H)) with reference to the private foundation, by aggregating their votes or positions of authority, can cause or prevent action on legislative issues by the recipient.

(ii) EXAMPLES. The provisions of paragraphs (a)(6) and (a)(7) of this section are illustrated by the following examples:

EXAMPLE (1). W, a private foundation, makes a general support grant to Z, a public charity described in section 509(a)(1). Z informs W that, as an insubstantial portion of its activities, Z attempts to influence the State legislature with regard to changes in the mental health laws. The use of the grant is not earmarked by W to be used in a manner that would violate section 4945(d)(1). Even if the grant is subsequently devoted by Z to its legislative activities, the grant by W is not a taxable expenditure under section 4945(d).

EXAMPLE (2). X, a private foundation, makes a specific project grant to Y University for the purpose of conducting research on the potential environmental effects of certain pesticides. X does not earmark the grant for any purpose that would violate section 4945(d)(1) and there is no oral or written agreement or understanding whereby X may cause Y to engage in any activity described in section 4945(d)(1), (2), or (3), or to select any recipient to which the grant may be devoted. Further, X determines, based on budget information supplied by Y, that Y's budget for the project does not contain any amount for attempts to influence legislation. X has no reason to doubt the accuracy or reliability of the budget information. Y uses most of the funds for the research project; however, Y expends a portion of the grant funds to send a representative to testify at Congressional hearings on a specific bill proposing certain pesticide control measures. The portion of the grant funds expended with respect to the Congressional hearings is not treated as a taxable expenditure by X under section 4945(d)(1).

EXAMPLE (3). M, a private foundation, makes a specific project grant of \$150,000 to P, a public charity described in section 509(a)(1). In requesting the grant from M, P stated that the total budgeted cost of the project is \$200,000, and that of this amount \$20,000 is allocated to attempts to influence legislation related to the project. M relies on the budget figures provided by P in determining the amount P will spend on influencing legislation and M has no reason to doubt the accuracy or reliability of P's

budget figures. In making the grant, M did not earmark any of the funds from the grant to be used for attempts to influence legislation. M's grant of \$150,000 to P will not constitute a taxable expenditure under section 4945(d)(1) because M did not earmark any of the funds for attempts to influence legislation and because the amount of its grant (\$150,000) does not exceed the amount allocated to specific project activities that are not attempts to influence legislation (\$200,000 - \$20,000 = \$180,000).

EXAMPLE (4). Assume the same facts as in example (3), except that M's grant letter to P provides that M has the right to renegotiate the terms of the grant if there is a substantial deviation from those terms. This additional fact does not make M's grant a taxable expenditure under section 4945(d)(1).

EXAMPLE (5). Assume the same facts as in example (3), except that M made a specific project grant of \$200,000 to P. Part of M's grant of \$200,000 will constitute a taxable expenditure under section 4945(d)(1). The amount of the grant (\$200,000) exceeds by \$20,000 the amount P allocated to specific project activities that are not attempts to influence legislation (\$180,000). M has made a taxable expenditure of \$20,000.

EXAMPLE (6). Assume the same facts as example (3), except that M made a specific project grant of \$180,000, and received from P an enforceable commitment that grant funds would not be used in connection with attempts to influence legislation. M's grant is not a taxable expenditure under section 4945(d)(1).

EXAMPLE (7). Assume the same facts as in example (3) except that M directed P to hire A, an individual, to expend \$20,000 from the grant to engage in direct lobbying (within the meaning of section 56.4911-2(b)) and grass roots lobbying (within the meaning of section 56.4911-2(c)). P does not expend any other grant funds for lobbying activities. The \$20,000 that is earmarked for direct lobbying and grass roots lobbying is a taxable expenditure under section 4945(d)(1).

EXAMPLE (8). R, a public charity described in section 509(a)(1), requested N, a private foundation, to make a general purpose grant to it to aid R in carrying out its exempt purpose. In making this request, R notified N that it had elected the expenditure test under section 501(h) and that it expected to attempt to influence legislation in areas related to its exempt purpose. Since its formation, R generally has had exempt purpose expenditures (as defined in section 56.4911-4) in excess of \$7,000,000 in each of its taxable years, and has budgeted in excess of \$7,000,000 of exempt purpose expenditures for the year of the grant. N made a grant of \$200,000 to R. N did not earmark the funds for R's attempt to influence legislation. The general purpose grant by N does not constitute a taxable expenditure under section 4945(d)(1).

EXAMPLE (9). Assume the same facts as in example (8), except that N learns that R has had excess lobbying expenditures (within the meaning of section 56.4911-1(b)) in some prior years. N also learns that in no year has R's lobbying or grass roots expenditures (within the meaning of section 56.4911-2(a) and (c)) exceeded the corresponding ceiling amount (within the meaning of section 1.501(h)-3(c)(3) and (6)). N then makes the grant to R. After receiving the grant, R spends a large portion of its funds on influencing legislation and, as a consequence, is denied exemption from tax, as an organization described in section 501(c)(3), under section 501(h) and section 1.501(h)-3. No disqualified person with respect to N controlled, in whole or in part, R's attempts to influence

legislation. The general purpose grant will not constitute a taxable expenditure under section 4945(d)(1).

EXAMPLE (10). X, a private foundation, makes a specific project grant to Y, a public charity described in section 509(a). In requesting the grant, Y stated that it planned to use the funds to purchase a computer for purposes of computerizing its research files and that the grant will not be used to influence legislation. Two years after X makes the grant, X discovers that Y has also used the computer for purposes of maintaining and updating the mailing list for Y's lobbying newsletter. Because X did not earmark any of the grant funds to be used for attempts to influence legislation and because X had no reason to doubt the accuracy or reliability of Y's documents representing that the grant would not be used to influence legislation, X's grant is not treated as a taxable expenditure.

EXAMPLE (11). G, a private foundation, makes a specific project grant of \$300,000 to L, a public charity described in section 509(a)(1) for a three-year specific project studying child care problems. L provides budget material indicating that the specific project will expend \$200,000 in each of three years. L's budget materials indicate that attempts to influence legislation will amount to \$10,000 in the first year, \$20,000 in the second year, and \$100,000 in the third year. G intends to pay its \$300,000 grant over three years as follows: \$200,000 in the first year, \$50,000 in the second year and \$50,000 in the third year. The amount of the grant actually disbursed by G in the first year of the grant exceeds the nonlobbying expenditures of L in that year. However, because the amount of the grant in each of the three years, when divided equally among the three years (\$100,000 for each year), is not more than the nonlobbying expenditures of L on the specific project for any of the three years, none of the grant is treated as a taxable expenditure under section 4945(d)(1).

EXAMPLE (12). P, a private foundation, makes a \$120,000 specific project grant to C, a public charity described in section 509(a) for a three-year project. P intends to pay its grant to C in three equal annual installments of \$40,000. C provides budget material indicating that the specific project will expend \$100,000 in each of three years. C's budget materials, which P reasonably does not doubt, indicate that the project's attempts to influence legislation will amount to \$50,000 in each of the three years. After P pays the first annual installment to C, but before P pays the second installment to C, reliable information comes to P's attention that C has spent \$90,000 of the project's \$100,000 first-year budget on attempts to influence legislation. This information causes P to doubt the accuracy and reliability of C's budget materials. Because of the information, P does not pay the second-year installment to C. P's payment of the first installment of \$40,000 is not a taxable expenditure under section 4945(d)(1) because the grant in the first year is not more than the nonlobbying expenditures C projected in its budget materials that P reasonably did not doubt.

EXAMPLE (13). Assume the same facts as in Example (12), except that P pays the second-year installment of \$40,000 to C. In the project's second year, C once again spends \$90,000 of the project's \$100,000 annual budget in attempts to influence legislation. Because P doubts or reasonably should doubt the accuracy or reliability of C's budget materials when P makes the second-year grant payment, P may not rely upon C's budget documents at that time. Accordingly, although none of the \$40,000 paid in the first installment is a taxable expenditure, only \$10,000 (\$100,000 minus \$90,000) of the second-year grant payment is not a taxable expenditure. The remaining

\$30,000 of the second installment is a taxable expenditure within the meaning of section 4945(d)(1).

EXAMPLE (14). B, a private foundation, makes a specific project grant to C, a public charity described in section 509(a), of \$40,000 for the purpose of conducting a study on the effectiveness of seat belts in preventing traffic deaths. B did not earmark any of the grant for attempts to influence legislation. In requesting the grant from B, C submitted a budget of \$100,000 for the project. The budget contained expenses for postage and mailing, computer time, advertising, consulting services, salaries, printing, advertising, and similar categories of expenses. C also submitted to B a statement, signed by an officer of C, that 30% of the budgeted funds would be devoted to attempts to influence legislation within the meaning of section 4945. B has no reason to doubt the accuracy of the budget figures or the statement. B may rely on the budget figures and signed statement provided by C in determining the amount C will spend on influencing legislation. B's grant to C will not constitute a taxable expenditure under section 4945(d)(1), because the amount of the grant does not exceed the amount allocated to specific project activities that are not attempts to influence legislation.

(b) [Reserved]

(c) [Reserved]

(d) **EXCEPTIONS — (1) NONPARTISAN ANALYSIS, STUDY, OR RESEARCH — (i) IN GENERAL.** A communication is not a lobbying communication, for purposes of section 53.4945-2(a)(1), if the communication constitutes engaging in nonpartisan analysis, study or research and making available to the general public or a segment or members thereof or to governmental bodies, officials, or employees the results of such work. Accordingly, an expenditure for such a communication does not constitute a taxable expenditure under section 4945(d)(1) and section 53.4945-2(a)(1).

(ii) **NONPARTISAN ANALYSIS, STUDY, OR RESEARCH.** For purposes of section 4945(e), "nonpartisan analysis, study, or research" means an independent and objective exposition of a particular subject matter, including any activity that is "educational" within the meaning of section 1.501(c)(3)-1(d)(3). Thus, "nonpartisan analysis, study, or research" may advocate a particular position or viewpoint so long as there is a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent opinion or conclusion. On the other hand, the mere presentation of unsupported opinion does not qualify as "nonpartisan analysis, study, or research".

(iv) **MAKING AVAILABLE RESULTS OF NONPARTISAN ANALYSIS, STUDY, OR RESEARCH.** * * * For purposes of this paragraph (d)(1)(iv), such communications may not be limited to, or be directed toward, persons who are interested solely in one side of a particular issue.

(v) **SUBSEQUENT LOBBYING USE OF CERTAIN ANALYSIS, STUDY OR RESEARCH — (A) IN GENERAL.** Even though certain analysis, study or research is initially within the exception for nonpartisan analysis, study or research, subsequent use of that analysis, study or research for grass roots lobbying may cause that analysis, study or research to be treated as a grass roots lobbying communication that is not within the exception for nonpartisan analysis, study or research. This paragraph (d)(1)(v) of this section does not cause any analysis, study or research to be considered a direct lobbying communication. For rules regarding when analysis, study

or research is treated as a grass roots lobbying communication that is not within the scope of the exception for nonpartisan analysis, study or research, see section 56.4911-2(b)(2)(v).

(B) SPECIAL RULE FOR GRANTS TO PUBLIC CHARITIES. This paragraph (d)(1)(v)(B) of this section applies where a public charity uses a private foundation grant to finance, in whole or in part, a nonlobbying communication that is subsequently used in lobbying, causing the public charity's expenditures for the communication to be treated as lobbying expenditures under the subsequent use rule. In such a case, the private foundation's grant will ordinarily not be characterized as a lobbying expenditure by virtue of the subsequent use rule. The only situations where the private foundation's grant will be treated as a lobbying expenditure under the subsequent use rule are where the private foundation's primary purpose in making the grant to the public charity was for lobbying or where, at the time of making the grant, the private foundation knows (or in light of all the facts and circumstances reasonably should know) that the public charity's primary purpose in preparing the communication to be funded by the grant is for use in lobbying.

(vi) DIRECTLY ENCOURAGING ACTION BY RECIPIENTS OF A COMMUNICATION. A communication that reflects a view on specific legislation is not within the nonpartisan analysis, study or research exception of this section 53.4945-2(d)(1) if the communication directly encourages the recipient to take action with respect to such legislation. For purposes of this section, a communication directly encourages the recipient to take action with respect to legislation if the communication is described in one or more of section 56.4911-2(b)(2)(iii)(A) through (C). As described in section 56.4911-2(b)(2)(iv), a communication would encourage the recipient to take action with respect to legislation, but not DIRECTLY encourage such action, if the communication does no more than specifically identify one or more legislators who will vote on the legislation as: opposing the communication's view with respect to the legislation; being undecided with respect to the legislation; being the recipient's representative in the legislature; or being a member of the legislative committee or subcommittee that will consider the legislation.

(vii) EXAMPLES. * * *

EXAMPLE (4). P publishes a bi-monthly newsletter to collect and report all published materials, ongoing research, and new developments with regard to the use of pesticides in raising crops. The newsletter also includes notices of proposed pesticide legislation with impartial summaries of the provisions and debates on such legislation. The newsletter does not encourage recipients to take action with respect to such legislation, but is designed to present information on both sides of the legislative controversy and does present such information fully and fairly. It is within the exception for nonpartisan analysis, study, or research.

EXAMPLE (5). X is satisfied that A, a member of the faculty of Y University, is exceptionally well qualified to undertake a project involving a comprehensive study of the effects of pesticides on crop yields. Consequently, X makes a grant to A to underwrite the cost of the study and of the preparation of a book on the effect of pesticides on crop yields. X does not take any position on the issues or control the content of A's output. A produces a book which concludes that the use of pesticides often has a favorable effect on crop yields, and on that basis argues against pending bills which would ban the use of pesticides. A's book contains a sufficiently full and fair exposition of the

pertinent facts, including known or potential disadvantages of the use of pesticides, to enable the public or an individual to form an independent opinion or conclusion as to whether pesticides should be banned as provided in the pending bills. The book does not directly encourage readers to take action with respect to the pending bills. Consequently, the book is within the exception for nonpartisan analysis, study, or research.

* * * * *

EXAMPLE (8). Organization Z researches, writes, prints and distributes a study on the use and effects of pesticide X. A bill is pending in the U.S. Senate to ban the use of pesticide X. Z's study leads to the conclusion that pesticide X is extremely harmful and that the bill pending in the U.S. Senate is an appropriate and much needed remedy to solve the problems caused by pesticide X. The study contains a sufficiently full and fair exposition of the pertinent facts, including known or potential advantages of the use of pesticide X, to enable the public or an individual to form an independent opinion or conclusion as to whether pesticides should be banned as provided in the pending bills. In its analysis of the pending bill, the study names certain undecided Senators on the Senate committee considering the bill. Although the study meets the three part test for determining whether a communication is a grass roots lobbying communication, the study is within the exception for nonpartisan analysis, study or research, because it does not directly encourage recipients of the communication to urge a legislator to oppose the bill.

EXAMPLE (9). Assume the same facts as in Example (8), except that, after stating support for the pending bill, the study concludes: "You should write to the undecided committee members to support this crucial bill." The study is not within the exception for nonpartisan analysis, study or research because it directly encourages the recipients to urge a legislator to support a specific piece of legislation.

EXAMPLE (10). Organization X plans to conduct a lobbying campaign with respect to illegal drug use in the United States. It incurs \$5,000 in expenses to conduct research and prepare an extensive report primarily for use in the lobbying campaign. Although the detailed report discusses specific pending legislation and reaches the conclusion that the legislation would reduce illegal drug use, the report contains a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent conclusion regarding the effect of the legislation. The report does not encourage readers to contact legislators regarding the legislation. Accordingly, the report does not, in and of itself, constitute a lobbying communication.

Copies of the report are available to the public at X's office, but X does not actively distribute the report or otherwise seek to make the contents of the report available to the general public. Whether or not X's distribution is sufficient to meet the requirement in section 53.4945-2(d)(1)(iv) that a nonpartisan communication be made available, X's distribution is not substantial (for purposes of sections 53.4945-2(d)(1)(v) and 56.4911-2(b)(2)(v)) in light of all of the facts and circumstances, including the normal distribution pattern of similar nonpartisan reports. X then mails copies of the report, along with a letter, to 10,000 individuals on X's mailing list. In the letter, X requests that individuals contact legislators urging passage of the legislation discussed in the report. Because X's research and report were primarily undertaken by X for lobbying purposes and X did not make a substantial distribution of the report (without an accompanying lobbying message) prior to or contemporaneously with the use of the report in lobbying, the report is a grass roots

lobbying communication that is not within the exception for nonpartisan analysis, study or research. Thus, the expenditures for preparing and mailing both the report and the letter are taxable expenditures under section 4945.

EXAMPLE (11). Assume the same facts as in Example (10), except that before using the report in the lobbying campaign, X sends the research and report (without an accompanying lobbying message) to universities and newspapers. At the same time, X also advertises the availability of the report in its newsletter. This distribution is similar in scope to the normal distribution pattern of similar nonpartisan reports. In light of all of the facts and circumstances, X's distribution of the report is substantial. Because of X's substantial distribution of the report, X's primary purpose will be considered to be other than for use in lobbying and the report will not be considered a grass roots lobbying communication. Accordingly, only the expenditures for copying and mailing the report to the 10,000 individuals on X's mailing list, as well as for preparing and mailing the letter, are expenditures for grass roots lobbying communications, and are thus taxable expenditures under section 4945.

EXAMPLE (12). Organization M pays for a bumper sticker that reads: "STOP ABORTION: Vote NO on Prop. X." M also pays for a 30-second television advertisement and a billboard that similarly advocate opposition to Prop. X. In light of the limited scope of the communications, none of the communications is within the exception for nonpartisan analysis, study or research. First, none of the communications rises to the level of analysis, study or research. Second, none of the communications is nonpartisan because none contains a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent opinion or conclusion. Thus, each communication is a lobbying communication.

(2) TECHNICAL ADVICE OR ASSISTANCE -- (i) *

(iii) EXAMPLES. ***

EXAMPLE (5). In response to a telephone inquiry from Senator X's staff, organization B sends Senator X a report concluding that the Senate should not advise and consent to the nomination of Z to serve as a Supreme Court Justice. Because the request was not in writing, and also because the request was not from the Senate itself or from a committee or subcommittee, B's report is not within the scope of the exception for responses to requests for technical advice. Accordingly, B's report is a lobbying communication unless the report is within the scope of the exception for nonpartisan analysis, study or research.

EXAMPLE (6). Assume the same facts as in Example (5), except that B's report is sent in response to a written request that Senator X sends to B. The request from Senator X is a request from the Senator as an individual member of the Senate rather than from the Senate itself or from a committee or subcommittee. Accordingly, B's report is not within the scope of the exception for responses to requests for technical advice and is a lobbying communication unless the report is within the scope of the exception for nonpartisan analysis, study or research.

EXAMPLE (7). Assume the same facts as in Example (6), except that B's report is sent in response to a written request from the Senate committee that is considering the nomination for an evaluation of the nominee's legal writings and a recommendation as to whether the candidate is or is not qualified to serve on the Supreme Court. The report is within the scope of the exception for responses to

requests for technical advice and is not a lobbying communication.

(4) EXAMINATIONS AND DISCUSSIONS OF BROAD SOCIAL, ECONOMIC, AND SIMILAR PROBLEMS. Examinations and discussions of broad social, economic, and similar problems are neither direct lobbying communications under section 56.4911-2(b)(1) nor grass roots lobbying communications under section 56.4911-2(b)(2) even if the problems are of the type with which government would be expected to deal ultimately. Thus, under sections 56.4911-2(b)(1) and (2), lobbying communications do not include public discussion, or communications with members of legislative bodies or governmental employees, the general subject of which is also the subject of legislation before a legislative body, so long as such discussion does not address itself to the merits of a specific legislative proposal and so long as such discussion does not directly encourage recipients to take action with respect to legislation. For example, this paragraph (d)(4) excludes from grass roots lobbying under section 56.4911-2(b)(2) an organization's discussions of problems such as environmental pollution or population growth that are being considered by Congress and various State legislatures, but only where the discussions are not directly addressed to specific legislation being considered, and only where the discussions do not directly encourage recipients of the communication to contact a legislator, an employee of a legislative body, or a government official or employee who may participate in the formulation of legislation.

Par. 17. Part 56 is added to read as follows:

PART 56 -- PUBLIC CHARITY EXCISE TAXES

Sec.

- 56.4911-0 Outline of regulations under section 4911.
- 56.4911-1 Tax on excess lobbying expenditures.
- 56.4911-2 Lobbying expenditures, direct lobbying communications, and grass roots lobbying communications.
- 56.4911-3 Expenditures for direct and/or grass roots lobbying communications.
- 56.4911-4 Exempt purpose expenditures.
- 56.4911-5 Communications with members.
- 56.4911-6 Records of lobbying and grass roots expenditures.
- 56.4911-7 Affiliated group of organizations.
- 56.4911-8 Excess lobbying expenditures of affiliated group.
- 56.4911-9 Application of section 501(h) to affiliated groups of organizations.
- 56.4911-10 Members of a limited affiliated group of organizations.
- 56.6001-1 Notice or regulations requiring records, statements, and special returns.
- 56.6011-1 General requirement of return, statement, or list.

AUTHORITY: 26 U.S.C. 7805, Sec. 56.4911-7 also issued under 26 U.S.C. 4911(f)(3).

SECTION 56.4911-0 OUTLINE OF REGULATIONS UNDER SECTION 4911.

Immediately following is an outline of the regulations under section 4911 of the Internal Revenue Code relating to an excise tax on electing public charities' excess lobbying expenditures.

SECTION 56.4911-0 OUTLINE OF REGULATIONS UNDER SECTION 4911.

SECTION 56.4911-1 TAX ON EXCESS LOBBYING EXPENDITURES.

- (a) In general.
- (b) Excess lobbying expenditures.
- (c) Nontaxable amounts.
 - (1) Lobbying nontaxable amount.
 - (2) Grass roots nontaxable amount.
- (d) Examples.

SECTION 56.4911-2 LOBBYING EXPENDITURES, DIRECT LOBBYING COMMUNICATIONS, AND GRASS ROOTS LOBBYING COMMUNICATIONS.

- (a) Lobbying expenditures.
 - (1) In general.
 - (2) Overview of section 56.4911 and the definitions of "direct lobbying communication" and "grass roots lobbying communication".
- (b) Influencing legislation: direct and grass roots lobbying communications defined.
 - (1) Direct lobbying communication.
 - (2) Grass roots lobbying communication.
 - (3) Exceptions to the definition of influencing legislation.
 - (4) Examples.
 - (5) Special rule for certain mass media advertisements.
- (c) Exceptions to the definitions of direct lobbying communication and grass roots lobbying communication.
 - (1) Nonpartisan analysis, study, or research exception.
 - (2) Examinations and discussions of broad social, economic, and similar problems.
 - (3) Requests for technical advice.
 - (4) Communications pertaining to "self-defense" by the organization.
- (d) Definitions.
 - (1) Legislation.
 - (2) Action.
 - (3) Legislative body.
 - (4) Administrative bodies.

SECTION 56.4911-3 EXPENDITURES FOR DIRECT AND/OR GRASS ROOTS LOBBYING COMMUNICATIONS.

- (a) Definition of term "expenditures for".
 - (1) In general.
 - (2) Allocation of mixed purpose expenditures.
 - (3) Allocation of mixed lobbying.
- (b) Examples.
- (c) Certain transfers treated as lobbying expenditures.
 - (1) Transfer earmarked for grass roots purposes.
 - (2) Transfer earmarked for direct and grass roots lobbying.
 - (3) Certain transfers to noncharities that lobby.

SECTION 56.4911-4 EXEMPT PURPOSE EXPENDITURES.

- (a) Application.
- (b) Included expenditures.
- (c) Excluded expenditures.
- (d) Certain transfers treated as exempt purpose expenditures.
- (e) Transfers not exempt purpose expenditures.
- (f) Definitions.
- (g) Example.

SECTION 56.4911-5 COMMUNICATIONS WITH MEMBERS.

- (a) In general.
- (b) Communications (directed only to members) that are not lobbying communications.
- (c) Communications (directed only to members) that are direct lobbying communications.
- (d) Communications (directed only to members) that are grass roots lobbying communications.
- (e) Written communications directed to members and nonmembers.
 - (1) In general.
 - (2) Direct lobbying directly encouraged.
 - (3) Grass roots expenditure if grass roots lobbying directly encouraged.
 - (4) No direct encouragement of direct lobbying or of grass roots lobbying.
- (f) Definitions and special rules.
 - (1) Member: general rule.
 - (2) Member: special rule.
 - (3) Member: affiliated group of organizations.
 - (4) Member: limited affiliated group of organizations.
 - (5) Subscriber.
 - (6) Directly encourages.
 - (7) Percentages of total distribution.
 - (8) Reasonable allocation rule.

SECTION 56.4911-6 RECORDS OF LOBBYING AND GRASS ROOTS EXPENDITURES.

- (a) Records of lobbying expenditures.
- (b) Records of grass roots expenditures.

SECTION 56.4911-7 AFFILIATED GROUP OF ORGANIZATIONS.

- (a) Affiliation between two organizations.
 - (1) In general.
 - (2) Organizations not described in section 501(c)(3).
 - (3) Action on legislative issues.
- (b) Interlocking governing boards.
 - (1) In general.
 - (2) Majority or quorum.
 - (3) Votes required under governing instrument or local law.
 - (4) Representatives constituting less than 15% of governing board.
 - (5) Representatives.
- (c) Governing instrument.
- (d) Three or more organizations affiliated.
 - (1) Two controlled organizations affiliated.
 - (2) Chain rule.

- (e) **Affiliated group of organizations.**
 - (1) Defined.
 - (2) Multiple membership.
 - (3) Taxable year of affiliated group.
 - (4) Electing member organization.
 - (5) Election of member's year as group's taxable year.
- (f) **Examples.**

SECTION 56.4911-8 EXCESS LOBBYING EXPENDITURES OF AFFILIATED GROUP.

- (a) **Application.**
- (b) **Affiliated group treated as one organization.**
- (c) **Tax imposed on excess lobbying expenditures of affiliated group.**
- (d) **Liability for tax.**
 - (1) **Electing organizations.**
 - (2) **Tax based on excess lobbying expenditures.**
 - (3) **Tax based on excess grass roots expenditures.**
 - (4) **Tax based on exempt purpose expenditures.**
 - (5) **Taxable year for which liable.**
 - (6) **Organization a member of more than one affiliated group.**
- (e) **Former member organization.**

SECTION 56.4911-9 APPLICATION OF SECTION 501(H) TO AFFILIATED GROUPS OF ORGANIZATIONS.

- (a) **Scope.**
- (b) **Determination required.**
- (c) **Member organizations that are not electing organizations.**
- (d) **Filing of information relating to affiliated group of organizations.**
 - (1) **Scope.**
 - (2) **In general.**
 - (3) **Additional information required.**
 - (4) **Information required of electing member organization.**
- (e) **Example.**
- (f) **Cross reference.**

SECTION 56.4911-10 MEMBERS OF A LIMITED AFFILIATED GROUP OF ORGANIZATIONS.

- (a) **Scope.**
- (b) **Members of limited affiliated group.**
- (c) **Controlling and controlled organizations.**
- (d) **Expenditures of controlling organization.**
 - (1) **Scope.**
 - (2) **Expenditures for direct lobbying.**
 - (3) **Grass roots expenditures.**
 - (4) **Exempt purpose expenditures.**
- (e) **Expenditures of controlled member.**
- (f) **Reports of members of limited affiliated groups.**
 - (1) **Controlling member organization's additional information on annual return.**
 - (2) **Reports of controlling members to other members.**
 - (3) **Reports of controlled member organizations.**
- (g) **National legislative issues.**
- (h) **Examples.**

SECTION 56.6001-1 NOTICE OR REGULATIONS REQUIRING RECORDS, STATEMENTS, AND SPECIAL RETURNS.

- (a) **In general.**
- (b) **Cross references.**

SECTION 56.6011-1 GENERAL REQUIREMENT OF RETURN, STATEMENT, OR LIST.

SECTION 56.4911-1 TAX ON EXCESS LOBBYING EXPENDITURES.

(a) **IN GENERAL.** Section 4911(a) imposes an excise tax of 25 percent on the excess lobbying expenditures (as defined in paragraph (b) of this section) for a taxable year of an organization for which the expenditure test election under section 501(h) is in effect (an "electing public charity"). An electing public charity's annual limit on expenditures for influencing legislation (i.e., the amount of lobbying expenditures on which no tax is due) is the lobbying nontaxable amount or, on expenditures for influencing legislation through grass roots lobbying, the grass roots nontaxable amount (see paragraph (c) of this section). For rules concerning the application of the excise tax imposed by section 4911(a) to the members of an affiliated group of organizations (as defined in section 56.4911-7(e)), see section 56.4911-8.

(b) **EXCESS LOBBYING EXPENDITURES.** For any taxable year for which the expenditure test election under section 501(h) is in effect, the amount of an electing public charity's excess lobbying expenditures is the greater of --

(1) The amount by which the organization's lobbying expenditures (within the meaning of section 56.4911-2(a)) exceed the organization's lobbying nontaxable amount, or

(2) The amount by which the organization's grass roots expenditures (within the meaning of sections 56.4911-2(a)) exceed the organization's grass roots nontaxable amount.

(c) **NONTAXABLE AMOUNTS -- (1) LOBBYING NONTAXABLE AMOUNT.** Under section 4911(c)(2), the lobbying nontaxable amount for any taxable year for which the expenditure test election is in effect is the lesser of --

(i) \$1,000,000, or

(ii) To the extent of the electing public charity's exempt purpose expenditures (within the meaning of section 56.4911-4) for that year, the sum of 20 percent of the first \$500,000 of such expenditures, plus 15 percent of the second \$500,000 of such expenditures, plus 10 percent of the third \$500,000 of such expenditures, plus 5 percent of the remainder of such expenditures.

(2) **GRASS ROOTS NONTAXABLE AMOUNT.** Under section 4911(c)(4), an electing public charity's grass roots nontaxable amount for any taxable year is 25 percent of its lobbying nontaxable amount for that year.

(d) **EXAMPLES.** The provisions of this section are illustrated by the examples in section 1.501(h)-3.

SECTION 56.4911-2 LOBBYING EXPENDITURES, DIRECT LOBBYING COMMUNICATIONS, AND GRASS ROOTS LOBBYING COMMUNICATIONS.

(a) **LOBBYING EXPENDITURES -- (1) IN GENERAL.** An electing public charity's lobbying expenditures for a year are the sum of its expenditures during that year for direct lobbying communications ("direct lobbying expenditures") plus its expenditures during that year for grass roots lobbying communications ("grass roots expenditures").

(2) OVERVIEW OF SECTION 56.4911-2 AND THE DEFINITIONS OF "DIRECT LOBBYING COMMUNICATION" AND "GRASS ROOTS LOBBYING COMMUNICATION". Paragraph (b)(1) of this section defines the term "direct lobbying communication." Paragraph (b)(2) of this section provides the general definition of the term "grass roots lobbying communication." (But also see paragraph (b)(5) of this section (special rebuttable presumption regarding certain paid mass media communications) and section 56.4911-5 (special, more lenient, definitions for certain communications from an electing public charity to its bona fide members). Paragraph (b)(3) of this section lists and cross-references various exceptions to the definitions set forth in paragraphs (b)(1) and (2) (the text of the exceptions, along with relevant definitions and examples, is generally set forth in paragraph (c)). Paragraph (b)(4) of this section contains numerous examples illustrating the application of paragraphs (b)(1), (2) and (3). As mentioned above, paragraph (b)(5) of this section sets forth the special rebuttable presumption regarding a limited number of paid mass media communications about highly publicized legislation. Paragraph (d) of this section contains definitions of (and examples illustrating) various terms used in this section.

(b) INFLUENCING LEGISLATION: DIRECT AND GRASS ROOTS LOBBYING COMMUNICATIONS DEFINED - (1) DIRECT LOBBYING COMMUNICATION - (i) DEFINITION. A direct lobbying communication is any attempt to influence any legislation through communication with:

- (A) Any member or employee of a legislative body; or
- (B) Any government official or employee (other than a member or employee of a legislative body) who may participate in the formulation of the legislation, but only if the principal purpose of the communication is to influence legislation.

(ii) REQUIRED ELEMENTS. A communication with a legislator or government official will be treated as a direct lobbying communication under this section 56.4911-2(b)(1) if, but only if, the communication:

- (A) Refers to specific legislation (see paragraph (d)(1) of this section for a definition of the term "specific legislation"); and
- (B) Reflects a view on such legislation.

(iii) SPECIAL RULE FOR REFERENDA, BALLOT INITIATIVES OR SIMILAR PROCEDURES. Solely for purposes of this section 4911, where a communication refers to and reflects a view on a measure that is the subject of a referendum, ballot initiative or similar procedure, the general public in the state or locality where the vote will take place constitutes the legislative body, and individual members of the general public are, for purposes of this paragraph (b)(1), legislators. Accordingly, if such a communication is made to one or more members of the general public in that state or locality, the communication is a direct lobbying communication (unless it is nonpartisan analysis, study or research (see paragraph (c)(1) of this section).

(2) GRASS ROOTS LOBBYING COMMUNICATION - (i) DEFINITION. A grass roots lobbying communication is any attempt to influence any legislation through an attempt to affect the opinions of the general public or any segment thereof.

(ii) REQUIRED ELEMENTS. A communication will be treated as a grass roots lobbying communication under

this section 56.4911-2(b)(2)(ii) if, but only if, the communication:

- (A) Refers to specific legislation (see paragraph (d)(1) of this section for a definition of the term "specific legislation");
- (B) Reflects a view on such legislation; and
- (C) Encourages the recipient of the communication to take action with respect to such legislation (see paragraph (b)(2)(iii) of this section for the definition of encouraging the recipient to take action).

For special, more lenient rules regarding an organization's communications directed only or primarily to bona fide members of the organization, see section 56.4911-5. For special rules regarding certain paid mass media advertisements about highly publicized legislation, see paragraph (b)(5) of this section. For special rules regarding lobbying on referenda, ballot initiatives and similar procedures, see paragraph (b)(1)(iii) of this section.

(iii) DEFINITION OF ENCOURAGING RECIPIENT TO TAKE ACTION. For purposes of this section, encouraging a recipient to take action with respect to legislation means that the communication:

(A) States that the recipient should contact a legislator or an employee of a legislative body, or should contact any other government official or employee who may participate in the formulation of legislation (but only if the principal purpose of urging contact with the government official or employee is to influence legislation).

(B) States the address, telephone number, or similar information of a legislator or an employee of a legislative body;

(C) Provides a petition, tear-off postcard or similar material for the recipient to communicate with a legislator or an employee of a legislative body, or with any other government official or employee who may participate in the formulation of legislation (but only if the principal purpose of so facilitating contact with the government official or employee is to influence legislation); or

(D) Specifically identifies one or more legislators who will vote on the legislation as: opposing the communication's view with respect to the legislation; being undecided with respect to the legislation; being the recipient's representative in the legislature; or being a member of the legislative committee or subcommittee that will consider the legislation. Encouraging the recipient to take action under this paragraph (b)(2)(iii)(D) does not include naming the main sponsor(s) of the legislation for purposes of identifying the legislation.

(iv) DEFINITION OF ENCOURAGING RECIPIENT TO TAKE ACTION. Communications described in one or more of paragraphs (b)(2)(iii)(A) through (C) of this section not only "encourage," but also "directly encourage" the recipient to take action with respect to legislation. Communications described in paragraph (b)(2)(iii)(D) of this section, however, do not directly encourage the recipient to take action with respect to legislation. Thus, a communication would encourage the recipient to take action with respect to legislation, but not DIRECTLY encourage such action, if the communication does no more than identify one or more legislators who will vote on the legislation as: opposing the communication's view with respect to the legislation; being undecided with respect to the legislation; being the recipient's representative in the legislature; or being a member of the legislative committee or subcommittee that will consider the legislation. Communications that encourage the recipient to take action with respect to legislation but that do not DIRECTLY

encourage the recipient to take action with respect to legislation may be within the exception for nonpartisan analysis, study or research (see paragraph (c)(1) of this section) and thus not be grass roots lobbying communications.

(v) **SUBSEQUENT LOBBYING USE OF NONLOBBYING COMMUNICATIONS OR RESEARCH MATERIALS - (A) LIMITED EFFECT OF APPLICATION.** Even though certain communications or research materials are initially not grass roots lobbying communications under the general definition set forth in paragraph (b)(2)(ii) of this section, subsequent use of the communications or research materials for grass roots lobbying may cause them to be treated as grass roots lobbying communications. This paragraph (b)(2)(v) does not cause any communications or research materials to be considered direct lobbying communications.

(B) **LIMITED SCOPE OF APPLICATION.** Under this paragraph (b)(2)(v), only "ADVOCACY communications or research materials" are potentially treated as grass roots lobbying communications. Communications or research materials that are not "ADVOCACY communications or research materials" are not treated as grass roots lobbying communications under this paragraph (b)(2)(v). "Advocacy communications or research materials" are any communications or materials that both refer to and reflect a view on specific legislation but that do not, in their initial format, contain a direct encouragement for recipients to take action with respect to legislation.

(C) **SUBSEQUENT USE IN LOBBYING.** Where advocacy communications or research materials are subsequently accompanied by a direct encouragement for recipients to take action with respect to legislation, the advocacy communications or research materials themselves are treated as grass roots lobbying communications unless the organization's primary purpose in undertaking or preparing the advocacy communications or research materials was not for use in lobbying. In such a case, all expenses of preparing and distributing the advocacy communications or research materials will be treated as grass roots expenditures.

(D) **TIME LIMIT ON APPLICATION OF SUBSEQUENT USE RULE.** The characterization of expenditures as grass roots lobbying expenditures under paragraph (b)(2)(v)(C) shall apply only to expenditures paid less than six months before the first use of the advocacy communications or research materials with a direct encouragement to action.

(E) **SAFE HARBOR IN DETERMINING "PRIMARY PURPOSE".** The primary purpose of the organization in undertaking or preparing advocacy communications or research materials will not be considered to be for use in lobbying if, prior to or contemporaneously with the use of the advocacy communications or research materials with the direct encouragement to action, the organization makes a substantial nonlobbying distribution of the advocacy communications or research materials (without the direct encouragement to action). Whether a distribution is substantial will be determined by reference to all of the facts and circumstances, including the normal distribution pattern of similar nonpartisan analyses, studies or research by that and similar organizations.

(F) **SPECIAL RULE FOR PARTISAN ANALYSIS, STUDY OR RESEARCH.** In the case of advocacy communications or research materials that are not nonpartisan analysis, study or research, the nonlobbying distribution thereof will not be considered "substantial"

unless that distribution is at least as extensive as the lobbying distribution thereof.

(G) **FACTORS CONSIDERED IN DETERMINING PRIMARY PURPOSE.** Where the nonlobbying distribution of advocacy communications or research materials is not substantial, all of the facts and circumstances must be weighed to determine whether the organization's primary purpose in preparing the advocacy communications or research materials was for use in lobbying. While not the only factor, the extent of the organization's nonlobbying distribution of the advocacy communications or research materials is particularly relevant, especially when compared to the extent of their distribution with the direct encouragement to action. Another particularly relevant factor is whether the lobbying use of the advocacy communications or research materials is by the organization that prepared the document, a related organization, or an unrelated organization. Where the subsequent lobbying distribution is made by an unrelated organization, clear and convincing evidence (which must include evidence demonstrating cooperation or collusion between the two organizations) will be required to establish that the primary purpose for preparing the communication was for use in lobbying.

(H) **EXAMPLES.** The provisions of this paragraph (b)(2)(v) are illustrated by the following examples:

EXAMPLE (1). Assume a nonlobbying "report" (that is not nonpartisan analysis, study or research) is prepared by an organization, but distributed to only 50 people. The report, in that format, refers to and reflects a view on specific legislation but does not contain a direct encouragement for the recipients to take action with respect to legislation. Two months later, the organization sends the report to 10,000 people along with a letter urging recipients to write their Senators about the legislation discussed in the report. Because the report's nonlobbying distribution is not as extensive as its lobbying distribution, the report's nonlobbying distribution is not substantial for purposes of this paragraph (b)(2)(v). Accordingly, the organization's primary purpose in preparing the report must be determined by weighing all of the facts and circumstances. In light of the relatively minimal nonlobbying distribution and the fact that the lobbying distribution is by the preparing organization rather than by an unrelated organization, and in the absence of evidence to the contrary, both the report and the letter are grass roots lobbying communications. Assume that all costs of preparing the report were paid within the six months preceding the mailing of the letter. Accordingly, all of the organization's expenditures for preparing and mailing the two documents are grass roots lobbying expenditures.

EXAMPLE (2). Assume the same facts as in Example (1), except that the costs of the report are paid over the two month period of January and February. Between January 1 and 31, the organization pays \$1,000 for the report. In February, the organization pays \$500 for the report. Further assume that the report is first used with a direct encouragement to action on August 1. Six months prior to August 1 is February 1. Accordingly, no costs paid for the report before February 1 are treated as grass roots lobbying expenditures under the subsequent use rule. Under these facts, the subsequent use rule treats only the \$500 paid for the report in February as grass roots lobbying expenditures.

(3) **EXCEPTIONS TO THE DEFINITION OF INFLUENCING LEGISLATION.** In many cases, a communication is not a direct or grass roots lobbying communication under paragraph (b)(1) or (b)(2) of this section if it falls within one of the exceptions listed in paragraph (c) of this section. See paragraph (c)(1).

NONPARTISAN ANALYSIS, STUDY OR RESEARCH; paragraph (c)(2). EXAMINATIONS AND DISCUSSIONS OF BROAD SOCIAL, ECONOMIC AND SIMILAR PROBLEMS; paragraph (c)(3). REQUESTS FOR TECHNICAL ADVICE; and paragraph (c)(4), COMMUNICATIONS PERTAINING TO SELF-DEFENSE BY THE ORGANIZATION. In addition, see section 56.4911-5, which provides special rules regarding the treatment of certain lobbying communications directed in whole or in part to members of an electing public charity.

(4) **EXAMPLES.** This paragraph (b)(4) provides examples to illustrate the rules set forth in this section regarding direct and grass roots lobbying. The expenditure test election under section 501(h) is assumed to be in effect for all organizations discussed in the examples in this paragraph (b)(4). In addition, it is assumed that the special rules of section 56.4911-5, regarding certain of a public charity's communications with its members, do not apply to any of the examples in this paragraph (b)(4).

(i) **DIRECT LOBBYING.** The provisions of this section regarding direct lobbying communications are illustrated by the following examples:

EXAMPLE (1). Organization P's employee, X, is assigned to approach members of Congress to gain their support for a pending bill. X drafts and P prints a position letter on the bill. P distributes the letter to members of Congress. Additionally, X personally contacts several members of Congress or their staffs to seek support for P's position on the bill. The letter and the personal contacts are direct lobbying communications.

EXAMPLE (2). Organization M's president writes a letter to the Congresswoman representing the district in which M is headquartered, requesting that the Congresswoman write an administrative agency regarding proposed regulations recently published by that agency. M's president also requests that the Congresswoman's letter to the agency state the Congresswoman's support of M's application for a particular type of permit granted by the agency. The letter written by M's president is not a direct lobbying communication.

EXAMPLE (3). Organization Z prepares a paper on a particular state's environmental problems. The paper does not reflect a view on any specific pending legislation or on any specific legislative proposal that Z either supports or opposes. Z's representatives give the paper to a state legislator. Z's paper is not a direct lobbying communication.

EXAMPLE (4). State X enacts a statute that requires the licensing of all day care providers. Agency B in State X is charged with preparing rules to implement the bill enacted by State X. One week after enactment of the bill, organization C sends a letter to Agency B providing detailed proposed rules that organization C suggests to Agency B as the appropriate standards to follow in implementing the statute on licensing of day care providers. Organization C's letter to Agency B is not a lobbying communication.

EXAMPLE (5). 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. Because 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, separate from any legislative requirement, the research, preparation, printing and public distribution of the code of standards is not an expenditure for a direct (or grass roots) lobbying communication. Costs, such as transportation, photocopying, and other similar expenses, incurred in lobbying state legislators for passage of the code of standards into law are expenditures for direct lobbying communications.

EXAMPLE (6). On the organization's own initiative, representatives of Organization F present written testimony to a Congressional committee. The news media report on the testimony of Organization F, detailing F's opposition to a pending bill. The testimony is a direct lobbying communication but is not a grass roots lobbying communication.

EXAMPLE (7). Organization R's monthly newsletter contains an editorial column that refers to and reflects a view on specific pending bills. R sends the newsletter to 10,000 nonmember subscribers. Senator Doe is among the subscribers. The editorial column in the newsletter copy sent to Senator Doe is not a direct lobbying communication because the newsletter is sent to Senator Doe in her capacity as a subscriber rather than her capacity as a legislator. (Note, though, that the editorial column may be a grass roots lobbying communication if it encourages recipients to take action with respect to the pending bills it refers to and on which it reflects a view).

EXAMPLE (8) Assume the same facts as in Example (7), except that one of Senator Doe's staff members sees Senator Doe's copy of the editorial and writes to R requesting additional information. R responds with a letter that refers to and reflects a view on specific legislation. R's letter is a direct lobbying communication unless it is within one of the exceptions set forth in paragraph (c) of this section (such as the exception for nonpartisan analysis, study or research). (R's letter is not within the scope of the exception for responses to written requests from a legislative body or committee for technical advice (see paragraph (c)(3) of this section) because the letter is not in response to a written request from a legislative body or committee).

(ii) **GRASS ROOTS LOBBYING.** The provisions of this section regarding grass roots lobbying communications are illustrated in paragraph (b)(4)(i)(A) of this section by examples of communications that are not grass roots lobbying communications and in paragraph (b)(4)(i)(B) by examples of communications that are grass roots lobbying communications. The provisions of this section are further illustrated in paragraph (b)(4)(ii)(C), with particular regard to the exception for nonpartisan analysis, study, or research:

(A) COMMUNICATIONS THAT ARE NOT GRASS ROOTS LOBBYING COMMUNICATIONS.

EXAMPLE (1). Organization L places in its newsletter an article that asserts that lack of new capital is hurting State W's economy. The article recommends that State W residents either invest more in local businesses or increase their savings so that funds will be available to others interested in making investments. The article is an attempt to influence opinions with respect to a general problem that might receive legislative attention and is distributed in a manner so as to reach and influence many individuals. However, the article does not refer to specific legislation that is pending in a legislative body, nor does the article refer to a specific legislative proposal the organization

either supports or opposes. The article is not a grass roots lobbying communication.

EXAMPLE (2). Assume the same facts as Example (1), except that the article refers to a bill pending in State W's legislature that is intended to provide tax incentives for private savings. The article praises the pending bill and recommends that it be enacted. However, the article does not encourage readers to take action with respect to the legislation. The article is not a grass roots lobbying communication.

EXAMPLE (3). Organization B sends a letter to all persons on its mailing list. The letter includes an update on numerous environmental issues with a discussion of general concerns regarding pollution, proposed federal regulations affecting the area, and several pending legislative proposals. The letter endorses two pending bills and opposes another pending bill, but does not name any legislator involved (other than the sponsor of one bill, for purposes of identifying the bill), nor does it otherwise encourage the reader to take action with respect to the legislation. The letter is not a grass roots lobbying communication.

EXAMPLE (4). A pamphlet distributed by organization Z discusses the dangers of drugs and encourages the public to send their legislators a coupon, printed with the statement "I support a drug-free America." The term "drug-free America" is not widely identified with any of the many specific pending legislative proposals regarding drug issues. The pamphlet does not refer to any of the numerous pending legislative proposals, nor does the organization support or oppose a specific legislative proposal. The pamphlet is not a grass roots lobbying communication.

EXAMPLE (5). A pamphlet distributed by organization B encourages readers to join an organization and "get involved in the fight against drugs." The text states, in the course of a discussion of several current drug issues, that organization B supports a specific bill before Congress that would establish an expanded drug control program. The pamphlet does not encourage readers to communicate with legislators about the bill (such as by including the names of undecided or opposed legislators). The pamphlet is not a grass roots lobbying communication.

EXAMPLE (6). Organization E, an environmental organization, routinely summarizes in each edition of its newsletter the new environment-related bills that have been introduced in Congress since the last edition of the newsletter. The newsletter identifies each bill by a bill number and the name of the legislation's sponsor. The newsletter also reports on the status of previously introduced environment-related bills. The summaries and status reports do not encourage recipients of the newsletter to take action with respect to legislation, as described in paragraphs (b)(2)(iii)(A) through (D) of this section. Although the summaries and status reports refer to specific legislation and often reflect a view on such legislation, they do not encourage the newsletter recipients to take action with respect to such legislation. The summaries and status reports are not grass roots lobbying communications.

EXAMPLE (7). Organization B prints in its newsletter a report on pending legislation that B supports, the Family Equity bill. The report refers to and reflects a view on the Family Equity bill, but does not directly encourage recipients to take action. Nor does the report specifically identify any legislator as opposing the communication's view on the legislation, as being undecided, or as being a member of the legislative committee or subcommittee that will consider the legislation. However, the report does state the following:

Rep. Doe (D-Ky.) and Rep. Roe (R-Ma.), both ardent supporters of the Family Equity bill, spoke at B's annual convention last week. Both encouraged B's efforts to get the Family Equity bill enacted and stated that they thought the bill could be enacted even over a presidential veto. B's legislative affairs liaison questioned others, who seemed to agree with that assessment. For example, Sen. Roe (I-Ca.) said that he thinks the bill will pass with such a large majority, "the President won't even consider vetoing it."

Assume the newsletter, and thus the report, is sent to individuals throughout the U.S., including some recipients in Kentucky, Massachusetts and California. Because the report is distributed nationally, the mere fact that the report identifies several legislators by party and state as part of its discussion does not mean the report specifically identifies the named legislators as the Kentucky, Massachusetts and California recipients' representatives in the legislature for purposes of paragraph (b)(2)(iii) of this section. The report is not a grass roots lobbying communication.

(B) COMMUNICATIONS THAT ARE GRASS ROOTS LOBBYING COMMUNICATIONS.

EXAMPLE (1). A pamphlet distributed by organization Y states that the "President's plan for a drug-free America," which will establish a drug control program, should be passed. The pamphlet encourages readers to "write or call your senators and representatives and tell them to vote for the President's plan." No legislative proposal formally bears the name "President's plan for a drug-free America," but that and similar terms have been widely used in connection with specific legislation pending in Congress that was initially proposed by the President. Thus, the pamphlet refers to specific legislation, reflects a view on the legislation, and encourages readers to take action with respect to the legislation. The pamphlet is a grass roots lobbying communication.

EXAMPLE (2). Assume the same facts as in Example (1), except that the pamphlet does not encourage the public to write or call representatives, but does list the members of the committee that will consider the bill. The pamphlet is a grass roots lobbying communication.

EXAMPLE (3). Assume the same facts as in Example (1), except that the pamphlet encourages readers to "write the President to urge him to make the bill a top legislative priority" rather than encouraging readers to communicate with members of Congress. The pamphlet is a grass roots lobbying communication.

EXAMPLE (4). Organization B, a nonmembership organization, includes in one of three sections of its newsletter an endorsement of two pending bills and opposition to another pending bill and also identifies several legislators as undecided on the three bills. The section of the newsletter devoted to the three pending bills is a grass roots lobbying communication.

EXAMPLE (5). Organization D, a nonmembership organization, sends a letter to all persons on its mailing list. The letter includes an extensive discussion concluding that a significant increase in spending for the Air Force is essential in order to provide an adequate defense of the nation. Prior to a concluding fundraising request, the letter encourages readers to write their Congressional representatives urging increased appropriations to build the B-1 bomber. The letter is a grass roots lobbying communication.

EXAMPLE (6). The President nominates X for a position in the President's cabinet. Organization Y disagrees with the views of X and does not believe X has the necessary administrative capabilities to effectively run a cabinet-level department. Accordingly, Y sends a general

mailing requesting recipients to write to four Senators on the Senate Committee that will consider the nomination. The mailing is a grass roots lobbying communication.

EXAMPLE (7). Organization F mails letters requesting that each recipient contribute money to or join F. In addition, the letters express F's opposition to a pending bill that is to be voted upon by the U.S. House of Representatives. Although the letters are form letters sent as a mass mailing, each letter is individualized to report to the recipient the name of the recipient's congressional representative. The letters are grass roots lobbying communications.

EXAMPLE (8) Organization C sends a mailing that opposes a specific legislative proposal and includes a postcard addressed to the President for the recipient to sign stating opposition to the proposal. The letter requests that the recipient send to C a contribution as well as the postcard opposing the proposal. C states in the letter that it will deliver all the postcards to the White House. The letter is a grass roots lobbying communication.

(C) ADDITIONAL EXAMPLES.

EXAMPLE (1). The newsletter of an organization concerned with drug issues is circulated primarily to individuals who are not members of the organization. A story in the newsletter reports on the prospects for passage of a specifically identified bill, stating that the organization supports the bill. The newsletter story identifies certain legislators as undecided, but does not state that readers should contact the undecided legislators. The story does not provide a full and fair exposition sufficient to qualify as nonpartisan analysis, study or research. The newsletter story is a grass roots lobbying communication.

EXAMPLE (2). Assume the same facts as in Example (1), except that the newsletter story provides a full and fair exposition sufficient to qualify as nonpartisan analysis, study or research. The newsletter story is NOT a grass roots lobbying communication because it is within the exception for nonpartisan analysis, study or research (since it does not DIRECTLY encourage recipients to take action).

EXAMPLE (3). Assume the same facts as in Example (2), except that the newsletter story explicitly asks readers to contact the undecided legislators. Because the newsletter story directly encourages readers to take action with respect to the legislation, the newsletter story is not within the exception for nonpartisan analysis, study or research. Accordingly, the newsletter story is a grass roots lobbying communication.

EXAMPLE (4). Assume the same facts as in Example (1), except that the story does not identify any undecided legislators. The story is not a grass roots lobbying communication.

EXAMPLE (5). X organization places an advertisement that specifically identifies and opposes a bill that X asserts would harm the farm economy. The advertisement is not a mass media communication described in paragraph (b)(5)(ii) of this section and does not directly encourage readers to take action with respect to the bill. However, the advertisement does state that Senator Y favors the legislation. Because the advertisement refers to and reflects a view on specific legislation, and also encourages the readers to take action with respect to the legislation by specifically identifying a legislator who opposes X's views on the legislation, the advertisement is a grass roots lobbying communication.

EXAMPLE (6). Assume the same facts as in Example (5), except that instead of identifying Senator Y as

favoring the legislation, the advertisement identifies the "junior Senator from State Z" as favoring the legislation. The advertisement is a grass roots lobbying communication.

EXAMPLE (7). Assume the same facts as in Example (5), except that instead of identifying Senator Y as favoring the legislation, the advertisement states: "Even though this bill will have a devastating effect upon the farm economy, most of the Senators from the Farm Belt states are inexplicably in favor of the bill." The advertisement does not specifically identify one or more legislators as opposing the advertisement's view on the bill in question. Accordingly, the advertisement is not a grass roots lobbying communication because it does not encourage readers to take action with respect to the legislation.

EXAMPLE (8). Organization V trains volunteers to go door-to-door to seek signatures for petitions to be sent to legislators in favor of a specific bill. The volunteers are wholly unreimbursed for their time and expenses. The volunteers' costs (to the extent any are incurred) are not lobbying or exempt purpose expenditures made by V (but the volunteers may not deduct their out-of-pocket expenditures (see section 170(f)(6)). When V asks the volunteers to contact others and urge them to sign the petitions, V encourages those volunteers to take action in favor of the specific bill. Accordingly, V's costs of soliciting the volunteers' help and its costs of training the volunteers are grass roots expenditures. In addition, the costs of preparing, copying, distributing, etc. the petitions (and any other materials on the same specific subject used in the door-to-door signature gathering effort), are grass roots expenditures.

(5) SPECIAL RULE FOR CERTAIN MASS MEDIA ADVERTISEMENTS - (i) IN GENERAL. A mass media advertisement that is not a grass roots lobbying communication under the three-part grass roots lobbying definition contained in paragraph (b)(2) of this section may be a grass roots lobbying communication by virtue of paragraph (b)(5)(ii) of this section. The special rule in paragraph (b)(5)(ii) generally applies only to a limited type of paid advertisements that appear in the mass media.

(ii) PRESUMPTION REGARDING CERTAIN PAID MASS MEDIA ADVERTISEMENTS ABOUT HIGHLY PUBLICIZED LEGISLATION. If within two weeks before a vote by a legislative body, or a committee (but not a subcommittee) thereof, on a highly publicized piece of legislation, an organization's paid advertisement appears in the mass media, the paid advertisement will be presumed to be a grass roots lobbying communication, but only if the paid advertisement both reflects a view on the general subject of such legislation and either: refers to the highly publicized legislation; or encourages the public to communicate with legislators on the general subject of such legislation. An organization can rebut this presumption by demonstrating that the paid advertisement is a type of communication regularly made by the organization in the mass media without regard to the timing of legislation (that is, a customary course of business exception) or that the timing of the paid advertisement was unrelated to the upcoming legislative action. Notwithstanding the fact that an organization successfully rebuts the presumption, a mass media communication described in this paragraph (b)(5)(ii) is a grass roots lobbying communication if the communication would be a grass roots lobbying communication under the rules contained in paragraph (b)(2) of this section.

(iii) DEFINITIONS - (A) MASS MEDIA. For purposes of this paragraph (b)(5), the term "mass media"

means television, radio, billboards and general circulation newspapers and magazines. General circulation newspapers and magazines do not include newspapers or magazines published by an organization for which the expenditure test election under section 501(h) is in effect, except where both: the total circulation of the newspaper or magazine is greater than 100,000; and fewer than one-half of the recipients are members of the organization (as defined in section 56.4911-5(f)).

(B) **PAID ADVERTISEMENT.** For purposes of this paragraph (b)(5), where an electing public charity is itself a mass media publisher or broadcaster, all portions of that organization's mass media publications or broadcasts are treated as paid advertisements in the mass media, except those specific portions that are advertisements paid for by another person. The term "mass media" is defined in paragraph (b)(5)(iii)(A).

(C) **HIGHLY PUBLICIZED.** For purposes of this paragraph (b)(5), "highly publicized" means frequent coverage on television and radio, and in general circulation newspapers, during the two weeks preceding the vote by the legislative body or committee. In the case of state or local legislation, "highly publicized" means frequent coverage in the mass media that serve the state or local jurisdiction in question. Even where legislation receives frequent coverage, it is "highly publicized" only if the pendency of the legislation or the legislation's general terms, purpose, or effect are known to a significant segment of the general public (as opposed to the particular interest groups directly affected) in the area in which the paid mass media advertisement appears.

(iv) **EXAMPLES.** The special rule of this paragraph (b)(5) is illustrated by the following examples. The expenditure test election under section 501(h) is assumed to be in effect for all organizations discussed in the examples in this paragraph (b)(5)(iv):

EXAMPLE (1). Organization X places a television advertisement advocating one of the President's major foreign policy initiatives, as outlined by the President in a series of speeches and as drafted into proposed legislation. The initiative is popularly known as "the President's World Peace Plan," and is voted upon by the Senate four days after X's advertisement. The advertisement concludes: "SUPPORT THE PRESIDENT'S WORLD PEACE PLAN" The President's plan and position are highly publicized during the two weeks before the Senate vote, as evidenced by: coverage of the plan on several nightly television network news programs; more than one article about the plan on the front page of a majority of the country's ten largest daily general circulation newspapers; and an editorial about the plan in four of the country's ten largest daily general circulation newspapers. Although the advertisement does not encourage readers to contact legislators or other government officials, the advertisement does refer to specific legislation and reflect a view on the general subject of the legislation. The communication is presumed to be a grass roots lobbying communication.

EXAMPLE (2). Assume the same facts as in Example (1), except that the advertisement appears three weeks before the Senate's vote on the plan. Because the advertisement appears more than two weeks before the legislative vote, the advertisement is NOT within the scope of the special rule for mass media communications on highly publicized legislation. Accordingly, the advertisement is a grass roots lobbying communication only if it is described in the general definition contained in paragraph (b)(2) of this section. Because the advertisement does not encourage recipients to take action with respect to

the legislation in question, the advertisement is not a grass roots lobbying communication.

EXAMPLE (3). Organization Y places a newspaper advertisement advocating increased government funding for certain public works projects the President has proposed and that are being considered by a legislative committee. The advertisement explains the President's proposals and concludes: "SUPPORT FUNDING FOR THESE VITAL PROJECTS!" The advertisement does not encourage readers to contact legislators or other government officials nor does it name any undecided legislators, but it does name the legislation being considered by the committee. The President's proposed funding of public works, however, is not highly publicized during the two weeks before the vote: there has been little coverage of the issue on nightly television network news programs, only one front-page article on the issue in the country's ten largest daily general circulation newspapers, and only one editorial about the issue in the country's ten largest daily general circulation newspapers. Two days after the advertisement appears, the committee votes to approve funding of the projects. Although the advertisement appears less than two weeks before the legislative vote, the advertisement is not within the scope of the special rule for mass media communications on highly publicized legislation because the issue of funding for public works projects is not highly publicized. Thus, the advertisement is a grass roots lobbying communication only if it is described in the general definition contained in paragraph (b)(2) of this section. Because the advertisement does not encourage recipients to take action with respect to the legislation in question, the advertisement is not a grass roots lobbying communication.

EXAMPLE (4). Organization P places numerous advertisements in the mass media about a bill being considered by the State Assembly. The bill is highly publicized, as evidenced by numerous front-page articles, editorials and letters to the editor published in the state's general circulation daily newspapers, as well as frequent coverage of the bill by the television and radio stations serving the state. The advertisements run over a three week period and, in addition to showing pictures of a family being robbed at gunpoint, say: "The State Assembly is considering a bill to make gun ownership illegal. This outrageous legislation would violate your constitutional rights and the rights of other law-abiding citizens. If this legislation is passed, you and your family will be criminals if you want to exercise your right to protect yourselves." The advertisements refer to and reflect a view on a specific bill but do not encourage recipients to take action. Sixteen days after the last advertisement runs, a State Assembly committee votes to defeat the legislation. None of the advertisements is a grass roots lobbying communication.

EXAMPLE (5). Assume the same facts as in Example (4), except that it is publicly announced prior to the advertising campaign that the committee vote is scheduled for five days after the last advertisement runs. Because of public pressure resulting from the advertising campaign, the bill is withdrawn and no vote is ever taken. None of the advertisements is a grass roots lobbying communication.

(c) **EXCEPTIONS TO THE DEFINITIONS OF DIRECT LOBBYING COMMUNICATION AND GRASS ROOTS LOBBYING COMMUNICATION - (1) NONPARTISAN ANALYSIS, STUDY, OR RESEARCH EXCEPTION - (i)** In general, Engaging in nonpartisan analysis, study, or research and making available to the general public or a segment or members thereof or to governmental bodies, officials, or employees the results of such work constitute neither a direct lobbying

communication under section 56.4911-2(b)(1) nor a grass roots lobbying communication under section 56.4911-2(b)(2).

(ii) **NONPARTISAN ANALYSIS, STUDY, OR RESEARCH.** For purposes of this section, "nonpartisan analysis, study, or research" means an independent and objective exposition of a particular subject matter, including any activity that is "educational" within the meaning of section 1.501(c)(3)-1(d)(3). Thus, "nonpartisan analysis, study, or research" may advocate a particular position or viewpoint so long as there is a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent opinion or conclusion. The mere presentation of unsupported opinion, however, does not qualify as "nonpartisan analysis, study, or research".

(iii) **PRESENTATION AS PART OF A SERIES.** Normally, whether a publication or broadcast qualifies as "nonpartisan analysis, study, or research" will be determined on a presentation-by-presentation basis. However, if a publication or broadcast is one of a series prepared or supported by an electing organization and the series as a whole meets the standards of paragraph (c)(1)(ii) of this section, then any individual publication or broadcast within the series is not a direct or grass roots lobbying communication even though such individual broadcast or publication does not, by itself, meet the standards of paragraph (c)(1)(ii) of this section. Whether a broadcast or publication is considered part of a series will ordinarily depend upon all the facts and circumstances of each particular situation. However, with respect to broadcast activities, all broadcasts within any period of six consecutive months will ordinarily be eligible to be considered as part of a series. If an electing organization times or channels a part of a series which is described in this paragraph (c)(1)(iii) in a manner designed to influence the general public or the action of a legislative body with respect to a specific legislative proposal, the expenses of preparing and distributing such part of the analysis, study, or research will be expenditures for a direct or grass roots lobbying communication, as the case may be.

(iv) **MAKING AVAILABLE RESULTS OF NONPARTISAN ANALYSIS, STUDY, OR RESEARCH.** An organization may choose any suitable means, including oral or written presentations, to distribute the results of its nonpartisan analysis, study, or research, with or without charge. Such means include distribution of reprints of speeches, articles and reports; presentation of information through conferences, meetings and discussions; and dissemination to the news media, including radio, television and newspapers, and to other public forums. For purposes of this paragraph (c)(1)(iv), such communications may not be limited to, or be directed toward, persons who are interested solely in one side of a particular issue.

(v) **SUBSEQUENT LOBBYING USE OF CERTAIN ANALYSIS, STUDY OR RESEARCH.** Even though certain analysis, study or research is initially within the exception for nonpartisan analysis, study or research, subsequent use of that analysis, study or research for grass roots lobbying may cause that analysis, study or research to be treated as a grass roots lobbying communication that is not within the exception for nonpartisan analysis, study or research. This paragraph (c)(1)(v) does not cause any analysis, study or research to be considered a direct lobbying communication. For rules regarding when analysis, study or research is treated as a grass roots lobbying communication that is not within the scope of the exception for nonpartisan analysis, study or research, see paragraph (b)(2)(v) of this section.

(vi) **DIRECTLY ENCOURAGING ACTION BY RECIPIENTS OF A COMMUNICATION.** A communication that reflects a view on specific legislation is not within the nonpartisan analysis, study, or research exception of this paragraph (c)(1) if the communication directly encourages the recipient to take action with respect to such legislation. For purposes of this section, a communication directly encourages the recipient to take action with respect to legislation if the communication is described in one or more of paragraphs (b)(2)(iii)(A) through (C) of this section. As described in paragraph (b)(2)(iv) of this section, a communication would encourage the recipient to take action with respect to legislation, but not **DIRECTLY** encourage such action, if the communication does no more than specifically identify one or more legislators who will vote on the legislation as: opposing the communication's view with respect to the legislation; being undecided with respect to the legislation; being the recipient's representative in the legislature; or being a member of the legislative committee or subcommittee that will consider the legislation.

(vii) **EXAMPLES.** The provisions of this paragraph (c)(1) may be illustrated by the following examples:

EXAMPLE (1). Organization M establishes a research project to collect information for the purpose of showing the dangers of the use of pesticides in raising crops. The information collected includes data with respect to proposed legislation, pending before several State legislatures, which would ban the use of pesticides. The project takes favorable positions on such legislation without producing a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent opinion or conclusion on the pros and cons of the use of pesticides. This project is not within the exception for nonpartisan analysis, study, or research because it is designed to present information merely on one side of the legislative controversy.

EXAMPLE (2). Organization N establishes a research project to collect information concerning the dangers of the use of pesticides in raising crops for the ostensible purpose of examining and reporting information as to the pros and cons of the use of pesticides in raising crops. The information is collected and distributed in the form of a published report which analyzes the effects and costs of the use and nonuse of various pesticides under various conditions on humans, animals and crops. The report also presents the advantages, disadvantages, and economic cost of allowing the continued use of pesticides unabated, of controlling the use of pesticides, and of developing alternatives to pesticides. Even if the report sets forth conclusions that the disadvantages as a result of using pesticides are greater than the advantages of using pesticides and that prompt legislative regulation of the use of pesticides is needed, the project is within the exception for nonpartisan analysis, study, or research since it is designed to present information on both sides of the legislative controversy and presents a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent opinion or conclusion.

EXAMPLE (3). Organization O establishes a research project to collect information on the presence or absence of disease in humans from eating food grown with pesticides and the presence or absence of disease in humans from eating food not grown with pesticides. As part of the research project, O hires a consultant who prepares a "fact sheet" which calls for the curtailment of the use of pesticides and which addresses itself to the merits of several specific legislative proposals to curtail the use of

pesticides in raising crops which are currently pending before State Legislatures. The "fact sheet" presents reports of experimental evidence tending to support its conclusions but omits any reference to reports of experimental evidence tending to dispute its conclusions. O distributes ten thousand copies to citizens' groups. Expenditures by O in connection with this work of the consultant are not within the exception for nonpartisan analysis, study, or research.

EXAMPLE (4). P publishes a bi-monthly newsletter to collect and report all published materials, ongoing research, and new developments with regard to the use of pesticides in raising crops. The newsletter also includes notices of proposed pesticide legislation with impartial summaries of the provisions and debates on such legislation. The newsletter does not encourage recipients to take action with respect to such legislation, but is designed to present information on both sides of the legislative controversy and does present such information fully and fairly. It is within the exception for nonpartisan analysis, study, or research.

EXAMPLE (5). X is satisfied that A, a member of the faculty of Y University, is exceptionally well qualified to undertake a project involving a comprehensive study of the effects of pesticides on crop yields. Consequently, X makes a grant to A to underwrite the cost of the study and of the preparation of a book on the effect of pesticides on crop yields. X does not take any position on the issues or control the content of A's output. A produces a book which concludes that the use of pesticides often has a favorable effect on crop yields, and on that basis argues against pending bills which would ban the use of pesticides. A's book contains a sufficiently full and fair exposition of the pertinent facts, including known or potential disadvantages of the use of pesticides, to enable the public or an individual to form an independent opinion or conclusion as to whether pesticides should be banned as provided in the pending bills. The book does not directly encourage readers to take action with respect to the pending bills. Consequently, the book is within the exception for nonpartisan analysis, study, or research.

EXAMPLE (6). Assume the same facts as Example (2), except that, instead of issuing a report, X presents within a period of 6 consecutive months a two-program television series relating to the pesticide issue. The first program contains information, arguments, and conclusions favoring legislation to restrict the use of pesticides. The second program contains information, arguments, and conclusions opposing legislation to restrict the use of pesticides. The programs are broadcast within 6 months of each other during commensurate periods of prime time. X's programs are within the exception for nonpartisan analysis, study, or research. Although neither program individually could be regarded as nonpartisan, the series of two programs constitutes a balanced presentation.

EXAMPLE (7). Assume the same facts as in Example (6), except that X arranged for televising the program favoring legislation to restrict the use of pesticides at 8:00 on a Thursday evening and for televising the program opposing such legislation at 7:00 on a Sunday morning. X's presentation is not within the exception for nonpartisan analysis, study, or research, since X disseminated its information in a manner prejudicial to one side of the legislative controversy.

EXAMPLE (8). Organization Z researches, writes, prints and distributes a study on the use and effects of pesticide X. A bill is pending in the U.S. Senate to ban the use of pesticide X. Z's study leads to the conclusion that pesticide X is extremely harmful and that the bill pending

in the U.S. Senate is an appropriate and much needed remedy to solve the problems caused by pesticide X. The study contains a sufficiently full and fair exposition of the pertinent facts, including known or potential advantages of the use of pesticide X, to enable the public or an individual to form an independent opinion or conclusion as to whether pesticides should be banned as provided in the pending bills. In its analysis of the pending bill, the study names certain undecided Senators on the Senate committee considering the bill. Although the study meets the three part test for determining whether a communication is a grass roots lobbying communication, the study is within the exception for nonpartisan analysis, study or research, because it does not directly encourage recipients of the communication to urge a legislator to oppose the bill.

EXAMPLE (9). Assume the same facts as in Example (8), except that, after stating support for the pending bill, the study concludes: "You should write to the undecided committee members to support this crucial bill." The study is not within the exception for nonpartisan analysis, study or research because it directly encourages the recipients to urge a legislator to support a specific piece of legislation.

EXAMPLE (10). Organization X plans to conduct a lobbying campaign with respect to illegal drug use in the United States. It incurs \$5,000 in expenses to conduct research and prepare an extensive report primarily for use in the lobbying campaign. Although the detailed report discusses specific pending legislation and reaches the conclusion that the legislation would reduce illegal drug use, the report contains a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent conclusion regarding the effect of the legislation. The report does not encourage readers to contact legislators regarding the legislation. Accordingly, the report does not, in and of itself, constitute a lobbying communication.

Copies of the report are available to the public at X's office, but X does not actively distribute the report or otherwise seek to make the contents of the report available to the general public. Whether or not X's distribution is sufficient to meet the requirement in section 56.4911-2(c)(1)(iv) that a nonpartisan communication be made available, X's distribution is not substantial (for purposes of section 56.4911-2(b)(2)(v)(E)) in light of all of the facts and circumstances, including the normal distribution pattern of similar nonpartisan reports. X then mails copies of the report, along with a letter, to 10,000 individuals on X's mailing list. In the letter, X requests that individuals contact legislators urging passage of the legislation discussed in the report. Because X's research and report were primarily undertaken by X for lobbying purposes and X did not make a substantial distribution of the report (without an accompanying lobbying message) prior to or contemporaneously with the use of the report in lobbying, the report is a grass roots lobbying communication that is not within the exception for nonpartisan analysis, study or research.

EXAMPLE (11). Assume the same facts as in Example (10), except that before using the report in the lobbying campaign, X sends the research and report (without an accompanying lobbying message) to universities and newspapers. At the same time, X also advertises the availability of the report in its newsletter. This distribution is similar in scope to the normal distribution pattern of similar nonpartisan reports. In light of all of the facts and circumstances, X's distribution of the report is substantial. Because of X's substantial distribution of the report, X's primary purpose will be considered to be other than for use in lobbying and the report will not be considered a grass

roots lobbying communication. Accordingly, only the expenditures for copying and mailing the report to the 10,000 individuals on X's mailing list, as well as for preparing and mailing the letter, are expenditures for grass roots lobbying communications.

EXAMPLE (12). Organization M pays for a bumper sticker that reads: "STOP ABORTION: Vote No on Prop. X." M also pays for a 30-second television advertisement and a billboard that similarly advocate opposition to Prop. X. In light of the limited scope of the communications, none of the communications is within the exception for nonpartisan analysis, study or research. First, none of the communications rises to the level of analysis, study or research. Second, none of the communications is nonpartisan because none contains a sufficiently full and fair exposition of the pertinent facts to enable the public or an individual to form an independent opinion or conclusion. Thus, each communication is a direct lobbying communication.

(2) EXAMINATIONS AND DISCUSSIONS OF BROAD SOCIAL, ECONOMIC, AND SIMILAR PROBLEMS. Examinations and discussions of broad social, economic, and similar problems are neither direct lobbying communications under section 56.4911-2(b)(1) nor grass roots lobbying communications under section 56.4911-2(b)(2) even if the problems are of the type with which government would be expected to deal ultimately. Thus, under sections 56.4911-2(b)(1) and (2), lobbying communications do not include public discussion, or communications with members of legislative bodies or governmental employees, the general subject of which is also the subject of legislation before a legislative body, so long as such discussion does not address itself to the merits of a specific legislative proposal and so long as such discussion does not directly encourage recipients to take action with respect to legislation. For example, this paragraph (c)(2) excludes from grass roots lobbying under section 56.4911-2(b)(2) an organization's discussions of problems such as environmental pollution or population growth that are being considered by Congress and various State legislatures, but only where the discussions are not directly addressed to specific legislation being considered, and only where the discussions do not directly encourage recipients of the communication to contact a legislator, an employee of a legislative body, or a government official or employee who may participate in the formulation of legislation.

(3) REQUESTS FOR TECHNICAL ADVICE. A communication is not a direct lobbying communication under section 56.4911-2(b)(1) if the communication is the providing of technical advice or assistance to a governmental body, a governmental committee, or a subdivision of either in response to a written request by the body, committee, or subdivision, as set forth in section 53.4945-2(d)(2).

(4) COMMUNICATIONS PERTAINING TO "SELF-DEFENSE" BY THE ORGANIZATION. A communication is not a direct lobbying communication under section 56.4911-2(b)(1) if either:

(i) The communication is an appearance before, or communication with, any legislative body with respect to a possible action by the body that might affect the existence of the electing public charity, its powers and duties, its tax-exempt status, or the deductibility of contributions to the organization, as set forth in section 53.4945-2(d)(3);

(ii) The communication is by a member of an affiliated group of organizations (within the meaning of section 56.4911-7(e)), and is an appearance before, or

communication with, a legislative body with respect to a possible action by the body that might affect the existence of any other member of the group, its powers and duties, its tax-exempt status, or the deductibility of contributions to it;

(iii) The communication is by an electing public charity more than 75 percent of the members of which are other organizations that are described in section 501(c)(3), and is an appearance before, or communication with, any legislative body with respect to a possible action by the body which might affect the existence of one or more of the section 501(c)(3) member organizations, their powers, duties, or tax-exempt status, or the deductibility (under section 170) of contributions to one or more of the section 501(c)(3) member organizations, but only if the principal purpose of the appearance or communication is to defend the section 501(c)(3) member organizations (rather than the non-section 501(c)(3) member organizations); or

(iv) The communication is by an electing public charity that is a member of a limited affiliated group of organizations under section 56.4911-10, and is an appearance before, or communication with, the Congress of the United States with respect to a possible action by the Congress that might affect the existence of any member of the limited affiliated group, its powers and duties, tax-exempt status, or the deductibility of contributions to it.

(v) Under the self-defense exception of paragraphs (c)(4)(i) through (iv) of this section, a charity may communicate with an entire legislative body, with committees or subcommittees of a legislative body, with individual legislators, with legislative staff members, or with representatives of the executive branch who are involved with the legislative process, so long as such communication is limited to the prescribed subjects. Similarly, under the self-defense exception, a charity may make expenditures in order to initiate legislation if such legislation concerns only matters which might affect the existence of the charity, its powers and duties, its tax-exempt status, or the deductibility of contributions to such charity. For examples illustrating the application and scope of the self-defense exception of this paragraph (c)(4), see section 53.4945-2(d)(3)(ii).

(d) DEFINITIONS. For purposes of section 4911 and the regulations thereunder -

(1) LEGISLATION - (i) IN GENERAL. "Legislation" includes action by the Congress, any state legislature, any local council, or similar legislative body, or by the public in a referendum, ballot initiative, constitutional amendment, or similar procedure. "Legislation" includes a proposed treaty required to be submitted by the President to the Senate for its advice and consent from the time the President's representative begins to negotiate its position with the prospective parties to the proposed treaty.

(ii) DEFINITION OF SPECIFIC LEGISLATION. For purposes of paragraphs (b)(1) and (b)(2) of this section, "specific legislation" includes both legislation that has already been introduced in a legislative body and a specific legislative proposal that the organization either supports or opposes. In the case of a referendum, ballot initiative, constitutional amendment, or other measure that is placed on the ballot by petitions signed by a required number or percentage of voters, an item becomes "specific legislation" when the petition is first circulated among voters for signature.

(iii) EXAMPLES. The terms "legislation" and "specific legislation" are illustrated using the following examples:

EXAMPLE (1). A nonmembership organization includes in its newsletter an article about problems with the

use of pesticide X that states in part: "Legislation that is pending in Congress would prohibit the use of this very dangerous pesticide. Fortunately, the legislation will probably be passed. Write your congressional representatives about this important issue." This is a grass roots lobbying communication that refers to and reflects a view on specific legislation and that encourages recipients to take action with respect to that legislation.

EXAMPLE (2). An organization based in State A notes in its newsletter that State Z has passed a bill to accomplish a stated purpose and then says that State A should pass such a bill. The organization urges readers to write their legislators in favor of such a bill. No such bill has been introduced into the State A legislature. The organization has referred to and reflected a view on a specific legislative proposal and has also encouraged readers to take action thereon.

(2) ACTION. The term "action" in paragraph (d)(1)(i) of this section is limited to the introduction, amendment, enactment, defeat or repeal of Acts, bills, resolutions, or similar items.

(3) LEGISLATIVE BODY. "Legislative body" does not include executive, judicial, or administrative bodies.

(4) ADMINISTRATIVE BODIES. "Administrative bodies" includes school boards, housing authorities, sewer and water districts, zoning boards, and other similar Federal, State, or local special purpose bodies, whether elective or appointive. Thus, for example, for purposes of section 4911, the term "any attempt to influence any legislation" does not include attempts to persuade an executive body or department to form, support the formation of, or to acquire property to be used for the formation or expansion of, a public park or equivalent preserves (such as public recreation areas, game, or forest preserves, and soil demonstration areas) established or to be established by act of Congress, by executive action in accordance with an act of Congress, or by a State, municipality or other governmental unit described in section 170(c)(1), as compared with attempts to persuade a legislative body, a member thereof, or other governmental official or employee, to promote the appropriation of funds for such an acquisition or other legislative authorization of such an acquisition. Therefore, for example, an organization would not be influencing legislation for purposes of section 4911, if it proposed to a Park Authority that it purchase a particular tract of land for a new park, even though such an attempt would necessarily require the Park Authority eventually to seek appropriations to support a new park. However, in such a case, the organization would be influencing legislation, for purposes of section 4911, if it provided the Park Authority with a proposed budget to be submitted to a legislative body, unless such submission is described by one of the exceptions set forth in paragraph (c) of this section.

SECTION 56.4911-3. EXPENDITURES FOR DIRECT AND/OR GRASS ROOTS LOBBYING COMMUNICATIONS.

(A) DEFINITION OF TERM "EXPENDITURES FOR"
— (1) IN GENERAL. This section 56.4911-3 contains allocation rules regarding what portion of a lobbying communication's costs is a direct lobbying expenditure, what portion is a grass roots expenditure and what portion is, in certain cases, a nonlobbying expenditure. Except as otherwise indicated in this paragraph (a), all costs of preparing a direct or grass roots lobbying communication are included as expenditures for direct or grass roots lobbying. Expenditures for a direct or grass roots lobbying communication ("lobbying expenditures") include amounts

paid or incurred as current or deferred compensation for an employee's services attributable to the direct or grass roots lobbying communication, and the allocable portion of administrative, overhead, and other general expenditures attributable to the direct or grass roots lobbying communication. For example, except as otherwise provided in this paragraph (a), all expenditures for researching, drafting, reviewing, copying, publishing and mailing a direct or grass roots lobbying communication, as well as an allocable share of overhead expenses, are included as expenditures for direct or grass roots lobbying.

(2) ALLOCATION OF MIXED PURPOSE EXPENDITURES — (i) NONMEMBERSHIP COMMUNICATIONS. Except as provided in paragraph (a)(2)(ii) of this section, lobbying expenditures for a communication that also has a bona fide nonlobbying purpose must include all costs attributable to those parts of the communication that are on the same specific subject as the lobbying message. All costs attributable to those parts of the communication that are not on the same specific subject as the lobbying message are not included as lobbying expenditures for allocation purposes. Whether or not a portion of a communication is on the same specific subject as the lobbying message will depend on the surrounding facts and circumstances. In general, a portion of a communication will be on the same specific subject as the lobbying message if that portion discusses an activity or specific issue that would be directly affected by the specific legislation that is the subject of the lobbying message. Moreover, discussion of the background or consequences of the specific legislation, or discussion of the background or consequences of an activity or specific issue affected by the specific legislation, is also considered to be on the same specific subject as the lobbying communication.

(ii) MEMBERSHIP COMMUNICATIONS. In the case of lobbying expenditures for a communication that also has a bona fide nonlobbying purpose and that is sent only or primarily to members, an electing public charity must make a reasonable allocation between the amount expended for the lobbying purpose and the amount expended for the nonlobbying purpose. An electing public charity that includes as a lobbying expenditure only the amount expended for the specific sentence or sentences that encourage the recipient to take action with respect to legislation has not made a reasonable allocation. For purposes of this paragraph, a communication is sent only or primarily to members if more than half of the recipients of the communication are members of the electing public charity making the communication within the meaning of section 56.4911-3. See section 56.4911-5 for separate rules on communications sent only or primarily to members. Nothing in this paragraph (a) shall change any allocation required by section 56.4911-5.

(3) ALLOCATION OF MIXED LOBBYING. If a communication (to which section 56.4911-3 does not apply) is both a direct lobbying communication and a grass roots lobbying communication, the communication will be treated as a grass roots lobbying communication except to the extent that the electing public charity demonstrates that the communication was made primarily for direct lobbying purposes, in which case a reasonable allocation shall be made between the direct and the grass roots lobbying purposes served by the communication.

(b) EXAMPLES. The provisions of paragraph (a) of this section are illustrated by the following examples. Except where otherwise explicitly stated, the expenditure test election under section 501(h) is assumed to be in effect for all organizations discussed in the examples in this

paragraph (b). See section 56.4911-5 for special rules applying to the member communications described in some of the following examples.

EXAMPLE (1). Organization R makes the services of E, one of its paid executives, available to S, an organization described in section 501(c)(4) of the Code. E works for several weeks to assist S in developing materials that urge voters to contact their congressional representatives to indicate their support for specific legislation. In performing this work, E uses office space and clerical assistance provided by R. R pays full salary and benefits to E during this period and receives no reimbursement from S for these payments or for the other facilities and assistance provided. All expenditures of R, including allocable office and overhead expenses, that are attributable to this assignment are grass roots expenditures because E was engaged in an attempt to influence legislation.

EXAMPLE (2). An organization distributes primarily to nonmembers a pamphlet with two articles on unrelated subjects. The total cost of preparing, printing and mailing the pamphlet is \$11,000, \$1,000 for preparation and \$10,000 for printing and mailing. The cost of preparing one article, a nonlobbying communication, is \$600. The article is printed on three of the four pages in the pamphlet. The cost of preparing the second article, a grassroots lobbying communication that addresses only one specific subject, is \$400. This article is printed on one page of the four page pamphlet. In this situation, \$400 of preparation costs and \$2,500 (25% of \$10,000) of printing and mailing costs are expenditures for a grass roots lobbying communication.

EXAMPLE (3). Assume the same facts as in Example (2), except that the pamphlet is distributed only to members. In addition, assume the second article states that the recipient members should contact their congressional representatives. The organization allocates \$400 of preparation costs and \$2,500 of printing and mailing costs as expenditures for direct lobbying (see section 56.4911-5(c)). The allocation is reasonable for purposes of section 56.4911-3(a)(2)(ii).

EXAMPLE (4). Organization J places a full-page advertisement in a newspaper. The advertisement urges passage of pending legislation to build three additional nuclear powered submarines, and states that readers should write their Congressional representatives in favor of the legislation. The advertisement also provides a general description of J's purposes and activities, invites readers to become members of J and asks readers to contribute money to J. Except for the cost of the portion of the advertisement describing J's purposes and activities and the portion specifically seeking members and contributions, the entire cost of the advertisement is an expenditure for a grass roots lobbying communication, because the entire advertisement, except for the lines specifically describing J and specifically seeking members and contributions, is on the same specific subject as the grass roots lobbying message.

EXAMPLE (5). Assume the same facts as in Example (4), except that J places in the newspaper two separate half-page advertisements instead of one full-page advertisement. One of the two advertisements discusses the need for three additional nuclear powered submarines and urges readers to write their Congressional representatives in favor of the pending legislation to build the three submarines. The other advertisement contains only the membership and fundraising appeals, along with a general description of J's purposes and activities. The half-page advertisement urging readers to write to Congress is a

grass roots lobbying communication and all of J's expenditures for producing and placing that advertisement are expenditures for a grass roots lobbying communication. J's expenditures for the other half-page advertisement are not expenditures for a grass roots or direct lobbying communication.

EXAMPLE (6). Assume the same facts as in Example (4), except that the communication by J is in a letter mailed only to members of J, rather than in a newspaper advertisement, and the invitation to become a member of J is an invitation to join a new membership category. In addition, assume that the communication states that the member recipients should ask nonmembers to write their Congressional representatives. J allocates one-half of the cost of the mailing as an expenditure for a grass roots lobbying communication (see section 56.4911-5(d)). Because the communication had both bona fide nonlobbying (e.g., membership solicitation and fundraising) purposes as well as lobbying purposes, J's allocation of one-half of the cost of the communication to grass roots lobbying and one-half to nonlobbying is reasonable for purposes of section 56.4911-3(a)(2)(ii).

EXAMPLE (7). A particular monthly issue of organization X's newsletter, which is distributed mainly to nonmembers of X, has three articles of equal length. The first article is a grass roots lobbying communication, the sole specific subject of which is pending legislation to help protect seals from being slaughtered in certain foreign countries. The second article discusses the rapid decline in the world's whale population, particularly because of the illegal hunting of whales by foreign countries. The third article deals with air pollution and the acid rain problem in North America. Because the first article is a grass roots lobbying communication, all of the costs allocable to that article (e.g., one-third of the newsletter's printing and mailing costs) are lobbying expenditures. The second article is not a lobbying communication and the pending legislation relating to seals addressed in the first article does not affect the illegal whale hunting activities. Because the second and third articles are not lobbying communications and are also not on the same specific subject as the first article, no portion of the costs attributable to those articles is a grass roots lobbying expenditure.

EXAMPLE (8). Organization T, a nonmembership organization, prepares a three page document that is mailed to 3,000 persons on T's mailing list. The first two pages of the three page document, titled "The Need for Child Care," support the need for additional child care programs, and include statistics on the number of children living in homes where both parents work or in homes with a single parent. The two pages also make note of the inadequacy of the number of day care providers to meet the needs of these parents. The third page of the document, titled "H.R. 1," indicates T's support of H.R. 1, a bill pending in the U.S. House of Representatives. The document states that H.R. 1 will provide for \$10,000,000 in additional subsidies to child care providers, primarily for those providers caring for lower income children. The third page of the document also notes that H.R. 1 includes new federal standards regulating the quality of child care providers. The document ends with T's request that recipients contact their congressional representative in support of H.R. 1. The entire three page document is on the same specific subject, and, therefore, all expenditures of preparing and distributing the three page document are grass roots lobbying expenditures.

EXAMPLE (9). Assume the same facts as in Example (8), except that the document has a fourth page. The fourth

page does not refer to the general need for child care or the specific need for additional child care providers. Instead, the fourth page advocates that a particular federal agency commence, under its existing statutory authority, licensing of day care providers in order to promote safe and effective child care. The cost of the fourth page is not a lobbying expenditure.

EXAMPLE (10). Assume the same facts as in Example (8), except that T is a membership organization, 75 percent of the recipients of the three page document are members of T, and 25 percent of the recipients are nonmembers and are not subscribers within the meaning of section 56.4911-5(f)(5). Assume also that the document states that readers should write to Congress, but does not state that the readers should urge nonmembers to write to Congress. T treats the document as having a bona fide nonlobbying purpose, the purpose of educating its members about the need for child care. Accordingly, T allocates one-half of the cost of preparing and distributing the document as a lobbying expenditure (see section 56.4911-5(e)(2)(i)), of which 75 percent is a direct lobbying expenditure (see section 56.4911-5(e)(2)(iii)) and 25 percent is a grass roots lobbying expenditure (see section 56.4911-5(e)(2)(ii)). The remaining one-half is allocated as a nonlobbying expenditure. T's allocation is reasonable for purposes of section 56.4911-3(a)(2)(ii) and is correct for purposes of section 56.4911-5(e).

EXAMPLE (11). Assume the same facts as in Example (10), except that T allocates one percent of the cost of preparing and distributing the document as a lobbying expenditure (for purposes of section 56.4911-5(e)(2)) and 99 percent as a nonlobbying expenditure. T's allocation is based upon the fact that out of 200 lines in the document, only two lines state that the recipient should contact legislators about the pending legislation. T's allocation is unreasonable for purposes of section 56.4911-3(a)(2)(ii).

EXAMPLE (12). Organization F, a nonmembership organization, sends a one page letter to all persons on its mailing list. The only subject of the letter is the organization's opposition to a pending bill allowing private uses of certain national parks. The letter requests recipients to send letters opposing the bill to their congressional representatives. A second one page letter is sent in the same envelope. The second letter discusses the broad educational activities and publications of the organization in all areas of environmental protection and ends by requesting the recipient to make a financial contribution to organization F. Since the separate second letter is on a different subject from the lobbying letter, and the letters are of equal length, 50 percent of the mailing costs must be allocated as an expenditure for a grass roots lobbying communication.

EXAMPLE (13). Assume the same facts as in Example (12), except that F is a membership organization and the letters in question are sent primarily (90 percent) to members. The other 10 percent of the recipients are nonmembers and are not subscribers within the meaning of section 56.4911-5(f)(5). Assume also that the first letter does not state that readers should urge nonmembers to write to legislators. F allocates one-half of the mailing costs as a lobbying expenditure, of which 90 percent is a direct lobbying expenditure and 10 percent is a grass roots lobbying expenditure (see section 56.4911-5(e)(2)). F's allocation is reasonable for purposes of section 56.4911-3(a)(2)(ii) and is correct for purposes of section 56.4911-5.

(c) CERTAIN TRANSFERS TREATED AS LOBBYING EXPENDITURES - (i) TRANSFER EARMARKED FOR GRASS ROOTS PURPOSES. A

transfer is a grass roots expenditure to the extent that it is earmarked (as defined in section 56.4911-4(f)(4)) for grass roots lobbying purposes and is not described in section 56.4911-4(e).

(2) TRANSFER EARMARKED FOR DIRECT AND GRASS ROOTS LOBBYING. A transfer that is earmarked for direct lobbying purposes or for direct lobbying and grass roots lobbying purposes is treated as a grass roots expenditure in full except to the extent the transferor demonstrates that all or part of the amounts transferred were expended for direct lobbying purposes, in which case that part of the amounts transferred is a direct lobbying expenditure by the transferor. This paragraph (c)(2) shall not apply to any expenditure described in section 56.4911-4(e).

(3) CERTAIN TRANSFERS TO NONCHARITIES THAT LOBBY - (i) LIMITED APPLICATION OF PARAGRAPH (c)(3) - (A) IN GENERAL. This paragraph (c)(3) applies only to transfers for less than fair market value from an electing public charity to any noncharity that makes lobbying expenditures. A noncharity is any entity that is not described in section 501(c)(3). In order for this paragraph to apply, the electing public charity must transfer to a noncharity more in value than it receives in return. For example, this paragraph does not apply to an electing public charity's fair market value payment of rent to a landlord. However, this paragraph does apply where an electing public charity and a noncharity share office space and the electing public charity pays more than fair market value rent to the noncharity. Similarly, this paragraph applies where an electing public charity sells goods or services to a noncharity for less than fair market value. See paragraphs (c)(3)(B), (C) and (D) of this section for exceptions where non-fair market value transfers are not covered by this paragraph (c)(3). See paragraph (c)(3)(E) of this section to determine the amount of any non-fair market value transfer covered by this paragraph (c)(3). See paragraph (c)(3)(ii) of this section for the rules that apply to transfers governed by this paragraph (c)(3).

(B) EXCEPTION FOR CONTROLLED GRANTS. Notwithstanding paragraph (c)(3)(A) of this section, this paragraph (c)(3) does not apply where an electing public charity makes a grant to a noncharity that is a controlled grant (as defined in section 56.4911-4(f)(3)).

(C) EXCEPTION FOR TRANSFERS THAT ARTIFICIALLY INFLATE EXEMPT PURPOSE EXPENDITURES. Notwithstanding paragraph (c)(3)(A) of this section, this paragraph (c)(3) does not apply where an electing public charity makes a grant to a noncharity that is an expenditure described in section 56.4911-4(e) (relating to grants that artificially inflate exempt purpose expenditures).

(D) EXCEPTION FOR SUBSTANTIALLY RELATED ACTIVITY. Notwithstanding paragraph (c)(3)(A) of this section, this paragraph (c)(3) does not apply where an electing public charity, in the course of an activity that is substantially related to the accomplishment of the electing public charity's exempt purposes, makes goods or services widely available for less than fair market value to individual members of the general public and those goods or services are actually purchased (or consumed for no charge) by a substantial number of wholly unrelated individual members of the general public for less than fair market value. For purposes of the preceding sentence, the term "individual member of the general public" does not include any person or entity directly or indirectly affiliated with the electing public charity in question. The following example illustrates this paragraph (c)(3)(D).

EXAMPLE. Organization P is an educational organization dedicated to preserving the environment. One of P's activities is educating the public about the benefits of installing cost-effective passive solar energy systems, thereby helping to preserve the environment. P charges for its extensive literature and advice, but the charges are less than the fair market value of the literature and advice. P makes its literature and advice widely available to individual members of the general public by advertising in various media and by pamphlets distributed in various areas. P annually provides its literature and advice for less than fair market value to 500 wholly unrelated families, businesses, and tax-exempt organizations. Several of the businesses and tax-exempt organizations make lobbying expenditures within the meaning of section 4911. P's provision of its goods and services to these entities is not covered by this paragraph (c)(3) (and thus does not give rise to a lobbying expenditure by P under paragraph (c)(3)(ii)).

(E) DETERMINATION OF AMOUNT OF TRANSFER GOVERNED BY PARAGRAPH (c)(3). Where an electing public charity receives nothing of value in return for its transfer, the amount of the transfer governed by this paragraph (c)(3) is the greater of the fair market value or the cost of the goods or services transferred to the noncharity. Where the noncharity transfers something of value to the electing public charity in return for the charity's transfer, but that payment is less than the fair market value of the charity's transfer to the noncharity, the amount of the transfer governed by this paragraph (c)(3) is the excess of: first, the greater of the fair market value or cost of the goods or services transferred to the noncharity over, second, the value of the amount transferred to the charity. For example, if an electing public charity transfers \$10,000 of goods and services to a noncharity that makes lobbying expenditures in return for payment by the noncharity of \$2,000, the amount of the transfer governed by this paragraph (c)(3) is \$8,000.

(ii) RULES GOVERNING TRANSFERS TO WHICH PARAGRAPH (c)(3) APPLIES. A transfer to which this paragraph (c)(3) applies is treated in whole or in part as a grass roots and/or direct lobbying expenditure by the transferor in accordance with paragraphs (c)(3)(ii)(A), (B) and (C) of this section. In applying those paragraphs, the expenditures of the transferee will be determined as if the regulations under section 4911 applied to the transferee. This paragraph (c)(3) discusses only when certain transfers are lobbying expenditures by the transferor. This paragraph does not address other issues that may arise when an electing public charity makes a noncontrolled grant to a noncharity. Nothing in this paragraph (c)(3) shall be used to interpret issues relating to noncontrolled grants by charities to noncharities, such as whether the noncontrolled grant is consistent with the continued tax-exempt status of the electing public charity.

(A) TRANSFERS TREATED AS GRASS ROOTS EXPENDITURES. The transfer is treated as a grass roots expenditure to the extent of the lesser of two amounts: the amount of the transfer and the amount of the transferee's grass roots expenditures.

(B) TRANSFERS TREATED AS DIRECT LOBBYING EXPENDITURES. If the transfer is greater than the transferee's grass roots expenditures, the excess is treated as a direct lobbying expenditure, but only to the extent of the transferee's direct lobbying expenditures. (If, however, the transfer is less than the transferee's grass roots expenditures, none of the transfer is a direct lobbying expenditure).

(C) TRANSFERS TREATED AS NONLOBBYING. If the transfer is greater than the sum of the transferee's grass roots and direct lobbying expenditures, the excess of the transfer over those lobbying expenses is not a lobbying expenditure.

(iii) EXAMPLE. The following example illustrates the application of this paragraph (c)(3):

EXAMPLE. Organization C, an electing public charity, shares employee E with N, a noncharity that makes lobbying expenditures. N's grass roots expenditures are \$5,000 and its direct lobbying expenditures are \$25,000. Each organization pays one-half of the \$100,000 in direct and overhead costs associated with E. E devotes one-quarter of his time to C and three-quarters of his time to N. In substance, this arrangement is a transfer (for less than fair market value) from C to N in the amount of \$25,000 (one-quarter of the \$100,000 of direct and overhead costs associated with E's work). Accordingly, C is treated as having made a \$5,000 grass roots expenditure (the lesser of N's grass roots expenditures (\$5,000) or the amount of the transfer (\$25,000)). C is also treated as having made a \$20,000 direct lobbying expenditure (the lesser of N's direct lobbying expenditures (\$25,000) or the remaining amount of the transfer (\$20,000)).

SECTION 56.4911-4 EXEMPT PURPOSE EXPENDITURES.

(a) APPLICATION. This section provides rules under section 4911(e) for determining an electing public charity's "exempt purpose expenditures" for a taxable year for purposes of section 4911(c)(2) and section 56.4911-1(c)(2). Those two sections generally define an electing public charity's lobbying limit (lobbying nontaxable amount) as a sliding scale percentage of the organization's exempt purpose expenditures. In determining an electing public charity's exempt purpose expenditures, no expenditure shall be counted twice by an organization.

(b) INCLUDED EXPENDITURES. Amounts paid or incurred by an organization that are exempt purpose expenditures include -

(1) Amounts paid or incurred to accomplish a purpose enumerated in section 170(c)(2)(B), including (but not limited to) the amount of any transfer made by the organization (other than a transfer described in paragraph (e) of this section) to another organization to accomplish the transferor's exempt purposes, and including amounts expended by an organization out of transfers (other than a transfer described in paragraph (e) of this section) for which the organization is the transferee.

(2) Amounts paid or incurred as current or deferred compensation for an employee's services for a purpose enumerated in section 170(c)(2)(B).

(3) The allocable portion of administrative overhead, and other general expenditures attributable to the accomplishment of a purpose enumerated in section 170(c)(2)(B).

(4) Lobbying expenditures (as defined in section 56.4911-2(a)) whether or not for a purpose enumerated in section 170(c)(2)(B).

(5) Amounts paid or incurred for activities described in section 56.4911-2(c).

(6) Amounts paid or incurred for activities described in section 56.4911-5 that are not lobbying expenditures.

(7) A reasonable allowance for exhaustion, wear and tear, obsolescence or amortization, of assets to the extent used for one or more of the purposes described in

paragraphs (b)(1) through (6) of this section, computed on a straight-line basis (for this purpose, an allowance for depreciation will be treated as reasonable if based on a useful life that would satisfy section 312(k)(3)(A) as in effect on January 1, 1985), and

(8) fundraising expenditures (but see section 4911(e)(1)(C) and paragraphs (c)(3) and (4) of this section.)

(c) **EXCLUDED EXPENDITURES.** Notwithstanding paragraph (b) of this section, exempt purpose expenditures do not include —

(1) Amounts paid or incurred that are neither expenditures to accomplish a purpose enumerated in section 170(c)(2)(B), lobbying expenditures (as defined in section 56.4911-2(a)), nor expenditures described in paragraph (b)(5), (6) or (8) of this section.

(2) The amount of any transfer described in paragraph (e) of this section.

(3) Amounts paid to or incurred for a separate fundraising unit (as defined in paragraph (f)(2) of this section) of an organization or of an affiliated organization (see section 56.4911-7(a)).

(4) Amounts paid to or incurred for any person not an employee, or any organization not an affiliated organization, if paid or incurred primarily for fundraising, but only if such person or organization engages in fundraising, fundraising counseling or the provision of similar advice or services.

(5) Amounts paid or incurred that are properly chargeable to a capital account, determined in accordance with the principles that apply under section 263 or, as applicable, section 263A, with respect to an unrelated trade or business.

(6) Amounts paid or incurred for a tax that is not imposed in connection with the organization's efforts to accomplish a purpose described in section 170(c)(2)(B), such as taxes imposed under sections 511(a)(1) and 4911(a), and

(7) Amounts paid or incurred for the production of income. For purposes of this section, amounts are paid or incurred for the production of income if they are paid or incurred for a purpose or activity that is not substantially related (aside from the need of the organization for income or funds or the use it makes of the profits derived) to the exercise or performance by the organization of its charitable, educational or other purpose or function constituting the basis for its exemption under section 501. For example, the costs of managing an endowment are amounts that are paid or incurred for the production of income and are thus not exempt purpose expenditures. Fundraising expenditures are not, for purposes of this section, amounts that are paid or incurred for the production of income. Instead, the determination of whether fundraising costs are exempt purpose expenditures must be made with reference to section 4911(e)(1)(C) and paragraphs (b)(8), (c)(3) and (c)(4) of this section.

(d) **CERTAIN TRANSFERS TREATED AS EXEMPT PURPOSE EXPENDITURES** — (1) An organization's transfer will be treated as an exempt purpose expenditure under paragraph (b)(1) of this section if it is —

(i) Described in either paragraph (d)(2) or (d)(3) of this section, and

(ii) Not described in paragraph (e) of this section. (2) A transfer is described in this paragraph (d)(2) if it is made to an organization described in section 501(c)(3) in furtherance of the transferor's exempt purposes and is not

earmarked for any purpose other than a purpose described in section 170(c)(2)(B). Thus, a payment of dues by a local or state organization to, respectively, a state or national organization that is described in section 501(c)(3) is considered an exempt purpose expenditure of the transferor to the extent it is not otherwise earmarked.

(3) A transfer is described in this paragraph (d)(3) if it is a controlled grant (as defined in paragraph (f)(3) of this section), but only to the extent of the amounts that are paid or incurred by the transferee that would be exempt purpose expenditures if paid or incurred by the transferor.

(e) **TRANSFERS NOT EXEMPT PURPOSE EXPENDITURES** — (1) An organization's transfer is described in this paragraph (e) if it is described in one of paragraphs (e)(2) through (e)(4).

(2) A transfer is described in this paragraph (e)(2) if it is made to a member of any affiliated group (as defined in section 56.4911-7(e)) of which the transferor is a member.

(3) A transfer is described in this paragraph (e)(3) if the Commissioner determines that the transfer artificially inflates the amount of the transferor's or transferee's exempt purpose expenditures. In general, the Commissioner will make that determination if a substantial purpose of a transfer is to inflate those exempt purpose expenditures. A transfer described in this paragraph will not be considered an exempt purpose expenditure of the transferor, but will be an exempt purpose expenditure of the transferee to the extent that the transferee expends the transfer in the active conduct of its charitable activities or attempts to influence legislation. Standards similar to those found in section 53.4942(b)-1(b) may be applied in determining whether the transferee has expended amounts in the "active conduct" of its charitable activities or attempts to influence legislation.

(4) A transfer is described in this paragraph (e)(4) if it is not a controlled grant and is made to an organization not described in section 501(c)(3) that does not attempt to influence legislation.

(f) **DEFINITIONS** — (1) For purposes of paragraph (c) of this section, "fundraising" includes —

(i) Soliciting dues or contributions from members of the organization, from persons whose dues are in arrears, or from the general public,

(ii) Soliciting grants from businesses or other organizations, including organizations described in section 501(c)(3), or

(iii) Soliciting grants from a governmental unit referred to in section 170(c)(1), or any agency or instrumentality thereof.

(2) For purposes of paragraph (c) of this section, a separate fundraising unit of any organization must consist of either two or more individuals a majority of whose time is spent on fundraising for the organization, or any separate accounting unit of the organization that is devoted to fundraising. For purposes of paragraph (c) of this section, amounts paid to or incurred for a separate fundraising unit include all amounts incurred for the creation, production, copying, and distribution of the fundraising portion of a separate fundraising unit's communication. (For example, an electing public charity that has a separate fundraising unit may not count the cost of postage for a separate fundraising unit's fundraising communication as an exempt purpose expenditure even though, under the electing public charity's accounting system, that cost is attributable to the mailroom rather than to the separate fundraising unit).

(3) For purposes of this section, a "controlled grant" is a grant made by an eligible organization described in section 1.501(h)-2(b) to an organization not described in section 501(c)(3) that meets the following requirements:

(i) The donor limits the grant to a specific project of the recipient that is in furtherance of the donor's (nonlobbying) exempt purposes; and

(ii) The donor maintains records to establish that the grant is used in furtherance of the donor's (nonlobbying) exempt purposes.

(4) A transfer, including a grant or payment of dues, is "earmarked" for a specific purpose --

(i) To the extent that the transferor directs the transferee to add the amount transferred to a fund established to accomplish the purpose, or

(ii) To the extent of the amount transferred or, if less, the amount agreed upon to be expended to accomplish the purpose, if there exists an agreement, oral or written, whereby the transferor may cause the transferee to expend amounts to accomplish the purpose or whereby the transferee agrees to expend an amount to accomplish the purpose.

(g) Example. The provisions of this section are illustrated by the following example:

EXAMPLE. Organization X is an exempt organization described in section 501(c)(3) that is organized for the purpose of rehabilitating alcoholics. X elected to be subject to the provisions of section 501(h) in 1981. For 1981, X had the following expenditures that are included in its exempt purpose expenditures to the extent indicated.

Description	Total	Includable
Cost of real estate purchased for use as half-way house for alcoholics, attributable to the following:		
Land	130,000	-0-
Building	200,000	-0-
Depreciation 40-year useful life	-0-	5,000
Expenses of operating its half-way house	170,000	170,000
Administrative expenses of the organization allocated to the operation of its half-way house	55,000	55,000
Depreciation and allowances for furniture	10,000	10,000
Expenses related to attempts to influence legislation (lobbying expenditures)	40,000	40,000
Amounts paid to Z by the organization for fundraising	35,000	-0-
Total	580,000	320,000

Note. -- For 1981, X's exempt purpose expenditures total \$320,000. The \$35,000 paid by X to Z for fundraising is not included in the exempt purpose expenditures total. All lobbying expenses are included in full. Only depreciation computed on a straight-line basis is included in exempt purpose expenditures.

SECTION 56.4911-5 COMMUNICATIONS WITH MEMBERS.

(a) **IN GENERAL.** For purposes of section 4911, expenditures for certain communications between an organization and its members ("membership communications") are treated more leniently than are communications to nonmembers. This section 56.4911-5 contains rules about the more lenient treatment. In certain cases, this section provides that expenditures for a membership communication are not lobbying expenditures even though those expenditures would be lobbying expenditures if the communication were to nonmembers. In other cases, this section provides that expenditures for a membership communication are direct lobbying expenditures even though those expenditures would be grass roots expenditures if the communication were to nonmembers. Paragraphs (b), (c) and (d) of this section set forth the more lenient rules that apply for communications that are directed only to members. Paragraph (e) of this section sets forth the more lenient rules that apply for communications that are directed primarily, but not solely, to members. Paragraph (f) of this section sets forth certain definitions and special rules.

(b) **COMMUNICATIONS (DIRECTED ONLY TO MEMBERS) THAT ARE NOT LOBBYING COMMUNICATIONS.** Expenditures for a communication that refers to, and reflects a view on, specific legislation are not lobbying expenditures if the communication satisfies the following requirements:

(1) The communication is directed only to members of the organization;

(2) The specific legislation the communication refers to, and reflects a view on, is of direct interest to the organization and its members;

(3) The communication does not directly encourage the member to engage in direct lobbying (whether individually or through the organization); and

(4) The communication does not directly encourage the member to engage in grass roots lobbying (whether individually or through the organization).

(c) **COMMUNICATIONS (DIRECTED ONLY TO MEMBERS) THAT ARE DIRECT LOBBYING COMMUNICATIONS.** Expenditures for a communication that refers to, and reflects a view on, specific legislation and that satisfies the requirements of paragraphs (b)(1), (b)(2), and (b)(4) of this section, but does not satisfy the requirements of paragraph (b)(3) of this section, are treated as expenditures for direct lobbying.

(d) **COMMUNICATIONS (DIRECTED ONLY TO MEMBERS) THAT ARE GRASS ROOTS LOBBYING COMMUNICATIONS.** Expenditures for a communication that refers to, and reflects a view on, specific legislation and that satisfies the requirements of paragraphs (b)(1) and (b)(2) of this section, but does not satisfy the requirements of paragraph (b)(4) of this section, are treated as grass roots expenditures (whether or not the communication satisfies the requirements of paragraph (b)(3) of this section).

(e) **WRITTEN COMMUNICATIONS DIRECTED TO MEMBERS AND NONMEMBERS -- (1) IN GENERAL.** Expenditures for any written communication that is designed primarily for members of an organization (but not directed only to members) and that refers to, and reflects a view on, specific legislation of direct interest to the organization and its members, are treated as expenditures for direct or grass roots lobbying in accordance with paragraph (e)(2), (e)(3) or (e)(4) of this section. For

purposes of this section, a communication is designed primarily for members of an organization if more than half of the recipients of the communication are members of the organization.

(2) **DIRECT LOBBYING DIRECTLY ENCOURAGED** - (i) **LOBBYING EXPENDITURE AMOUNT.** If a written communication described in paragraph (e)(1) of this section directly encourages readers to engage individually or through the organization in direct lobbying but does not directly encourage them to engage in grass roots lobbying, the cost of the communication is allocated between expenditures for direct lobbying and grass roots expenditures in accordance with paragraphs (e)(2)(ii) and (iii) of this section. The portion of the cost to be allocated includes all costs of preparing all the material with respect to which readers are urged to engage in direct lobbying plus the mechanical and distribution costs attributable to the lineage devoted to this material (see section 1.512(a)-1(f)(6)).

(ii) **GRASS ROOTS AMOUNT.** The amount allocable as a grass roots expenditure for a communication described in paragraph (e)(1) of this section is the amount calculated in paragraph (e)(2)(i) of this section multiplied by the sum of the nonmember subscribers percentage and the all other distribution percentage, both as defined in paragraph (f)(7) of this section. Solely for purposes of the allocation described in this paragraph (e)(2)(ii), the nonmember subscribers percentage is treated as zero unless it is greater than 15% of total distribution.

(iii) **DIRECT LOBBYING AMOUNT.** The amount allocable as an expenditure for direct lobbying for a communication described in paragraph (e)(1) of this section is the excess of the amount described in paragraph (e)(2)(i) of this section over the amount described in paragraph (e)(2)(ii) of this section.

(3) **GRASS ROOTS EXPENDITURE IF GRASS ROOTS LOBBYING DIRECTLY ENCOURAGED.** If a written communication described in paragraph (e)(1) of this section directly encourages readers to engage individually or collectively (whether through the organization or otherwise) in grass roots lobbying (whether or not it also encourages readers to engage in direct lobbying), the grass roots expenditure includes all the costs of preparing all the material with respect to which readers are urged to engage in grass roots lobbying plus the mechanical and distribution costs attributable to the lineage devoted to this material (see section 1.512(a)-1(f)(6)).

(4) **NO DIRECT ENCOURAGEMENT OF DIRECT LOBBYING OR OF GRASS-ROOTS LOBBYING.** If a written communication described in paragraph (e)(1) of this section does not directly encourage readers to engage in either direct lobbying or grass roots lobbying, expenditures for the communication are not lobbying expenditures.

(f) **DEFINITIONS AND SPECIAL RULES.** For purposes of the regulations under section 4911 -

(1) **MEMBER; GENERAL RULE.** A person is a member of an electing public charity if the person -

(i) Pays dues or makes a contribution of more than a nominal amount,

(ii) Makes a contribution of more than a nominal amount of time, or

(iii) Is one of a limited number of "honorary" or "life" members who have more than a nominal connection with the electing public charity and who have been chosen for a valid reason (such as length of service to the organization or involvement in activities forming the basis of the

electing public charity's exemption) unrelated to the electing public charity's dissemination of information to its members.

(2) **MEMBER; SPECIAL RULE.** A person not a member of an electing public charity within the meaning of paragraph (f)(1) of this section may be treated as a member if the electing public charity demonstrates to the satisfaction of the Internal Revenue Service that there is a good reason for its membership requirements not meeting the requirements of such paragraph (f)(1), and that its membership requirements do not operate to permit an abuse of the rules described in this section.

(3) **MEMBER; AFFILIATED GROUP OF ORGANIZATIONS.** For purposes of this section, a person who is a member of an organization that is a member of an affiliated group of organizations (within the meaning of section 56.4911-7(e)) is treated, as a member of each organization in the affiliated group.

(4) **MEMBER; LIMITED AFFILIATED GROUP OF ORGANIZATIONS.** For purposes of this section, a person who is a member of an organization that is a member of a limited affiliated group of organizations (within the meaning of section 56.4911-10(b)) is treated as a member of each organization in the limited affiliated group, but only to the extent that the communication relates to a national legislative issue (within the meaning of section 56.4911-10(g)).

(5) **SUBSCRIBER.** A person is a subscriber to a written communication if -

(i) The person is a member of the publishing organization and the membership dues expressly include the right to receive the written communication, or

(ii) The person has affirmatively expressed a desire to receive the written communication and has paid more than a nominal amount for the communication.

(6) **DIRECTLY ENCOURAGES** - (i) **DIRECT LOBBYING** - (A) **IN GENERAL.** For purposes of this section, a communication directly encourages a recipient to engage in direct lobbying, whether individually or through the organization, if the communication:

(1) States that the recipient should contact a legislator or an employee of a legislative body, or should contact any other government official or employee who may participate in the formulation of legislation (but only if the principal purpose of urging contact with the government official or employee is to influence legislation);

(2) States the address, telephone number, or similar information of a legislator or an employee of a legislative body; or

(3) Provides a petition, tear-off postcard or similar material for the recipient to communicate his or her views to a legislator or an employee of a legislative body, or to any other government official or employee who may participate in the formulation of legislation (but only if the principal purpose of so facilitating contact with the government official or employee is to influence legislation).

(B) **"SELF-DEFENSE" EXCEPTION FOR COMMUNICATIONS WITH MEMBERS.**

Notwithstanding the provisions of paragraph (f)(6)(i)(A) of this section, for purposes of paragraphs (b)(3), (c)(2)(i), (e)(3) and (e)(4) of this section, a communication that directly encourages a member to engage in direct lobbying activities that are described in section 4911(d)(2)(C) and that would not be attempts to influence legislation if engaged in directly by the organization is treated as a

communication that does not directly encourage a member to engage in direct lobbying.

(ii) **GRASS ROOTS LOBBYING.** For purposes of paragraphs (b)(4), (e)(3) and (e)(4) of this section, a communication directly encourages recipients to engage individually or collectively (whether through the organization or otherwise) in grass roots lobbying if the communication:

(A) States that the recipient should encourage any nonmember to contact a legislator or an employee of a legislative body, or to contact any other government official or employee who may participate in the formulation of legislation (but only if the principal purpose of urging contact with the government official or employee is to influence legislation);

(B) States that the recipient should provide to any nonmember the address, telephone number, or similar information of a legislator or an employee of a legislative body; or

(C) Provides (or requests that the recipient provide to nonmembers) a petition, tear-off postcard or similar material for the recipient (or nonmember) to use to ask any nonmember to communicate views to a legislator or an employee of a legislative body, or to any other government official or employee who may participate in the formulation of legislation, but only if the principal purpose of so facilitating contact with the government official or employee is to influence legislation. For purposes of this paragraph (f)(6)(ii)(C), a petition is provided for the recipient to use to ask any nonmember to communicate views if, for example, the petition has an entire page of preprinted signature blocks. Similarly, for purposes of this paragraph (f)(6)(ii)(C), where a communication is distributed to a single member and provides several tear-off postcards addressed to a legislator, the postcards are presumed to be provided for the member to use to ask a nonmember to communicate with the legislator.

(7) **PERCENTAGES OF TOTAL DISTRIBUTION.** With respect to a communication described in paragraph (e)(1) of this section -

(i) "Member percentage" means the percentage of total distribution that represents distribution of a single copy to any member;

(ii) "Nonmember subscribers percentage" means the percentage of total distribution that represents distribution to nonmember subscribers (including libraries); and

(iii) "All other distribution percentage" means 100% reduced by the sum of the member percentage and the nonmember subscribers percentage.

(8) **REASONABLE ALLOCATION RULE.** In the case of lobbying expenditures for a communication that also has a bona fide nonlobbying purpose and that is sent only or primarily to members, an electing public charity must make a reasonable allocation between the amount expended for the lobbying purpose and the amount expended for the nonlobbying purpose. See section 56.4911-3(a)(2)(ii).

SECTION 56.4911-6 RECORDS OF LOBBYING AND GRASS ROOTS EXPENDITURES.

(a) **RECORDS OF LOBBYING EXPENDITURES.** An electing public charity must keep a record of its lobbying expenditures for the taxable year. Lobbying expenditures of which an organization must keep a record include the following:

(1) Expenditures for grass roots lobbying, as described in paragraph (b) of this section;

(2) Amounts directly paid or incurred for direct lobbying, including payments to another organization earmarked for direct lobbying, fees and expenses paid to individuals or organizations for direct lobbying, and printing, mailing, and other direct costs of reproducing and distributing materials used in direct lobbying;

(3) The portion of amounts paid or incurred as current or deferred compensation for an employee's services for direct lobbying;

(4) Amounts paid for out-of-pocket expenditures incurred on behalf of the organization and for direct lobbying, whether or not incurred by an employee;

(5) The allocable portion of administrative, overhead, and other general expenditures attributable to direct lobbying;

(6) Expenditures for publications or for communications with members to the extent the expenditures are treated as expenditures for direct lobbying under section 56.4911-5; and

(7) Expenditures for direct lobbying of a controlled organization (within the meaning of section 56.4911-10(c)) to the extent included by a controlling organization (within the meaning of section 56.4911-10(c)) in its lobbying expenditures.

(b) **RECORDS OF GRASS ROOTS EXPENDITURES.** An electing public charity must keep a record of its grass roots expenditures for the taxable year. Grass roots expenditures of which an organization must keep a record include the following:

(1) Amounts directly paid or incurred for grass roots lobbying, including payments to other organizations earmarked for grass roots lobbying, fees and expenses paid to individuals or organizations for grass roots lobbying, and the printing, mailing, and other direct costs of reproducing and distributing materials used in grass roots lobbying;

(2) The portion of amounts paid or incurred as current or deferred compensation for an employee's services for grass roots lobbying;

(3) Amounts paid for out-of-pocket expenditures incurred on behalf of the organization and for grass roots lobbying, whether or not incurred by an employee;

(4) The allocable portion of administrative, overhead and other general expenditures attributable to grass roots lobbying;

(5) Expenditures for publications or communications that are treated as expenditures for grass roots lobbying under section 56.4911-5; and

(6) Expenditures for grass roots lobbying of a controlled organization (within the meaning of section 56.4911-10(c)) to the extent included by a controlling organization (within the meaning of section 56.4911-10(c)) in its grass roots expenditures.

SECTION 56.4911-7 AFFILIATED GROUP OF ORGANIZATIONS.

(a) **AFFILIATION BETWEEN TWO ORGANIZATIONS.** Sections 4911(f)(1) through (3) contain a limited anti-abuse rule for groups of affiliated organizations. In general, the rule operates to prevent numerous organizations from being created for the purpose of avoiding the sliding-scale percentage limitation on an electing public charity's lobbying expenditures (as well as

avoiding the \$1,000,000 cap on a single electing public charity's lobbying expenditures). This is generally accomplished by treating the members of an affiliated group as a single organization for purposes of measuring both lobbying expenditures and permitted lobbying expenditures. The anti-abuse rule is implemented by this section 56.4911-7 and sections 56.4911-8 and -9. This section 56.4911-7 defines the term "affiliated group of organizations" and defines the taxable year of an affiliated group of organizations. Section 56.4911-8 provides rules concerning the exempt purpose expenditures, lobbying expenditures and grass roots expenditures of an affiliated group of organizations, as well as rules concerning the application of the excise tax imposed by section 4911(a) on excess lobbying expenditures by the group. Section 56.4911-9 provides rules concerning the application of the section 501(h) lobbying expenditure limits to members of an affiliated group of organizations. (For additional rules for members of a limited affiliated group of organizations (generally, organizations that are affiliated solely by reason of governing instrument provisions that extend control solely with respect to national legislation), see section 4911(f)(4) and section 56.4911-10).

(1) **IN GENERAL.** For purposes of the regulations under section 4911, two organizations are affiliated, subject to the limitation described in paragraph (a)(2) of this section, if one organization is able to control action on legislative issues by the other by reason of interlocking governing boards (see paragraph (b) of this section) or by reason of provisions of the governing instruments of the controlled organization (see paragraph (c) of this section). The ability of the controlling organization to control action on legislative issues by the controlled organization is sufficient to establish that the organizations are affiliated; it is not necessary that the control be exercised.

(2) **ORGANIZATIONS NOT DESCRIBED IN SECTION 501(c)(3).** Two organizations, neither of which is described in section 501(c)(3), are affiliated only if there exists at least one organization described in section 501(c)(3) that is affiliated with both organizations.

(3) **ACTION ON LEGISLATIVE ISSUES.** For purposes of this section, the term "action on legislative issues" includes taking a position in the organization's name on legislation, authorizing any person to take a position in the organization's name on legislation, or authorizing any lobbying expenditures. The phrase does not include actions taken merely to correct unauthorized actions taken in the organization's name.

(b) **INTERLOCKING GOVERNING BOARDS - (1) IN GENERAL.** Two organizations have interlocking governing boards if one organization (the controlling organization) has a sufficient number of representatives (within the meaning of paragraph (b)(5) of this section) on the governing board of the second organization (the controlled organization) so that by aggregating their votes, the representatives of the controlling organization can cause or prevent action on legislative issues by the controlled organization. If two organizations have interlocking governing boards, the organizations are affiliated without regard to how or whether the representatives of the controlling organization vote on any particular matter.

(2) **MAJORITY OR QUORUM.** Except as provided in paragraph (b)(3) or (4) of this section, the number of representatives of an organization (the controlling organization) who are members of the governing board of a second organization (the controlled organization) will be presumed sufficient to cause or prevent action on

legislative issues by the controlled organization if that number either -

(i) Constitutes a majority of incumbents on the governing board, or

(ii) Constitutes a quorum, or is sufficient to prevent a quorum, for acting on legislative issues.

(3) **VOTES REQUIRED UNDER GOVERNING INSTRUMENT OR LOCAL LAW.** Except as provided in paragraph (b)(4) of this section, if under the governing documents of an organization (the controlled organization), it can be determined that a lesser number of votes than the number described in paragraph (b)(2) of this section is necessary or sufficient to cause or to prevent action on legislative issues, the number of representatives of the controlling organization who are members of the governing board of the controlled organization will be considered sufficient to cause or prevent action on legislative issues if it equals or exceeds that number.

(4) **REPRESENTATIVES CONSTITUTING LESS THAN 15% OF GOVERNING BOARD.** Notwithstanding paragraph (b)(2) or (3) of this section, if the number of representatives of one organization is less than 15 percent of the incumbents on the governing board of a second organization, the two organizations are not affiliated by reason of interlocking governing boards.

(5) **REPRESENTATIVES - (i)** This paragraph (b)(5) describes members of the governing board of one organization (the controlled organization) who are considered representatives of a second organization (the controlling organization). Under this paragraph (b)(5), a member of the governing board of a controlled organization may be a representative of more than one controlling organization. A person with no authority to vote on any issue being considered by the governing board is not a representative of any organization.

(ii) A board member of one organization (the controlled organization) is a representative of a second organization (the controlling organization) if the controlling organization has specifically designated that person to be a board member of the controlled organization. For purposes of this paragraph (b)(5)(ii) and paragraph (b)(5)(iii) of this section, a board member of the controlled organization is specifically designated by the controlling organization if the board member is selected by virtue of the right of the controlling organization, under the governing instruments of the controlled organization, either to designate a person to be a member of the controlled organization's governing board, or to select a person for a position that entitles the holder of that position to be a member of the controlled organization's governing board.

(iii) A board member of one organization who is specifically designated by a second organization, a majority of the governing board of which is made up of representatives of a third organization, is a representative of the third organization as well as being a representative of the second organization pursuant to paragraph (b)(5)(ii) of this section.

(iv) A board member of one organization who is also a member of the governing board of a second organization is a representative of the second organization.

(v) A board member of one organization who is an officer or paid executive staff member of a second organization is a representative of the second organization. Although titles are significant in determining whether a person is a member of the executive staff of an organization, any employee of an organization who possesses authority commonly exercised by an executive is

considered an executive staff member for purposes of this paragraph (b)(5)(v).

(c) **GOVERNING INSTRUMENT.** One organization (the "controlling" organization) is affiliated with a second organization (the "controlled" organization) by reason of the governing instruments of the controlled organization if the governing instruments of the controlled organization limit the independent action of the controlled organization on legislative issues by requiring it to be bound by decisions of the other organization on legislative issues.

(d) **THREE OR MORE ORGANIZATIONS AFFILIATED -- (1) TWO CONTROLLED ORGANIZATIONS AFFILIATED.** If a controlling organization described in this section is affiliated with each of two or more controlled organizations described in this section, then the controlled organizations are affiliated with each other.

(2) **CHAIN RULE.** If one organization is a controlling organization described in this section with respect to a second organization and that second organization is a controlling organization with respect to a third organization, then the first organization is affiliated with the third.

(e) **AFFILIATED GROUP OF ORGANIZATIONS -- (1) DEFINED.** For purposes of the regulations under section 4911, an affiliated group of organizations is a group of organizations --

(i) Each of which is affiliated with every other member for at least thirty days of the taxable year of the affiliated group (determined without regard to the election provided for in paragraph (e)(5) of this section).

(ii) Each of which is an eligible organization (within the meaning of section 1.501(h)-2(b)(1)), and

(iii) At least one of which is an electing member organization (within the meaning of paragraph (e)(4) of this section).

Each organization in a group of organizations that satisfies the requirements of the preceding sentence is a member of the affiliated group of organizations for the taxable year of the affiliated group.

(2) **MULTIPLE MEMBERSHIP.** For any taxable year of an organization, it may be a member of two or more affiliated groups of organizations.

(3) **TAXABLE YEAR OF AFFILIATED GROUP.** If all members of an affiliated group have the same taxable year, that taxable year is the taxable year of the affiliated group. If the members of an affiliated group do not all have the same taxable year, the taxable year of the affiliated group is the calendar year, unless the election under paragraph (e)(5) of this section is made.

(4) **ELECTING MEMBER ORGANIZATION.** For purposes of the regulations under section 4911, an "electing member organization" is an organization to which the expenditure test election under section 501(h) applies on at least one day of the taxable year of the affiliated group of which it is a member. For purposes of the preceding sentence (and notwithstanding section 1.501(h)-2(a)), the expenditure test is not considered to apply to the organization on any day before the date on which it files the Form 3768 making the expenditure test election.

(5) **ELECTION OF MEMBER'S YEAR AS GROUP'S TAXABLE YEAR.** The taxable year of an affiliated group may be determined according to the provisions of this paragraph (e)(5) if all of the members of the affiliated group so elect. Under this paragraph (e)(5), each member

organization shall apply the provisions of section 501(h) and 4911, and the regulations thereunder (unless the regulations provide otherwise), by treating its own taxable year as the taxable year of the affiliated group. The election may be made by an electing member organization by attaching to its annual return a statement from itself and every other member of the affiliated group that contains: the organization's name, address, and employer identification number; and its signed consent to the election provided for in this paragraph (e)(5). The election must be made no later than the due date of the first annual return of any electing member for its taxable year for which the member is liable for tax under section 4911(a), determined under section 56.4911-8(d). The election may not be made or revoked after the due date of the return referred to in the preceding sentence except upon such terms and conditions as the Commissioner may prescribe.

(f) **EXAMPLES.** The provisions of this section are illustrated by the following examples.

EXAMPLE (1). M, N, and O are eligible organizations within the meaning of section 1.501(h)-2(b)(1). Each has a governing board made up of nine members. Five members on the board of N are also members of the board of M. N designates five individuals from among its board, officers, and executive staff members to serve on the board of O. M is affiliated with N, N is affiliated with O, and M is affiliated with O.

EXAMPLE (2). X, an eligible organization, has a board consisting of 10 members. Five unaffiliated tax-exempt organizations each designate two individuals to serve on the governing board of X. A simple majority of the board of X is a quorum and may establish X's position on legislative issues. X is not affiliated with any of the five autonomous organizations by reason of interlocking governing boards.

EXAMPLE (3). P and Q are eligible organizations. The governing instruments of Q state that it will not take a position on legislation if P disapproves of the position. In addition, there is regular correspondence between P and Q with regard to positions on legislation. P is affiliated with Q regardless of whether P has ever vetoed a position taken by Q.

EXAMPLE (4). The governing board of organization R resolves to adopt the position taken on legislative issues by organization S. R and S are eligible organizations and do not have interlocking governing boards. The governing instruments of R do not mention organization S and do not indicate that R is to be bound by the decisions of legislation of any organization. R and S are not affiliated.

EXAMPLE (5). Organization Z is bound, under the terms of its governing instruments, by the legislative positions of Organization Y. Organization Y, however, is bound, under the terms of its governing instruments, by the legislative positions of Organization X. Organization X is affiliated with Y and Z; Y is affiliated with X and Z; and Z is affiliated with X and Y.

EXAMPLE (6). Organizations T and U have interlocking boards of directors. T is the controlling organization. Organization V is bound, under the terms of its governing instruments, by the legislative positions of U. T and V are affiliated because T may cause or prevent action on legislative issues by U, and V is bound by U's action. If U were the controlling organization, T and V would be affiliated as two organizations controlled by the same organization.

EXAMPLE (7). Organization A is described in section 501(c)(4). It is affiliated, as the controlling organization, with organizations K and L, both of which are described in

section 501(c)(3) and are eligible to elect under section 501(h). If K elects under section 501(h), K and L are an affiliated group of organizations. Even though A is affiliated with K and L, A is not a member of that affiliated group of organizations because A is not an eligible organization within the meaning of section 1.501(h)-2(b)(1) (see section 56.4911-7(e)(1) for the definition of which affiliated organizations may be members of an affiliated group of organizations).

EXAMPLE (8). G, H, I, and J are eligible organizations. G, H, and I have elected the expenditure test under section 501(h). The governing board of J has nine members. Under the governing instruments of J, organizations G, H, and I each designate three members of the governing board of J. Also under the governing instruments of J, action on legislative issues requires the approval of any seven board members. Because the three representatives of G may prevent action on legislative issues, J is affiliated with G. Similarly, J is affiliated with each of H and I. However, under none of the rules of affiliation is G affiliated with H, or H with I, or I with G. Therefore J is a member of one affiliated group comprising G and J, of another group comprising H and J, and of a third group comprising I and J.

EXAMPLE (9). Organizations C, D, and E have been affiliated for many years and have all elected the expenditure test. Each has a taxable year ending July 31. For every day of the year ending July 31, 1992, they were eligible organizations, electing member organizations, and affiliated with each other. On no day of that year were they affiliated with any other eligible organization having a different taxable year. Therefore, the year ending July 31, 1992, is the taxable year of the affiliated group comprising C, D, and E.

SECTION 56.4911-8 EXCESS LOBBYING EXPENDITURES OF AFFILIATED GROUP.

(a) **APPLICATION.** This section provides rules concerning the exempt purpose expenditures, lobbying expenditures, and grass roots expenditures of an affiliated group of organizations, and the application of the excise tax imposed by section 4911(a) on the excess lobbying expenditures of the group.

(b) **AFFILIATED GROUP TREATED AS ONE ORGANIZATION.** Under section 4911(f), an affiliated group of organizations is treated as a single organization for purposes of the tax imposed by section 4911(a). For any taxable year of the affiliated group, the group's lobbying expenditures, grass roots expenditures, and exempt purpose expenditures are equal to the sum of the lobbying expenditures, grass roots expenditures, and exempt purpose expenditures, respectively, paid or incurred by each member during the taxable year of the affiliated group. The lobbying and grass roots nontaxable amounts for the affiliated group for a taxable year are determined under section 4911(c)(2) and (4) and section 56.4911-1(c) and are based on the sum of the exempt purpose expenditures described in the preceding sentence. The lobbying and grass roots ceiling amounts for the affiliated group for a taxable year are calculated under section 1.501(h)-3(c)(3) and (6) based upon the nontaxable amounts determined pursuant to the preceding sentence.

(c) **TAX IMPOSED ON EXCESS LOBBYING EXPENDITURES OF AFFILIATED GROUP.** The excise tax under section 4911(a) is imposed for a taxable year of an affiliated group if the group has excess lobbying expenditures. For any taxable year of an affiliated group, the group's excess lobbying expenditures are the greater of

(1) The amount by which the group's lobbying expenditures exceed the group's lobbying nontaxable amount, or

(2) The amount by which the group's grass roots expenditures exceed the group's grass roots nontaxable amount.

(d) **LIABILITY FOR TAX - (1) ELECTING ORGANIZATIONS.** As provided in this paragraph (d), an electing member organization is liable for all or a portion of the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations. An organization that is liable under this paragraph (d) is not liable for any excise tax under section 4911 based on its own excess lobbying expenditures. A member of the affiliated group that is not an electing member organization is not liable for any portion of the excise tax that is imposed with respect to the affiliated group.

(2) **TAX BASED ON EXCESS LOBBYING EXPENDITURES.** If the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is based upon the amount described in paragraph (c)(1) of this section, and at least one electing member has made lobbying expenditures, each electing member organization is liable for a portion of the tax equal to the amount of the tax multiplied by a fraction, the numerator of which is the electing member organization's lobbying expenditures paid or incurred during the taxable year of the affiliated group, and the denominator of which is the sum of the lobbying expenditures of all electing member organizations in the group paid or incurred during the taxable year of the affiliated group.

(3) **TAX BASED ON EXCESS GRASS ROOTS EXPENDITURES.** If the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is based upon the amount described in paragraph (c)(2) of this section, and at least one electing member has made grass roots expenditures, each electing member organization is liable for a portion of the tax equal to the amount of the tax multiplied by the fraction described in paragraph (d)(2) of this section, except that "grass roots expenditures" is substituted for "lobbying expenditures."

(4) **TAX BASED ON EXEMPT PURPOSE EXPENDITURES.** If the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is based upon the amount described in paragraph (c)(2) of this section, and if paragraphs (d)(2) and (d)(3) of this section do not apply because no electing organization has made lobbying or grass roots expenditures, respectively, each electing member organization is liable for a portion of the tax equal to the amount of tax multiplied by a fraction the numerator of which is the electing member organization's exempt purpose expenditures and the denominator of which is the exempt purpose expenditures of all the electing member organizations in the affiliated group.

(5) **TAXABLE YEAR FOR WHICH LIABLE.** An electing member organization that is liable for all or a portion of the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is liable for the tax as if the tax were imposed for its taxable year with which or within which ends the taxable year of the affiliated group.

(6) **ORGANIZATION A MEMBER OF MORE THAN ONE AFFILIATED GROUP.** If, under this paragraph (d), an organization is liable for its taxable year for two or

more excise taxes imposed by section 4911(a) on the excess lobbying expenditures of two or more affiliated groups, then the organization is liable only for the greater of the two or more taxes.

(e) **FORMER MEMBER ORGANIZATION.** An electing member organization that ceases to be a member of an affiliated group of organizations, the taxable year of which is different from its own, must thereafter determine its liability under section 56.4911-1 for the excise tax imposed by section 4911(a) as if its taxable year were the taxable year of the affiliated group of which it was formerly a member. An organization to which this paragraph (e) applies that is liable for the excise tax imposed by section 4911(a) is liable for the tax as if the tax were imposed for its taxable year within which ends the taxable year of the affiliated group of which it was formerly a member. The Commissioner may, at the Commissioner's discretion, permit an organization to disregard the rules of this paragraph (e) and to determine any liability under section 4911(a) based upon its own taxable year.

SECTION 56.4911-9 APPLICATION OF SECTION 501(h) TO AFFILIATED GROUPS OF ORGANIZATIONS.

(a) **SCOPE.** This section provides rules concerning the application of the limitations of section 501(h) to members of an affiliated group of organizations (as defined in section 56.4911-7(e)(1)).

(b) **DETERMINATION REQUIRED.** For each taxable year of an affiliated group of organizations, the calculations described in section 1.501(h)-3(b)(1)(i) and (ii) must be made, based on the expenditures of the group. If, for a taxable year of an affiliated group, it is determined that the sum of the affiliated group's lobbying or grass roots expenditures for the group's base years exceeds 150 percent of the sum of the group's corresponding nontaxable amounts for the base years, then under section 501(h), each member organization that is an electing member organization (as defined in section 56.4911-7(e)(4)) at any time in the taxable year of the affiliated group shall be denied tax exemption beginning with its first taxable year beginning after the end of such taxable year of the affiliated group. Thereafter, exemption shall be denied unless (pursuant to section 1.501(h)-3(d)) the organization reapplies and is recognized as exempt as an organization described in section 501(c)(3). For purposes of this section, the term "base years" generally means the taxable year of the affiliated group for which a determination is made and the group's three preceding taxable years. Base years, however, do not include any year preceding the first year in which at least one member of the group was treated as described in section 501(c)(3).

(c) **MEMBER ORGANIZATIONS THAT ARE NOT ELECTING ORGANIZATIONS.** An organization that is a member of an affiliated group of organizations but that is not an electing member organization remains subject to the "substantial part test" described in section 501(c)(3) with respect to its activities involving attempts to influence legislation.

(d) **FILING OF INFORMATION RELATING TO AFFILIATED GROUP OF ORGANIZATIONS - (1) SCOPE.** The filing requirements described in this paragraph (d) apply to each member of an affiliated group of organizations for the taxable year of the member with which, or within which, ends the taxable year of the affiliated group.

(2) **IN GENERAL.** Each member of an affiliated group of organizations shall provide to every other member of the group, before the first day of the second month following the close of the affiliated group's taxable year, its name, identification number, and the information required under section 1.6033-2(a)(2)(ii)(k) for its expenditures during the group's taxable year and for prior taxable years of the group that are base years under paragraph (b). For groups electing under section 56.4911-7(e)(5) to have each member file information with respect to the group based on its taxable year, each member shall provide the information required by the preceding sentence by treating each taxable year of any member of the group as a taxable year for the group.

(3) **ADDITIONAL INFORMATION REQUIRED.** In addition to the information required by section 1.6033-2(a)(2)(ii)(k), each member of an affiliated group of organizations must provide on its annual return the group's taxable year and, if the election under section 56.4911-7(e)(5) is made, the name, identification number, and taxable year identifying the return with which its consent to the election was filed.

(4) **INFORMATION REQUIRED OF ELECTING MEMBER ORGANIZATION.** In addition to the information required by section 1.6033-2(a)(2)(ii)(k) and paragraph (d)(3) of this section, each electing member organization (as defined in section 56.4911-7(e)(4)) must provide on its annual return -

(i) The name and identification number of each member of the group, and

(ii) The appropriate calculation described in section 56.4911-8(d), if the organization is an electing member organization liable for all or any portion of the excise tax imposed by section 4911(a).

(c) **EXAMPLE.** The provisions of this section may be illustrated by the following example:

EXAMPLE. (1) M, N, and O are affiliated organizations under section 56.4911-7(a). M's taxable year ends November 30, N's, January 31, and O's, June 30. On June 20, 1979, O files Form 5768 to elect to be governed by the expenditure test. M files Form 5768 in December of 1979. Neither M nor O revokes the election, and no organization makes the election provided for in section 56.4911-7(e)(5). M, N, and O constitute an affiliated group of organizations, the first taxable year of which is the calendar year 1979.

(2) Because the organizations did not elect under section 56.4911-7(e)(5) to use their own taxable years as the group's taxable years, the expenditures of the affiliated group for its first taxable year are the expenditures made by M, N, and O during calendar year 1979, and are reported by M, N, and O on their returns for their taxable years within which falls December 31, 1979. M reports the expenditures of the affiliated group for 1979 on its return for its taxable year ending November 30, 1980; and O, on its return for its taxable year ending June 30, 1980. N is not an electing member (as defined in section 56.4911-7(e)(4)). Accordingly, under paragraph (d)(3)(i) of this section, it reports the name and identification number of each member of the group.

(3) The following tables summarize the expenditures by the affiliated group for the calendar years indicated. None of the group's lobbying expenditures for its taxable years 1979 through 1982 were grass roots expenditures.

Table 1. Group's Expenditures

Year	Exempt Purpose Expenditures		Lobbying Expenditures	
	(EPE)	Calculation	(LPE)	(LE)
1979	\$ 400,000	(20% x \$800,000) =	\$80,000	\$100,000
1980	\$ 200,000	(25% x \$800,000) =	\$200,000	\$100,000
1981	\$ 400,000	(25% x \$1,600,000) =	\$400,000	\$120,000
1982	\$ 200,000	(25% x \$800,000) =	\$200,000	\$220,000
Total	\$1,000,000		\$1,000,000	\$340,000

Table 15. Expenditures of M and O

Year	Exempt Purpose Expenditures		Lobbying Expenditures		Total	
	M	O	M	O	M	O
1979	125,000	100,000	20,000	20,000	145,000	120,000
1980	100,000	50,000	20,000	20,000	120,000	70,000
1981	200,000	100,000	20,000	20,000	220,000	120,000
1982	200,000	100,000	20,000	20,000	220,000	200,000

(4) For the affiliated group's taxable years 1979, 1980, 1981, and 1982, the group has excess lobbying expenditures. Under section 4911(f)(1)(B) and section 56.4911-8(d), M and O, as electing member organizations, are liable for a portion of the 25 percent excise tax imposed on the group's excess lobbying expenditures, based on their respective shares of the lobbying expenditures of all electing member organizations. For 1979, the excess lobbying expenditures are \$20,000 (\$100,000 - \$80,000). The tax is 25% of \$20,000 or \$5,000; M must pay \$3,750 ($(\$60,000/\$80,000) \times \$5,000 = \$3,750$), and O must pay \$1,250 ($(\$20,000/\$80,000) \times \$5,000 = \$1,250$). For 1980, the tax is \$10,000 and each must pay \$5,000. For 1981, the tax is \$1,250, of which M must pay \$750 and O must pay \$500. For 1982, the tax is \$30,000. M must pay \$24,000 and O must pay \$6,000. M and O are not liable for any separate 4911 excise tax that otherwise would have been imposed on their separate excess lobbying expenditures.

(5) Under section 56.4911-9(b), the group must make the calculation described in section 1.501(h)-3(b)(1) for each of the group's taxable years 1979 through 1982. The following illustrates only the required calculation for the group's taxable year 1982. For its taxable year 1982, the group must determine whether it normally has made lobbying expenditures in excess of its lobbying ceiling amount. The determination takes into account the group's expenditures in base years 1979 through 1982. The sum of the group's lobbying expenditures for the base years (\$540,000) exceeds 150% of the sum of the group's lobbying nontaxable amounts for the base years ($150\% \times \$355,000 = \$532,500$). Therefore, for its taxable year 1982, the group normally has made lobbying expenditures in excess of its lobbying ceiling amount. Under section 501(h) and section 56.4911-9(b), M is not exempt from tax under section 501(a) as an organization described in section 501(c)(3) for its taxable year beginning December 1, 1983, and O is not exempt for its year beginning July 1, 1983. Whether N's lobbying expenditures disqualify it for tax exemption at any time after January 1, 1979, is determined under the substantial part test of section 501(c)(3).

(f) CROSS REFERENCE. For other provisions relating to members of an affiliated group of organizations, see

sections 58.4911-2(c)(4)(ii), 56.4911-4(c)(2), 56.4911-4(e), and 56.4911-5(f)(3).

SECTION 56.4911-10 MEMBERS OF A LIMITED AFFILIATED GROUP OF ORGANIZATIONS.

(a) SCOPE. This section provides additional rules for members of a limited affiliated group of organizations, as defined in paragraph (b) of this section (relating generally to organizations that are affiliated solely by reason of provisions of their governing instruments that extend control solely with respect to national legislation). Except as otherwise provided in this section, sections 56.4911-8 and 56.4911-9 do not apply to members of a limited affiliated group. Thus, as modified by this section, the regulations under sections 501(h) and 4911 apply to electing members of a limited affiliated group individually. For example, sections 56.4911-2 through -4, which, by their terms, include amounts described in paragraph (d) of this section, are used in applying sections 501(h) and 4911 to controlling member organizations (within the meaning of paragraph (c) of this section). Except as otherwise provided in this section, members of a limited affiliated group that are not electing organizations are subject to the substantial part test.

(b) MEMBERS OF LIMITED AFFILIATED GROUP. For purposes of section 4911, a limited affiliated group consists of two or more organizations that meet the following requirements:

- (1) Each organization is a member of an affiliated group of organizations as defined in section 56.4911-7(e);
- (2) No two members of the affiliated group described in paragraph (b)(1) of this section are affiliated by reason of interlocking governing boards under section 56.4911-7(b); and
- (3) No member of the affiliated group described in paragraph (b)(1) of this section is, under its governing instrument, bound by decisions of one or more of the other such members on legislative issues other than national legislative issues.

Each organization in a group of organizations that satisfies the requirements of the preceding sentence is a member of the limited affiliated group.

(c) CONTROLLING AND CONTROLLED ORGANIZATIONS. For purposes of this section, a member of a limited affiliated group is a controlling member organization if it controls one or more of the other members of the limited affiliated group, and a member of a limited affiliated group is a controlled member organization if it is controlled by one or more of the other members of the limited affiliated group. For purposes of the preceding sentence, whether an organization controls a second organization shall be determined by whether the second organization is bound, under its governing instruments, by actions taken by the first organization on national legislative issues.

(d) EXPENDITURES OF CONTROLLING ORGANIZATION - (1) SCOPE. This paragraph (d) applies to a controlling member organization that has the expenditure test election in effect for its taxable year. This paragraph (d) applies whether or not the organization is also a controlled member organization. In determining a controlling member organization's expenditures, no expenditure shall be counted twice.

(2) EXPENDITURES FOR DIRECT LOBBYING. A controlling member organization for which the expenditure test election is in effect shall include in its direct lobbying expenditures for its taxable year the direct lobbying

expenditures (as defined in sections 56.4911-2 and -3) paid or incurred with respect to national legislative issues during such year by each organization that is a member of the limited affiliated group and is controlled (within the meaning of paragraph (c) of this section) by such controlling member organization.

(3) **GRASS ROOTS EXPENDITURES.** A controlling member organization for which the expenditure test election is in effect shall include in its grass roots expenditures for its taxable year the grass roots expenditures (as defined in sections 56.4911-2 and -3) paid or incurred with respect to national legislative issues during such year by each organization that is a member of the limited affiliated group and is controlled (within the meaning of paragraph (c) of this section) by such controlling member organization.

(4) **EXEMPT PURPOSE EXPENDITURES.** The exempt purpose expenditures of a controlling member organization do not include the exempt purpose expenditures (other than lobbying expenditures described in paragraphs (d)(2) and (d)(3) of this section) of any organization that is a controlled member organization with respect to it.

(e) **EXPENDITURES OF CONTROLLED MEMBER.** A controlled member organization that is an electing organization but that does not control (within the meaning of paragraph (c) of this section) any organization in the limited affiliated group shall apply sections 501(h) and 4911 and the regulations thereunder without regard to the expenditures of any other member of the limited affiliated group.

(f) **REPORTS OF MEMBERS OF LIMITED AFFILIATED GROUPS - (1) CONTROLLING MEMBER ORGANIZATION'S ADDITIONAL INFORMATION ON ANNUAL RETURN.** In addition to the information required by section 1.6033-2(a)(2)(ii)(k), each controlling member organization for which the expenditure test election is in effect must provide on its annual return the name and identification number of each member of the limited affiliated group.

(2) **REPORTS OF CONTROLLING MEMBERS TO OTHER MEMBERS.** Each controlling member organization for which an expenditure test election is in effect must notify each member that it controls of its taxable year in order for the controlled organization to prepare the report required by paragraph (f)(3) of this section. Such notification must be made before the beginning of the second month after the close of each taxable year of the controlling member for which the election is in effect.

(3) **REPORTS OF CONTROLLED MEMBER ORGANIZATION.** Every controlled member organization (whether or not the expenditure test election is in effect with respect to it) shall provide to each member of the limited affiliated group that controls it, before the first day of the second month following the close of the taxable year of each such controlling organization, its name, identification number, and the lobbying expenditures and grass roots expenditures on national legislative issues incurred by the controlled member organization.

(g) **NATIONAL LEGISLATIVE ISSUES.** The term "national legislative issue" means legislation, limited to action by the Congress of the United States or by the public in any national procedure. If an issue is both national and local, it is characterized as a national legislative issue if the contemplated legislation is Congressional legislation.

(h) **EXAMPLES.** The provisions of this section are illustrated by the following examples:

EXAMPLE (1). State X has an income tax law that uses definitions contained in the Internal Revenue Code as it may be amended from time to time. Legislation to change a definition in the Internal Revenue Code is pending in Congress. This is a national legislative issue even though Congressional action may affect state law.

EXAMPLE (2). Organization M takes a position favoring approval by Congress of a proposed amendment to the United States Constitution. This is a national legislative issue. After approval by Congress and submission to the states for ratification, the proposed amendment ceases to be a national legislative issue.

EXAMPLE (3). N, O, and P are organizations described in section 501(c)(3) that do not have interlocking governing boards, within the meaning of section 56.4911-7(b). N has elected the expenditure test under section 501(h). By virtue of the governing instruments of O and P, any decision made by N on national legislative issues (such as issues concerning action on acts, bills, resolutions, or similar items by Congress) binds both O and P. Under their governing instruments, O and P are not bound on any other issues. Therefore, N, O, and P constitute a limited affiliated group. If P sends a series of letters and pamphlets to members of Congress in support of bill V, their cost will be included in N's and P's expenditures for direct lobbying and in N's and P's exempt purposes expenditures, but will not be included in O's lobbying expenditures. If N hires a lobbyist to solicit support for bill V, the cost of hiring the lobbyist will be includable only in N's lobbying expenditures. Any lobbying expenditures incurred by either O or P on any issue that is not a national legislative issue will not be included in N's lobbying expenditures.

EXAMPLE (4). Y is an electing organization and a member of a limited affiliated group of organizations. Y controls organizations A, B, and C with respect to national legislative issues but is not controlled by any other organization. Y's taxable year is the calendar year. During 1982, A dissolves on March 15th and D, also controlled by Y with respect to national legislative issues, is established on May 1st. For 1982 the limited affiliated group comprises Y, A, B, C, and D.

EXAMPLE (5). P, Q, R, and S are electing organizations. The governing instruments of Q require it to adopt the positions on national legislative issues adopted by P. R is similarly bound by Q's positions. R and S have interlocking governing boards, within the meaning of section 56.4911-7(b), but S's governing instruments do not require it to adopt the position of any other organization on any legislative issues. Under section 56.4911-7(e)(1), P, Q, R, and S are members of an affiliated group. Applying paragraph (b) of this section, it is determined that (1) P, Q, R and S are members of an affiliated group; and (2) R and S are affiliated by reason of interlocking governing boards. Accordingly, P, Q, R and S are not a limited affiliated group. Similarly, P, Q, and R do not constitute a limited affiliated group because they are members of an affiliated group comprising P, Q, R, and S, two of whose members, R and S, are affiliated by reason of interlocking governing boards.

EXAMPLE 6. T, U, V, and W are electing organizations. The governing instruments of U and V require them to adopt the positions on national legislative issues adopted by T, but do not require them to adopt the positions of any organization on any other legislative issues. The governing documents of W require it to adopt the positions of V on all legislative issues. Applying

paragraph (b) of this section, it is determined that (1) T, U, V, and W are all members of an affiliated group; (2) no two of T, U, V, and W are affiliated by reason of interlocking governing boards; but (3) W is bound, under its governing instrument, by decisions of V on legislative issues that are not national legislative issues. Accordingly, T, U, V, and W do not constitute a limited affiliated group. Similarly, T, U, and V do not constitute a limited affiliated group. T, U, V, and W are an affiliated group under section 56.4911-7.

SECTION 56.6001-1 NOTICE OR REGULATIONS REQUIRING RECORDS, STATEMENTS, AND SPECIAL RETURNS.

(a) **IN GENERAL.** The provisions of section 53.6001-1 shall apply to any person subject to tax under chapter 41, Subtitle D, of the Code, by treating each reference to chapter 42 in section 53.6001-1 as a reference to chapter 41.

(b) **CROSS REFERENCES.** See section 56.4911-6 for general information on records of lobbying expenditures. See sections 56.4911-9(d) and 56.4911-10(f) for information that members of an affiliated group and a limited affiliated group, respectively, are to provide to other members of the group and to the Internal Revenue Service.

SECTION 56.6011-1 GENERAL REQUIREMENT OF RETURN, STATEMENT, OR LIST.

Every organization liable for the tax imposed by section 4911(a) shall file an annual return with respect to the tax on the form prescribed by the Internal Revenue Service for that purpose and shall include the information required by the form and its instructions.

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

PART 602 - (AMENDED)

Par. 18. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 19. Section 602.101(c) is amended by inserting in the appropriate place in the table "section 56.4911 . . . 1545-0052".

Fred T. Goldberg
Commissioner of Internal Revenue

Approved: August 3, 1990

Kenneth W. Gideon
Assistant Secretary of the Treasury for Tax Policy

IRS ISSUES NOTICE OF PROPOSED REG (CO-26-89)

(Section 1502 - Consolidated Return Regs.)

CONSOLIDATED RETURN REGULATIONS - COORDINATION WITH SECTION 833

CC:CO-26-89

Br3:JWhalen

[4830-01]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

CO-26-89

RIN: 1545-AM49

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: In the rules and regulations portion of this issue of the Federal Register, the Internal Revenue Service is issuing temporary regulations that add a new section 1.1502-75T(d)(5) of the consolidated return regulations by providing rules relating to the removal of the tax-exempt status of organizations described in section 833 of the Internal Revenue Code. The rules are needed because such organizations are, for taxable years beginning after 1986, includible corporations under section 1504(b). The text of the temporary regulations also serves as the comment document for this notice of proposed rulemaking.

DATES: Written comments and requests for a public hearing must be received by November 5, 1990.

ADDRESS: Send comments and requests for a public hearing to: Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Attn: CC:CORP:T:R (CC:CO-26-89), Room 4429, Washington, D.C. 20044.

FOR FURTHER INFORMATION CONTACT: Jean M. Whalen (Telephone 202-566-3938, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The temporary regulations published in the Rules and Regulations portion of this issue of the Federal Register add a new section 1.1502-75T(d)(5) to Part 1 of Title 26 of the Code of Federal Regulations. For the text of the new temporary regulations, see T.D. 8310, published in the Rules and Regulations portion of this issue of the Federal Register. The preamble to the temporary regulations explains the regulations.

SPECIAL ANALYSES

It has been determined that these proposed rules will not be major rules as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. Chapter 5) and the Regulatory Flexibility Act (5 U.S.C. Chapter 6) do not apply to these regulations, and therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these regulations will be submitted to the Administrator of the Small Business Administration for comment on their impact on small business.

**A Comparison of Treasury Regulations Issued August 31, 1990, Implementing
the 1976 Lobby Law and Definitions of Lobbying Under H.R. 823/S. 349
"Lobbying Disclosure Act of 1993"**

Following is a comparison between definitions related to lobbying under Public Law 94-455 and regulations, and H.R. 823/S.349. The comparison is drawn from H.R. 823/S.349, the Internal Revenue Code, the IRS Regulations and related documents.

(Note: IN SOME INSTANCES, the definitions are only roughly analogous so comparisons are sometimes inexact.)

Treasury Regulations Implementing Section 1307 of PL-94-455 (From I.R.C. Sec. 4911)	Lobbying Disclosure Act of 1993
<i>Influencing Legislation:</i>	
1 A) any attempt to influence any legislation through an attempt to affect the opinions of the general public or any segment thereof, and;	Lobbying activities include grass roots lobbying communications (as defined in regulations implementing section 4911(c)(3) of the Internal Revenue Code of 1986) to the extent that such activities are made in direct support of lobbying contacts. Sec 3 (6)
2 B) any attempt to influence any legislation through communication with any member or employee of a legislative body, or with any government official or employee who may participate in the formulation of the legislation.	The term "lobbying activities" means lobbying contacts and efforts in support of such contacts, including preparation and planning activities, research and other background work that is intended for use in contacts, and coordination with the lobbying activities of others. Sec. 3(6)

Treasury Regulations Implementing Section 1307 of PL-94-455 (From I.R.C. Sec. 4911)	Lobbying Disclosure Act of 1993
Other Definitions and Special Rules.	
<p>3 Legislation. The term "legislation" includes action with respect to Acts, bills, resolutions, or similar items by the Congress, any State Legislature, any local council, or similar governing body, or by the public in a referendum, initiative, constitutional amendment, or similar procedure.</p>	<p>The term "lobbying" contact" means any oral or written communication with a covered legislative or executive branch official made on behalf of a client with regard to--</p> <ul style="list-style-type: none"> (i) the formulation, modification, or adoption of Federal legislation (including legislative proposals); (ii) the formulation, modification, or adoption of a Federal rule, regulation, Executive order, or any other program, policy or position of the United States Government; or (iii) the administration or execution of a Federal program or policy (including the negotiation, award, or administration of a Federal contract, grant, loan, permit, or license) except that it does not include communications that are made to officials serving in the Senior Executive Service or the uniformed services in the agency responsible for taking such action.
<p>4 Action. The term "action" is limited to the introduction, amendment, enactment, defeat, or repeal of Acts, bills, resolutions, or similar items.</p>	See 3 above.
Communications with members. --	
<p>(Direct Lobbying)</p> <p>5 A) A communication between an organization and any bona fide member of such organization to directly encourage such member to communicate with a legislator, etc., to influence legislation.</p>	Lobbying activities [which include] coordination with the lobbying activities of others. Sec 3(8)
<p>(Grass Roots Lobbying)</p> <p>6 B) A communication between an organization and any bona fide member of such organization to directly encourage such member to urge persons other than members to communicate with legislators is grass roots lobbying because it attempts to affect the opinions of the general public or a segment thereof.</p>	Lobbying activities include grass roots lobbying communications (as defined in regulations implementing section 4911(c)(3) of the Internal Revenue Code of 1986) to the extent that such activities are made in direct support of lobbying contacts. Sec 3(8)

Treasury Regulations Implementing Section 1307 of PL-94-455 (From I.R.C. Sec. 4911).	Lobbying Disclosure Act of 1993
Exceptions. --"influencing legislation" does not include--	
7 A) making available the results of nonpartisan analysis, study or research;	No exception for charities.
8 B) providing of technical advice or assistance (for such advice that 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;	Disclosure not required.
9 C) appearances before, or communications to, any legislative body with respect to a possible decision of such body which might affect the existence of the organizations, its powers, and duties, tax-exempt status, or the deduction of contributions to the organizations;	No exception for charities.
10 D) 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 a communication between an organization and any bona fide member of such organization to directly encourage such member to communicate with a legislator as described in (B) above.	No exception for charities.
11 E) any communication with a government official or an employee, other than-- (i) a communication with a member or employee of a legislative body (where such communication would otherwise constitute the influencing of legislation), or (ii) a communication the principal purpose of which is to influence legislation.	No exception for charities.
12 Affiliated Organizations. If for a taxable year two or more organizations described in Section 501(c)(3) are members of an affiliated group of organizations (as defined) then...(note: what follows at this point is a complex description when organizations are affiliated and should be treated as one entity).	The term "organization" means any corporation (excluding a Government corporation), company, foundation, association, labor organizations, firm, partnership, society, joint stock company, or group of organizations. (Emphasis added.)