

NOTES

ALL SAINTS CHURCH AND THE ARGUMENT FOR A GOAL-DRIVEN APPLICATION OF INTERNAL REVENUE SERVICE RULES FOR TAX-EXEMPT ORGANIZATIONS

KARA BACKUS*

I. INTRODUCTION

At All Saints Church of Pasadena (“All Saints”), on the eve of the Bush-Kerry presidential election of 2004, a sermon delivered by Rector Emeritus George Regas discussing what Jesus would think of the war in Iraq prompted the Internal Revenue Service (“IRS”) to launch an investigation into whether the church had violated its obligation under federal tax rules to avoid endorsing political candidates.¹ Although Regas stated explicitly, “I don’t intend to tell you how to vote,” he went on to state, “President Bush, you have not made dramatically clear what have been the human consequences of the war Oh, the cost of your war.”² In September 2006, All Saints, led by Reverend Ed Bacon, refused to comply with an IRS summons directing them to turn over any documents from 2004 containing political references, claiming the summons intruded upon their religious freedom.³ After a year without contact with All Saints, the IRS issued a letter to the church in September 2007 concluding that, although the sermon was illegal, the church’s exempt status would not be revoked. All Saints described the “vague, mixed message” as unacceptable and demanded a clarification, correction, and apology from the IRS.⁴

* J.D. Candidate, University of Southern California Law School, 2008, B.A. Amherst College, 1996. Thank you to Professor Ron Garet for his valuable guidance and feedback.

¹ George F. Regas, *If Jesus Debated Senator Kerry and President Bush* (Oct. 31, 2004) (sermon transcript, All Saints Church).

² *Id.*

³ Press Release, All Saints Church, *The IRS Returns (2007)*, available at http://www.allsaints-pas.org/site/PageServer?pagename=IRS_Exam_splash (follow “8/17/06 Response to the IRS” hyperlink).

⁴ Letter from Marsha A. Ramirez, Director, EO Examinations, IRS, to Marcus S. Owens, Caplin & Drysdale (Sept. 10, 2007), available at http://www.allsaints-pas.org/site/DocServer/Letter_from_IRS_to_All_Saints_Church.pdf?docID=2541; Rebecca Trounson, *Pasadena Church Wants Apology from IRS*, L.A. TIMES, Sept. 24, 2007, at A1.

The conflict between All Saints and the IRS comes at a time of heightened public scrutiny of IRS enforcement of federal tax laws for tax-exempt organizations.⁵ The law limits all exempt organizations, not only churches,⁶ from venturing too far into the realm of politics.⁷ Three other highly publicized investigations are illustrative. In October 2004, in response to complaints from several Republican members of Congress, the IRS investigated whether statements made by National Association for the Advancement of Colored People (“NAACP”) Chairman Julian Bond that were critical of the Bush administration violated the prohibition against campaign intervention.⁸ At the NAACP 2004 National Convention, Bond said, “[T]he election this fall is a contest between two widely disparate views of who we are and what we believe. One view wants to march us backward” The IRS concluded, nearly two years later, that the statement did not violate the conditions of the NAACP’s exempt status.⁹ After the decision was announced, Bond expressed the opinion that the investigation was “initiated for partisan purposes to threaten our right to free speech.”¹⁰

The IRS does not, however, reserve its investigations for the political left. After an investigation into whether Focus on the Family Chairman James Dobson’s endorsement of 2004 Republican candidates violated tax laws, the IRS concluded that the Colorado evangelist acted as an individual, rather than in his capacity as chairman, and therefore his organization was not implicated in political activity.¹¹ In September 2006, the IRS revoked the tax-exempt status of Operation Rescue West, an anti-abortion group, after the group reportedly offered tax deductions in exchange for political contributions that would be used to defeat Senator John Kerry in the 2004 presidential election.¹²

The scope and purpose of this Note is threefold. Part II will provide a brief historical overview of the emergence of churches and nonprofits as a social, economic, and sometimes political presence in America, and will present six policy goals that underlie the tax rules for exempt entities. It will conclude that the IRS has not completely or successfully comprehended the modern-day convergence of social, religious, and political activity among exempt entities and those entities’ need for clear

⁵ See, e.g., Dan Gilgoff, *Turning a Blind Eye, IRS enables Church Politicking*, U.S.A. TODAY, Jan. 29, 2007, at 13A.

⁶ This Note uses the term “churches” to refer generally to all religious organizations or places of worship.

⁷ I.R.C. § 501(c)(3) (2007).

⁸ See Susan Jones, *NAACP Challenging IRS Probe into Its Tax-Exempt Status*, CYBERCAST NEWS SERVICE, Mar. 31, 2006,

<http://www.cnsnews.com/ViewPolitics.asp?Page=/Politics/archive/200603/POL20060331d.html> (last visited Jan. 4, 2008); *IRS Determines NAACP Should Retain Tax Exempt Status*, NAACP, Aug. 31, 2006, available at <http://www.naacp.org/legal/news/2006-08-31> [hereinafter NAACP]. See also Amy R. Murphy, *Revisiting Restrictions on Politicking from the Pulpit*, 16 TAX’N OF EXEMPTS 228, 228 (describing Bond’s criticism of Bush administration).

⁹ Julian Bond, Chairman, NAACP, Remarks at the Take Back America Conference, June 2, 2004, available at http://www.tompaine.com/articles/reclaim_the_land_of_opportun; Ramirez, *supra* note 4.

¹⁰ NAACP, *supra* note 8.

¹¹ See Eric Gorski, *Focus on the Family Nonprofit Status Upheld Amid Complaints*, PRESS-REGISTER, Sept. 15, 2007, at D2.

¹² See Stephanie Strom, *Anti-Abortion Group Loses Tax Exemption*, N.Y. TIMES, Sept. 15, 2006, at A4.

rules and guidance. Part III of this Note will review the law, rules, and guidance, specifically the recent steps taken by the IRS to better inform exempt organizations as to their rights and responsibilities with regard to political campaigns. It will conclude that these efforts are on the whole a positive improvement in clarifying the boundaries of political speech for exempt organizations. Part IV of the Note will review information pertaining to IRS enforcement of the tax rules, including its Political Activities Compliance Initiative (“PACI”). Through the lens of the policy goals, it will evaluate the referral process, investigations into political activities, and what is known of the substance of IRS decisions. It will argue that a “case-by-case” analysis of political activities is proper, but that insufficient communication, loose systems, and tedious investigations erode the ability of the IRS to realize such policy goals.

II. LAW, HISTORY, AND POLICY GOALS FOR CHURCHES AND NONPROFITS

A. 501(C)(3) STATUS

This Note focuses solely on 501(c)(3) organizations, named for the Internal Revenue Code (“the Code”) section that allows “public charities” to benefit from tax exemptions in two ways: such organizations are not required to pay income taxes on their earnings, and any charitable contributions to those organizations are deductible for donors.¹³ Section 501(c)(3) organizations can be “corporations, any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition . . . or for the prevention of cruelty to children or animals.”¹⁴ Section 501(c)(3) is the only tax class that offers deductions to donors for contributions.¹⁵

Because the benefits of tax exemption have been interpreted by courts as a government subsidy,¹⁶ the freedom of philanthropist-donors to contract for services, and of organizations to make use of donations or independent revenue, is limited.¹⁷ Those who utilize the exemption must follow rules that place limits on the organization’s goals and beneficiaries and that are intended to prevent government funds from flowing to individuals or influencing elections or legislation.¹⁸ Three broad prohibitions exist. The first restricts lobbying activity by the organization if it comprises a “substantial part” of the organization’s activities.¹⁹ The second prohibition

¹³ I.R.C. §§ 170, 501(c)(3) (2007).

¹⁴ I.R.C. § 501(c)(3) (2007).

¹⁵ I.R.C. §§ 170, 501(c)(3) (2007).

¹⁶ See *Regan v. Taxation With Representation*, 461 U.S. 540, 544 (1983); *Branch Ministries v. Rossotti*, 40 F. Supp. 2d 15, 31 (D.D.C. 1999). As discussed further in Part II.C, *infra*, the notion of a subsidy is also sometimes framed as a refusal of the government to inhibit through taxation activities by nonprofits that benefit the community and the public interest. See BRUCE R. HOPKINS, *THE LAW OF TAX EXEMPT ORGANIZATIONS* 18 (John Wiley & Sons eds., 1998).

¹⁷ I.R.C. §§ 170, 501(c)(3) (2007).

¹⁸ I.R.C. § 501(c)(3) (2007).

¹⁹ *Id.*

restricts electioneering: the endorsement of or opposition to candidates.²⁰ This provision of the statute was originally enacted by a floor vote in 1954, when Congress approved an amendment by Senator Lyndon Johnson prohibiting 501(c)(3) organizations from supporting candidates;²¹ in 1987, the language was amended again to also preclude organizations from speaking in opposition to candidates.²² The revised portion of the statute now bans “interven[tion] in . . . any political campaign on behalf of (or in opposition to) any candidate for public office.”²³ It is important to note that the provision does not ban 501(c)(3) organizations from simply announcing opposition to or support for certain political decisions, nor from discussing issues,²⁴ but due to the floor vote no legislative history is available to elaborate on this point.²⁵ The third prohibition forbids 501(c)(3) organizations from allowing any part of their net earnings to “inur[e] to the benefit of any private shareholder or individual.”²⁶ This Note will discuss the first two prohibitions relating to political activity: the ban on involvement in political campaigns and, to a lesser extent, the ban on “substantial” lobbying.

The Code of Federal Regulations (“CFR”), building on the Internal Revenue Code, declares that an organization is not exempt if it qualifies as an “action organization.”²⁷ With only slight variations from the Code, the CFR provides that a nonprofit will be considered an action organization if (a) “a substantial part of its activities is attempting to influence legislation by propaganda or otherwise”; (b) “it participates or intervenes, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office;” or (c) it has the two following characteristics: (1) “its main or primary objective or objectives (as distinguished from its incidental or secondary objectives) may be attained only by legislation or a defeat of proposed legislation;” and (2) “it advocates, or campaigns for, the attainment of such main or primary objective or objectives.”²⁸

Churches, along with a small handful of public foundations, are the only organizations not required to apply for 501(c)(3) status; rather, they

²⁰ *Id.*

²¹ Murphy, *supra* note 8, at 229 n.4; H.R. REP. NO. 1337, S. REP. NO. 1622 (Conf. Rep.).

²² Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, sec. 10711, § (b)(1), 101 Stat. 1018 (1987). H.R. REP. NO. 100-495 (Conf. Rep.).

²³ I.R.C. § 501(c)(3) (2007).

²⁴ IRS, U.S. DEP’T OF TREASURY, FACT SHEET FS-2006-17 (Feb. 2006) [hereinafter FACT SHEET]. See also HOPKINS, *supra* note 16, at 511 (describing First Amendment protections in the context of political activity restrictions for nonprofits) (“[T]here is a broad range of clearly action or political undertakings that may be described as the type of speech or activities sheltered by the First Amendment. These undertakings may be manifested in a variety of ways, such as writing, demonstrations, boycotts, strikes, picketing, and litigation, all protected by the rights of free speech and association and the right to petition (assuming the absence of any illegal activities). These activities frequently give the IRS pause in evaluating the status of an organization as a charitable entity but, unless the activities may be fairly characterized as being impermissible lobbying or electioneering, there is no basis in the law concerning action organization . . . for denying an organization engaging in these activities tax-exempt status or for revoking this type of organization’s tax-exempt status.”).

²⁵ Deirdre Halloran, *Keeping Church Political Activities within the Constraints of the Code*, 12 J. TAX’N EXEMPT ORGS. 73 (2000).

²⁶ I.R.C. § 501(c)(3).

²⁷ I.R.C. 1.501(c)(3)-1(c)(3).

²⁸ *Id.*

are automatically free from taxation.²⁹ Otherwise, churches and non-churches are treated mostly the same under § 501(c)(3).³⁰ Despite such similar treatment by the Code, however, restrictions on political activity are often more controversial when applied to churches. On the one hand is the belief that the very nature of a religious institution makes compliance with a restriction on speech difficult.³¹ Most religious institutions, including All Saints, speak out on social and moral issues.³² They are not only governed themselves by moral standards, but believe the larger society should also be so governed; some worship under the belief that the formation of public policy is itself a religious mandate.³³ On the other hand is the perception that the separation of church and state is undermined when churches interfere in government activity or sit too long at the table of political discourse.³⁴

The IRS, as an administrative body within the Department of Treasury, is responsible for administering the Code and has enforcement authority over tax-exempt organizations.³⁵ Within the IRS, the Tax Exempt and Government Entities Division (“TEGE”) is responsible for overseeing churches and charities.³⁶ Part III of this Note will review in more depth the meaning of the various 501(c)(3) provisions, relevant case law, and the guidance provided to nonprofits by the IRS.

B. HISTORY

Since the New Deal, two noteworthy developments have influenced the role of churches and nonprofits in America: First, there has been a marked increase in the prevalence of nonprofits and charitable giving as a percentage of the economy, and second, the government has gradually shifted a good portion of the burden of providing charitable services from itself to private entities.³⁷ Further, because the very idea of nonprofit organizations as an independent, developing sector is relatively new, the relationship between the government, the private sector, and the nonprofit sector, and the influence this “third sector”³⁸ now has on the economy and on society, is largely unstudied.³⁹

Between 1987 and 1997, the nonprofit sector, which includes churches, showed a growth rate of 64.2%, compared to 26.4% for the business sector

²⁹ I.R.C. § 508(c)(1)(A) (2007); I.R.C. § 1.501(d)-1 (2007).

³⁰ I.R.C. § 501(c)(3) (2007).

³¹ See HOPKINS, *supra* note 16, at 507. See also Gilgoff, *supra* note 5 (discussing the “American cultural taboo against government intrusion into churches.”).

³² HOPKINS, *supra* note 16, at 507.

³³ *Id.* See also Chris Kemmitt, *RFRA, Churches and the IRS: Reconsidering the Legal Boundaries of Church Activity in the Political Sphere*, 43 HARV. J. ON LEGIS. 145, 167–69 (2006).

³⁴ See, e.g., Gilgoff, *supra* note 5.

³⁵ I.R.C. § 7802(a) (2007).

³⁶ IRS, *Charities, Churches and Politics* (2007), available at <http://www.irs.gov/newsroom/article/0,,id=161131,00.html>.

³⁷ See JEFFREY M. BERRY & DAVID F. ARONS, *A VOICE FOR NONPROFITS* 6–22 (2005).

³⁸ See THE NON-PROFIT SECTOR IN A CHANGING ECONOMY 62 (Org. for Econ. Cooperation and Dev. ed., 2003).

³⁹ See BRIAN E. DOLLERY & JOE L. WALLIS, *THE POLITICAL ECONOMY OF THE VOLUNTARY SECTOR* 102, 108 (2003).

and 26.2% for all organizations combined.⁴⁰ The nonprofit sector now accounts for 5.2% of the United States' Gross Domestic Product ("GDP") and 8.3% of its citizens' wages and salaries.⁴¹ Between 1994 and 2004, gross revenues for 501(c)(3) organizations grew by 57.1% and total assets grew by 88.3%, adjusted for inflation.⁴² Much of this growth can be traced to growing contributions from the private sector. The private sector's involvement in philanthropy is responsible for the phrases "venture philanthropy" and "social entrepreneurship," which are used to describe the infusion of business principles into the nonprofit sector.⁴³ Charities received \$260 billion from private contributions in 2005,⁴⁴ and it is estimated that between \$21 and \$55 trillion will be donated to charities between 1998 and 2052.⁴⁵ These private contributions amount to about 23% of all monies received by 501(c)(3) organizations; the remaining 71% comes from the charities' own service revenues, including government grants.⁴⁶

The vast majority of exempt organizations are 501(c)(3)s, and about 350,000, or 41%, of those are religious congregations.⁴⁷ These congregations not only constitute a large percentage of the nonprofit sector, but they also control a large percentage of the sector's money. Over a third of all private giving went to religious organizations in 2006.⁴⁸ This is more than twice as much as was received by any other single category of exempt organizations.⁴⁹ These figures are attributable in part to the fact that donors who are members of religious organizations were not only twice as likely to give in 2000, but also gave twice as much as non-church-goers, especially if they attended religious services regularly.⁵⁰

Given their strong presence in the nonprofit sector, both by numbers and by dollars, it follows that churches are able to provide a vast array of services to the community. They are involved in, among many other things, the prevention of teen pregnancy, fighting crime and substance abuse, community development, education, and child care.⁵¹ Of course, churches also serve the community through less tangible means. Whether supporters of religion view it as helping individuals, helping communities, or both,

⁴⁰ See BERRY & ARONS, *supra* note 37, at 9. See also HOPKINS, *supra* note 16, at 25.

⁴¹ NATIONAL CENTER FOR CHARITABLE STATISTICS, URBAN INSTITUTE, THE NONPROFIT SECTOR IN BRIEF: FACTS AND FIGURES FROM THE NONPROFIT ALMANAC 2007.

⁴² *Id.*

⁴³ See THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38, at 111.

⁴⁴ John J. Havens, Mary A. O'Herlihy & Paul G. Schervish, *Charitable Giving: How Much, by Whom, to What, and How?*, in THE NON-PROFIT SECTOR: A RESEARCH HANDBOOK 542 (2006).

⁴⁵ *Id.*

⁴⁶ National Center for Charitable Statistics, *NCCS Quick Facts*, THE URBAN INSTITUTE (2004), available at <http://nccsdataweb.urban.org/NCCA/files/quickFacts.htm>. See also THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38 at 64 (explaining that earned income is the fastest growing source of income for nonprofits—54% of revenues come from earned income fees and charges).

⁴⁷ NATIONAL CENTER FOR CHARITABLE STATISTICS, URBAN INSTITUTE, *supra* note 41.

⁴⁸ *Id.*; Havens, O'Herlihy & Schervish, *supra* note 44, at 556.

⁴⁹ NATIONAL CENTER FOR CHARITABLE STATISTICS, URBAN INSTITUTE, *supra* note 41.

⁵⁰ See generally Havens, O'Herlihy & Schervish, *supra* note 44, at 550. See also DOLLERY & WALLIS, *supra* note 39, at 257.

⁵¹ See SACRED PLACES, CIVIC PURPOSES: SHOULD GOVERNMENT HELP FAITH-BASED CHARITY? (E.J. Dionne Jr. & Ming Hsu Chen, eds. 2001) [hereinafter SACRED PLACES].

religion is seen as providing ‘an initial basis of cooperation by grounding such action in a set of common values, goals, and commitments to the public good. . . . At its best, religion has provided a moral basis to conceive of our place in a larger human society and inspired people to work for racial equality, social justice, and democracy.’⁵²

Over the past few decades, a number of changes in the structure of federal budgeting have fostered the creation of a “shadow government” in the realm of charitable services. “Follow[ing] the federal structure of US government,”⁵³ this network of nonprofits keeps the official government workforce small. The federal government issues grants or subcontracts directly to nonprofits, or it shifts discretionary and block grants to state governments, which in turn often contract out to nonprofits as well.⁵⁴ Government funding accounts for a substantial percentage of working revenue in the nonprofit sector.⁵⁵ For non-health-related 501(c)(3)s, government funding accounts for about 20% of revenues; this percentage jumps significantly for the health and human services category, which relies on the government for 33% of its funding.⁵⁶ Nonprofits then leverage the stature created by the large percentage of government funding to increase their private contributions.⁵⁷ In the 1980s, when cuts to government programs left some nonprofits vulnerable, they turned increasingly to these established private funding sources to ensure long-term stability.⁵⁸

Considering such growth in the sector it comes as no surprise that nonprofits carry out many of the functions that are essential to American society, and which were once reserved for government.⁵⁹ The effects of such a shift are not insignificant. For better or worse, this arrangement has effectively severed the direct link between government and its neediest citizens.⁶⁰ “Indeed, the modern welfare state has largely been subcontracted to nonprofits.”⁶¹ The initial justification for the shift of such a large portion of government monies to the private sector was that private providers were inherently apolitical and had no stake in the game.⁶² Of course, as soon as responsibility for such a large percentage of charitable work shifts to private organizations, it is easy to imagine that a framework might be constructed for an economic and social machine with the potential to become a political force.⁶³

⁵² *Id.* at 2 (quoting sociologist Mark R. Warren).

⁵³ See DOLLERY & WALLIS, *supra* note 39, at 114.

⁵⁴ See BERRY & ARONS, *supra* note 37, at 17–19.

⁵⁵ *Id.* at 8.

⁵⁶ *Id.* at 8–10. The percentage of government funding for health and human services is even higher if you consider service fees paid to these organizations from government program dollars.

⁵⁷ *Id.* at 14.

⁵⁸ See THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38, at 63–64.

⁵⁹ See BERRY & ARONS, *supra* note 37, at 6.

⁶⁰ *Id.* at 15.

⁶¹ *Id.* at 3.

⁶² *Id.* at 6.

⁶³ See THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38, at 240–41 (“[T]he non-profit sector in the United States serves as an advocate on behalf of those who criticize or seek to change either government or for-profit activity. It mobilizes public attention to community problems or needs and allows people to be heard on issues that they consider important. . . . Both those seeking to preserve old values, ideals, and traditions, and those seeking to change them or create new ones utilize non-profit

Churches have historically involved themselves in social issues and advocacy⁶⁴ but have mostly abstained from direct involvement in politics.⁶⁵ In recent times, however—especially over the last fifteen years—churches and other nonprofit organizations have taken on a much more visible role in political campaigns and lobbying efforts, by inviting politicians to speak, establishing voter education and registration initiatives, and forming non-exempt “sister” organizations through which to participate freely in politics.⁶⁶ Most likely as a result of the Civil Rights Movement, black churches were the first to actively encourage their congregations to participate in politics.⁶⁷ Around the same time, some nonprofit organizations like the NAACP made use of the first “issue oriented” voter guides.⁶⁸ In the 1970s and 1980s, more right-leaning organizations and churches began to recognize and realize their own political opportunities.⁶⁹ Activism by conservative groups was initially credited to the Reverend Jerry Falwell. Although the message of his “moral majority” was well known, political success was fleeting and the group folded in the late 1980s.⁷⁰ It was quickly replaced by Pat Robertson’s Christian Coalition, whose mission was even more forthrightly committed to political involvement and influence.⁷¹ In more recent years, although churches of all types have been more active,⁷² many credit the Republican Party and the

organizations. In addition, the sector facilitates the development of bonds of trust and solidarity that make joint community action possible.”).

⁶⁴ Some churches are more involved than others. One study reports that six factors influence a church’s likelihood of participating in social service: size, income, racial makeup, need in the area, theological and political orientation, and leadership. See Avis C. Vidal, *Many Are Called, but Few Are Chosen: Faith-Based Organizations and Community Development*, in SACRED PLACES, *supra* note 51, at 130. There is also a difference between the types of services provided. While some churches run programs themselves, others are more likely to donate money or volunteers. *Id.* at 133. Another view emphasizes this wide variance in service activities among churches and their focus on the immediate needs of individuals. See Mark Chaves, *Testing the Assumptions: Who Provides Social Services?* in SACRED PLACES, *supra* note 51, at 288–89 (“The median dollar amount spent by congregations in direct support of social service programs is approximately \$1,200, or 3 percent of the median congregation’s total budget. . . . The basic picture is clear: although most congregations participate in some sort of social service activity, only a small minority actively and intensively engage in such activity.”).

⁶⁵ See Jerome Park Prather, Comment, *Tax Exemption of American Churches and Other Nonprofits: One Election Cycle After Branch Ministries v. Rossotti*, 94 KY. L.J. 139, 142 (2005–06).

⁶⁶ See Kemmitt, *supra* note 33, at 156–59. There are two alternatives to § 501(c)(3) status that allow organizations to participate more freely in politics. Section 501(c)(4) organizations are allowed to remain tax exempt themselves, but contributions from donors are no longer deductible. They are usually “civic leagues or organizations” that are (1) not organized for profit and (2) “operated exclusively for the promotion of social welfare.” They may engage in political campaign and lobbying activity as long as it is not their primary activity. 26 C.F.R. § 1.501(c)(4)-1(a)(2) (2007). By contrast, § 527 organizations are typically political parties or political action committees (PACs) whose primary purpose is political activity. Tax exemptions for 527 organizations are thus limited to “indirect expenses” that support the organization’s political activity, as opposed to “directly related expenses” that support an individual’s campaign. 26 C.F.R. § 1.527-2(c)(1)-(2) (2007).

⁶⁷ See Stephanie Simon, *Pastors Guiding Voters to GOP*, L.A. TIMES, Oct. 1, 2006, at A1. It is also interesting to note that black churches are widely known for being the most active in their communities, a phenomenon explained by a history of discrimination, segregation, and exclusionary practices. See Vidal, *supra* note 64 at 131. See also Vaughn E. James, *Reaping Where They Have Not Sowed: Have American Churches Failed to Satisfy the Requirements for the Religious Tax Exemption?*, 43 CATH. LAW. 29, 63–69 (2004).

⁶⁸ See Simon, *supra* note 67.

⁶⁹ See James, *supra* note 67, at 55–63.

⁷⁰ See *id.* at 56–57.

⁷¹ *Id.* at 57–61.

⁷² See Josh Getlin, *The Race for the White House: Pulpits Ring with Election Messages*, L.A. TIMES, Nov. 1, 2004, at A1.

latest Bush administration as innovators in the effort to directly cultivate support from churches.⁷³ Few will argue those efforts were in vain; the assistance of churches and faith-based groups during the 2004 election cycle helped lead to huge successes for conservative causes and conservative candidates.⁷⁴ Church-based campaigning may even have been the most influential factor in voter choice that year.⁷⁵ It also helped to ignite a storm of media attention.⁷⁶

In 2006, many conservative groups mobilized in a concerted effort to build on the success of the 2004 cycle and affect the 2006 mid-term election. Focus on the Family organized a sweeping voter registration drive in eight states with the goal of courting millions of new voters, utilizing strategies such as placing informational inserts into church publications and setting up registration booths outside places of worship.⁷⁷ But conservatives have taught the rest of the political spectrum a thing or two about modern politics, and now religious groups across the political spectrum are using what they have learned to court their religious bases.⁷⁸

These efforts by churches seem to emphasize a motivation coming from within them to speak out on issues and get more involved. However, a different argument explaining the increased political involvement by churches emphasizes their defensive posture. Under this second theory, churches are not entering the arena out of a desire to achieve changes in the larger society, but rather are being forced to fight for their political speech rights in an atmosphere of growing hostility toward religion and religious organizations by a secular citizenry, the courts, or an unwelcome and fast approaching multiculturalism.⁷⁹

Increased political activity on the part of nonprofits is harder to gauge. As do some churches, some nonprofits completely refrain from involving themselves in any kind of overtly political activity, including permitted activities such as voter education and mobilization.⁸⁰ Although such significant growth in the nonprofit sector is almost sure to result in increased political activity, both due to increases in economic influence and increases in the number of active nonprofits, there is not a comparable focus on non-church nonprofits in the press and in public discussion as

⁷³ See Peter Slevin, *Ohio Churches' Political Activities Challenged*, WASH. POST, April 25, 2006, at A03. See also Peter Wallsten, *Conservatives Put Faith in Church Voter Drives*, L.A. TIMES, Aug. 15, 2006, at A1. Attorney General Phil Kline, a Republican from Kansas, sent a memorandum to his campaign staff mid-year 2006 instructing them to arrange as many campaign stops at churches as possible and to establish miniature campaign committees in each church. The memo included a list of churches that had agreed to distribute his campaign literature. See Strom, *supra* note 12.

⁷⁴ See Kemmitt, *supra* note 33, at 156–59.

⁷⁵ See Simon, *supra* note 67.

⁷⁶ See, e.g., *id.*

⁷⁷ See Wallsten, *supra* note 73, at A1.

⁷⁸ See Simon, *supra* note 67, at A1; Gilgoff, *supra* note 5 (“Most of us have become familiar with the sight of Democratic candidates addressing liberal African-American congregations from the pulpit after being introduced by a pastor who is clearly making an endorsement.”).

⁷⁹ See Diana B. Henriques, *In the Congressional Hopper: A Long Wish List of Special Benefits and Exemptions*, N.Y. TIMES, Oct. 11, 2006, at A20; James, *supra* note 67 at 15. But see IRA C. LUPU & ROBERT W. TUTTLE, GOVERNMENT PARTNERSHIPS WITH FAITH-BASED SERVICE PROVIDERS 23–25 (2002) (outlining recent Supreme Court decisions that further the faith-based initiative).

⁸⁰ See BERRY & ARONS, *supra* note 37, at 94.

there is on church-based activity.⁸¹ Despite the lack of publicity, however—or perhaps because of it—the IRS has demonstrated a greater likelihood of stripping these organizations of their exempt status.⁸²

Whatever the cause of increased political activity by exempt organizations, the IRS has stated that, despite its reluctance to revoke an organization's exempt status, it intends to take a tougher stance on violations of the Code in response to what it views as a sharp increase in prohibited activities⁸³ and “a disturbing amount” of intervention into the 2004 election.⁸⁴ However, although the IRS has acknowledged increased political activity by nonprofits, they have neither traced the root causes of such activity nor comprehended the scope of the growth in the sector.⁸⁵ The IRS may need to adjust its strategy for enforcing the tax rules in order to fully recognize the increased economic and political stature of these entities. Additionally, any new strategy must be developed within the context of a larger public and legal policy framework so that the ambitious policy goals underlying the rules for exempt organizations are effectively realized. This Note reviews some goals of the tax-exempt status below.

C. POLICY GOALS

The IRS carries out its policy priorities not only through the mechanisms it sets up to collect revenue; the same priorities are reflected in the exemptions it grants. The exemptions serve as “a fiscal, economic and social policy tool.”⁸⁶ Especially in the nonprofit sector, the system of taxation and exemptions serves as a powerful instrument with which governments can dramatically affect an organization's funding, and thereby its success.⁸⁷ Although there are a myriad of theoretical and actual influences on the formation of public policy, both historical and emerging,⁸⁸ this Note identifies and explores six broad goals that seem to underlie tax policy generally with regard to exempt entities, and which help to influence the crafting of rules that exempt organizations and the IRS follow.

⁸¹ See, e.g., Peter Wallsten, *Tactic Uses Pulpits to Power the GOP*, L.A. TIMES, Sept. 23, 2006, at A12.

⁸² See Jones, *supra* note 8; Strom, *supra* note 12. In a recent statement, Republican Senator Chuck Grassley of Iowa, a ranking member of the Finance Committee, announced that he is actively investigating whether nonprofit groups engage in inappropriate political activity. *Sen. Grassley: Review of Non-Profits' Political Activity Continues, Despite Fannie Mae Foundation Move*, U.S. FED. NEWS, Feb. 23, 2007. See also Todd Milbourn, *Conservative Group Gains Momentum in War Debate*, SACRAMENTO BEE, Sept. 10, 2006 (discussing the need to protect “the integrity of the charitable sector”).

⁸³ See Strom, *supra* note 12, at A4.

⁸⁴ See David D. Kirkpatrick, *Pastors' Get-Out-the-Vote Training Could Test Tax Rules*, N.Y. TIMES, Mar. 21, 2006, at A15.

⁸⁵ Remarks of IRS Commissioner Mark W. Everson at the City Club of Cleveland, Ohio, Feb. 24, 2006, available at <http://www.irs.gov/irs/article/0,,id=154788,00.html>.

⁸⁶ See Donna D. Adler, *The Internal Revenue Code, The Constitution, and the Courts: The Use of Tax Expenditure Analysis in Judicial Decision Making*, 28 WAKE FOREST L. REV. 855, 859 (1993).

⁸⁷ See DOLLERY & WALLIS, *supra* note 39, at 133.

⁸⁸ See *id.* at 103.

1. *Benefits for a Loosely Identified Group of Beneficiaries*

The Code lists religious, educational, scientific, and other “charitable” causes, excluding direct benefits to individuals or private entities.⁸⁹ The identified categories are recognized to have not just social, but also sometimes emotional⁹⁰ and moral⁹¹ value. The definition of “charitable” is rooted in common law, and specifies simply that the status must be justified in social terms.⁹² The Code thus endorses broad support of socially beneficent causes, even if they are sometimes unpopular with the public.⁹³ Congress, while writing the Revenue Act of 1913, in an effort to keep tax policy consistent with the political philosophy of the day, created the exemption for charitable organizations and viewed the Revenue Act as “an extension of comparable practice throughout the whole of history.”⁹⁴

Under this policy, the benefits to all concerned are greatest when government involvement is limited. First, government is willing to forego tax revenue in order to be freed of some burdens.⁹⁵ Sometimes referred to as the “subsidization model,”⁹⁶ or the “public good rationale,” it identifies categories of charitable activity that, absent the exemption, would likely be performed by government.⁹⁷ But beyond being freed of a burden, there are other reasons for the view that government should be involved to the smallest extent possible in charitable activity.⁹⁸ The notion of “social capital” was espoused in the Twentieth Century to recognize, in part, that activity which comes from the community and directly benefits society also includes larger, indirect benefits to the providers and donors themselves.⁹⁹

Federal courts have reinforced many of these arguments. In 1924, the Supreme Court in *Trinidad v. Sagrada Orden* stated that the exemption helps corporations in completing activities that are not conducted for private gain, and which in turn benefit society.¹⁰⁰ In the 1970s, the Court acknowledged the less tangible aspect of the goal, describing nonprofit groups in *Walz v. Tax Commission* as “beneficial and stabilizing influences in community life.”¹⁰¹ One federal appeals court maintained in 1951 that

⁸⁹ See *Presbyterian and Reformed Publ'g Co. v. Comm'r of Internal Revenue*, 743 F.2d 148, 153 (1984).

⁹⁰ See DOLLERY & WALLIS, *supra* note 39, at 50.

⁹¹ See D. Alexander Ritchie, *Intermediate Sanctions: Controlling the Tax-Exempt Organization Manager*, 18 VA. TAX REV. 875, 896 (1999).

⁹² See *Bob Jones Univ. v. United States*, 439 F.2d 147, 151 (4th Cir. 1980). See also Ritchie, *supra* note 91, at 893.

⁹³ For example, a number of exempt organizations support AIDS groups, Muslim orphans and widows in war-torn countries, and non-traditional religions. See BERRY & ARONS, *supra* note 37 at 7; *United States v. Damrah*, 334 F. Supp. 2d 967 (N.D. Ohio 2004).

⁹⁴ HOPKINS, *supra* note 16, at 13.

⁹⁵ See *id.* But see Terry L. Slye, *Rendering Unto Caesar: Defining 'Religion' for Purposes of Administering Religion-Based Tax Exemptions*, 6 HARV. J.L. & PUB. POL'Y 219, 248–249 (1983) (addressing whether the conducting of religious services by religious institutions relieves the government of any burden).

⁹⁶ See David M. Andersen, Comment, *Political Silence at Church: The Empty Threat of Removing Tax-Exempt Status for Insubstantial Attempts to Influence Legislation*, 2006 B.Y.U. L. REV. 115, 143 (2006).

⁹⁷ See Ritchie, *supra* note 91, at 893.

⁹⁸ See HOPKINS, *supra* note 16, at 11.

⁹⁹ See DOLLERY & WALLIS, *supra* note 39, at 86–87.

¹⁰⁰ See *Trinidad v. Sagrada Orden de Predicadores de la Provincia del Satisimo Rosario de Filipinas*, 263 U.S. 578, 581 (1924).

¹⁰¹ See *Walz v. Tax Comm'n*, 397 U.S. 664, 673 (1970).

nonprofits “provid[e] a relief of the public of a burden that otherwise belongs to it.”¹⁰²

2. *Philanthropy*

Charitable institutions benefit not just from their own exemption, but also benefit significantly from the application of private wealth, usually made possible by deductions to donors, to specific purposes in the public interest.¹⁰³ Sometimes referred to as the “donative rationale,” this goal draws on the theory that without a tax deduction for donations there is a tendency for donative goods to be undersupplied.¹⁰⁴ The incentive for private donors to donate to 501(c)(3) organizations is twofold: the rules allow donors to deduct the contribution from income while simultaneously prohibiting the recipient organization from using the donation for purposes other than “charitable” ones.¹⁰⁵ Donors can therefore be assured that their donations will be used for the intended purpose. This desire for the efficient use of philanthropic dollars can also be explained through economic theory as a contract or market failure in the for-profit market. Under a “demand-side” analysis, philanthropist consumers prefer not to contract with for-profit entities, where there is no restraint on the distribution of profits. They prefer instead to contract with nonprofit entities, which are required by law to use all of their earnings for the delivery of services.¹⁰⁶

Philanthropy is not just efficient and necessary, though. Implicit in this goal is also a historical desire for community involvement among donors, which is seen as a uniquely American ideal.¹⁰⁷ It follows, then, that donations to nonprofits are not viewed as taxable events, because nonprofits are able to collect and expend them as though they were expended by individual donors.¹⁰⁸ As indicated in Part I, these unique characteristics of 501(c)(3) organizations help donors to fuel a massive machine of charitable work. As a corollary, the nonprofit sector has become very effective at soliciting donations.¹⁰⁹

3. *Efficient and Creative Charitable Services*

Similar to the policy prerogatives underlying the philanthropy goal, economic theories of government incapacity and market failure help to explain this goal.¹¹⁰ The nonprofit sector is viewed as filling the void where governments and the for-profit market fail, or fail to provide services at a level that consumers desire.¹¹¹ What consumers desire are unique kinds of

¹⁰² See *Duffy v. Birmingham*, 190 F.2d 738, 740 (8th Cir. 1951).

¹⁰³ See HOPKINS, *supra* note 16, at 14.

¹⁰⁴ See Ritchie, *supra* note 91, at 895–96.

¹⁰⁵ See Adler, *supra* note 86, at 859–65; I.R.C. § 501(c)(3).

¹⁰⁶ See HOPKINS, *supra* note 16, at 21. See also Ritchie, *supra* note 91, at 894–95.

¹⁰⁷ See HOPKINS, *supra* note 16, at 16.

¹⁰⁸ *Id.* at 19.

¹⁰⁹ See DOLLERY & WALLIS, *supra* note 39, at 43.

¹¹⁰ See HOPKINS, *supra* note 16, at 21.

¹¹¹ See DOLLERY & WALLIS, *supra* note 39, at 12. See also BERRY & ARONS, *supra* note 37, at 6. (“Economists offer a straightforward explanation of the rise of nonprofits in areas in which government itself directly offers services, such as health care, social services, and education. In their view, when

services, or government-type services delivered more efficiently and with less intrusion into the lives of individuals.¹¹² The Code accommodates this desire by placing no substantive restrictions on the manner in which such services are provided.¹¹³

John Stewart Mill recognized this need for pluralism, expressing the view that government benefits from “varied experiments, and endless diversity of experiences.”¹¹⁴ Examples of such “varied experiments” can be found in the nonprofit world, where the pressure to create profits does not prevent the implementation of effective service.¹¹⁵ Nonetheless, private organizations are still better at providing services inexpensively, typically only relying on government for a quarter of their operating costs.¹¹⁶ Philanthropists reinforce the efficiency goal in a broad sense, by focusing in recent years on the root causes of societal problems and granting charitable dollars for the prevention of societal harms instead of rehabilitation from them.¹¹⁷

4. *Insulation from the Private Sector*

Restrictions on the use of nonprofit dollars protect the for-profit sector by ensuring that tax-free dollars do not compete in the marketplace with taxed dollars. Nonprofits are not restricted from generating income, or from making profits within the realm of their charitable activities, but they may not disadvantage non-exempt entities by competing alongside them.¹¹⁸ Nonprofits also benefit from this insulation by encouraging for-profit investors to make charitable donations. Because investors in for-profit organizations are limited in their ability to take deductions on their investments, even in the case of a loss, they are often motivated to donate private capital to nonprofits to take advantage of the useful tax incentives.¹¹⁹ The restrictions also prevent funds from being improperly used for political purposes. Not only would it be improper for non-taxed dollars to compete with taxed dollars in the realm of political donations, it

government offers services it will aim to satisfy the demand of the median voter. (In plain English: government will offer what the typical consumer wants but nothing more extensive than that.)”

¹¹² See E.J. Dionne Jr. & Ming Hsu Chen, *When the Sacred Meets the Civic: An Introduction*, in SACRED PLACES, *supra* note 51, at 3.

¹¹³ I.R.C. § 501(c)(3).

¹¹⁴ See HOPKINS, *supra* note 16, at 11.

¹¹⁵ The Idaho Youth Ranch for troubled students is one example of such creativity. There, young men and women attend school while working on the ranch, and receive an education that better serves their needs. Although one can hardly imagine the government tackling such unusual projects on a broad scale, it may also be difficult for a for-profit entity to find enough students who could pay for it. See BERRY & ARONS, *supra* note 37, at 3.

¹¹⁶ *Id.* at 20.

¹¹⁷ The Bill and Melinda Gates Foundation, which recently made a large donation to New York City Public Schools, has been cited as one example of this effort to get at efficiency through what is perceived to be a more effective use of funds. See Paulo Botas, *New York City Schools to Receive \$51 Million from Gates Foundation*, CITYMAYORS.COM, available at <http://www.citymayors.com/news/nycschoolsgates.html>.

¹¹⁸ I.R.C. § 1.501(d)-1 (2007). See *Presbyterian and Reformed Publ'g Co. v. Comm'r of Internal Revenue*, 743 F.2d 148 (3rd Cir. 1984). See also IRS, U.S. DEPT. OF TREAS., PUBLICATION 1828, TAX GUIDE FOR CHURCHES (2006) [hereinafter GUIDE].

¹¹⁹ See THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38, at 110.

would also implicate government involvement in that activity because of the subsidization.¹²⁰

5. *Freedom to Carry Out a Religious or Social Purpose*

The first component of this goal is the simple notion that government should refrain from any involvement in a church's religious or spiritual mission. Exemptions for churches are rooted both in Establishment Clause protections separating church activity from state activity and, perhaps more significantly, in historical exemptions for churches.¹²¹ The goal not only reflects a widely held notion among the public that autonomous religious pursuit and activity add value to society,¹²² but also reconfirms the Congressional commitment to acknowledging the unique role of churches and religious organizations in American society.¹²³ This rationale extends to all nonprofits, whose donations are exempt from taxation so that donors may carry out the social cause they select without government interference in the form of taxation.¹²⁴

A second aspect of this policy priority recognizes that there is a fine line between social service by churches as a component of the religious mission and social service as an aid to or partnership with government. It is undeniably both, and the significance of the contribution of churches to social projects (leaving aside their religious contribution) is only recently being studied within the scope of the larger nonprofit sector.¹²⁵ The tax exemption becomes especially controversial for churches who receive government grants to provide social services.¹²⁶ Most critics will concede the policy choice is not a question of whether governments and churches can work together to take advantage of charitable activity offered by churches, but how they can most effectively work together.¹²⁷ It is somewhat difficult to distinguish a religious institution's contribution to community service from religious indoctrination, proselytizing, or politicking. Are churches "service providers or prophetic interrogators?"¹²⁸ Public trust regarding the separation of church and state has its limits,

¹²⁰ See *Regan*, 461 U.S. at 544; *Branch Ministries*, 40 F. Supp. 2d at 31.

¹²¹ See James, *supra* note 67, at 32–42; Kemmitt, *supra* note 33, at 147–51; HOPKINS, *supra* note 16, at 13. See also Andersen, *supra* note 96; Adler, *supra* note 86, at 246–47.

¹²² See Andersen, *supra* note 96, at 151–52.

¹²³ *Id.* at 123.

¹²⁴ See BERRY & ARONS, *supra* note 37, at 60.

¹²⁵ See THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38, at 256.

¹²⁶ Until recently, federal grants to charitable organizations did not include grants to faith-based organizations. The Bush administration's White House Office of Faith-Based and Community Initiatives recognizes the new policy that organizations providing services to elders, the homeless, at-risk youth, or those transitioning from welfare to work are eligible for grant monies, regardless of whether they are religious organizations. WHITE HOUSE FAITH BASED AND COMMUNITY INITIATIVES, WHITE HOUSE, FEDERAL FUNDS FOR ORGANIZATIONS WHO HELP THOSE IN NEED (2006). Many are surprised that conservative churches receive less in government grants than less conservative ones. See Dionne & Chen, *supra* note 112, at 11.

¹²⁷ See Julie A. Segal, *Even Church-State Separationists Care about Serving the Poor*, in SACRED PLACES, *supra* note 51, at 104.

¹²⁸ See Jim Wallis, *Eyes on the Prize*, in SACRED PLACES, *supra* note 51, at 146.

despite protestations from the faithful that service to others does not necessarily entail bringing the recipients of services into the faith.¹²⁹

6. *Recognition of Exempt Entities' Voice in the Community, Within Specified Limits*

Especially in light of the lack of direct contact between the “shadow government” and its citizens, this goal acknowledges that civic engagement and social capital are two essential components of the nonprofit sector.¹³⁰ Exempt entities have latitude to enter the realm of political speech and activism if they choose to, while at the same time being precluded from issuing political endorsements and lobbying. Similar to the “accommodation model,” which allows churches to operate free of financial burdens, it emphasizes the need to allow churches and church leaders to encourage their members in “applying religious doctrines to real-world issues.”¹³¹ Churches increasingly want to exercise this role in policy-making,¹³² hoping religion can “get some respect” in the civic and policy dialogues and somehow avoid notions that faith is only a private and personal endeavor.¹³³

Each of the above six goals is implicated in the attempt to resolve the challenges surrounding IRS investigations into exempt organizations. The IRS is tasked with balancing these complex priorities and needs, which can sometimes conflict when practically applied to the law.

III. LEGAL RULES AND RECENT COMMUNICATION EFFORTS BY THE IRS

There is little case law relating to political activity by exempt entities, and even less information can be found in the congressional record.¹³⁴ Because the IRS has rarely stripped organizations of their tax exempt status, and because there is no public record of IRS investigations, internal deliberations, or decisions,¹³⁵ it is difficult to predict how the IRS may conclude an investigation. This Part of the Note will briefly review what legal frameworks do exist, focusing primarily on guidance issued by the IRS for 501(c)(3) organizations.

A. POLITICAL ACTIVITY DETERMINATIONS: THE CASE LAW

The case law on the subject of political activity by 501(c)(3) organizations seems to illustrate “easy cases,” where there has been little

¹²⁹ See Dionne & Chen, *supra* note 112, at 9; Pietro Nivola, *Redefining the Mission of Faith-Based Organizations in Community Development*, in SACRED PLACES, *supra* note 51, at 149. See also HOPKINS, *supra* note 16, at 507.

¹³⁰ See DOLLERY & WALLIS, *supra* note 39, at 86–87. See also THE NON-PROFIT SECTOR IN A CHANGING ECONOMY, *supra* note 38, at 241.

¹³¹ See Andersen, *supra* note 96, at 147–48.

¹³² See Wallis, *supra* note 128, at 147; David Saperstein, *Appropriate and Inappropriate Use of Religion*, in SACRED PLACES, *supra* note 51, at 297.

¹³³ See Peter Steinfels, *Holy Waters: Plunging into the Sea of Faith-Based Initiatives*, in SACRED PLACES, *supra* note 51, at 329.

¹³⁴ See Halloran, *supra* note 25.

¹³⁵ See I.R.C. § 6103(a) (2007).

question that the actions taken by the exempt organizations were inappropriate and illegal. As a foundational issue, in the 1983 case, *Regan v. Taxation With Representation*, the Supreme Court discussed the notion that tax benefits offered to organizations under § 501(c)(3) are a form of subsidization of those entities.¹³⁶ In *Regan*, the IRS denied a taxpayer advocacy group 501(c)(3) status after concluding that a substantial part of the group's activities consisted of lobbying, in violation of § 501(c)(3).¹³⁷ The Court held that the prohibition against substantial lobbying is constitutional under the First Amendment because the organization's speech was not substantially burdened by their choice between giving up tax-free donations,¹³⁸ a subsidy, and exercising their right to lobby.¹³⁹ The Court stated,

Both tax exemptions and tax deductibility are a form of subsidy that is administered through the tax system. . . . The system Congress has enacted provides this kind of subsidy to nonprofit civic welfare organizations generally and an additional subsidy to those charitable organization that do not engage in substantial lobbying.¹⁴⁰ In short, Congress chose not to subsidize lobbying as extensively as it chose to subsidize other activities that nonprofit organizations undertake to promote the public welfare.¹⁴¹

The Court went on to state, "Congress has merely refused to pay for the lobbying out of public moneys. The Court has never held that Congress must grant a benefit . . . to a person who wishes to exercise a constitutional right."¹⁴²

In 1972, in *Christian Echoes National Ministry v. United States*, the Tenth Circuit helped to define the prohibition against interference in a political campaign.¹⁴³ In *Christian Echoes*, the IRS revoked a nonprofit corporation's exempt status upon reexamination of its activities and finances. One ground for the revocation was direct and indirect intervention in a political campaign. The Tenth Circuit upheld the IRS decision, concluding that the corporation's use of publications and broadcasts to attack candidates it considered too liberal, to urge its followers to elect or defeat other candidates, and its endorsement of a senator at its annual convention constituted improper interference in an election, in violation of

¹³⁶ See *Regan*, 461 U.S. at 544.

¹³⁷ See *Regan*, 461 U.S. 540; 26 C.F.R. § 1.501(c)(3) (2007) ("[A]n organization will be regarded as attempting to influence legislation if the organization: (a) Contacts, or urges the public to contact, members of a legislative body for the purpose of proposing, supporting, or opposing legislation; or (b) Advocated the adoption or refection of legislation.").

¹³⁸ The advocacy group had the option to become a 501(c)(4) organization. See *supra* text accompanying note 66.

¹³⁹ See *Regan*, 461 U.S. at 540. In response to the advocacy group's argument that Congress's decision to allow veteran groups to lobby while maintaining their 501(c)(3) status violated the equal protection clause of the Fifth Amendment, the Court went on to hold that the distinction made by Congress for veteran groups was unlike distinctions of race or national origin and therefore permissible. *Id.* at 548.

¹⁴⁰ The additional subsidy refers to deductible contributions not available to 501(c)(4) and 527 organizations due to their substantial engagement in political activity.

¹⁴¹ *Id.* at 544.

¹⁴² *Id.* at 545.

¹⁴³ See *Christian Echoes Nat'l Ministry v. United States*, 470 F.2d 849 (10th Cir. 1972) (overturning district court's holding that it was improper to inquire into whether an organization's actions were religious or political).

§ 501(c)(3).¹⁴⁴ The court held that the limitations did not deprive the ministry of its free speech rights, explaining, “The taxpayer may engage in all such activities without restraint, subject, however, to withholding of the exemption or, in the alternative the taxpayer may refrain from such activities and obtain the privilege of exemption.”¹⁴⁵ The court’s rationale demonstrates that the receipt of the benefits of tax exemptions includes the choice to accept and abide by the limitations inherent to the subsidy.

The most recent case regarding the prohibition against interference in a political campaign came in 2000 in *Branch Ministries, Inc. v. Rossotti*,¹⁴⁶ the first case in which the IRS stripped a church of its exempt status. *Branch Ministries* concerned interference into the 1992 presidential election. A New York church had published multiple, full-page newspaper advertisements just days before the election between Bill Clinton and George H.W. Bush, encouraging voters not to elect Clinton. A U.S. District Court held that the revocation was proper because the church had published a statement in opposition to a candidate for public office, in clear violation of § 501(c)(3).¹⁴⁷ Addressing the church’s argument that its free exercise rights were substantially burdened because it was effectively pressured to modify its religious behavior in order to comply with § 501(c)(3), the court said the revocation was caused by the organization’s choice to accept 501(c)(3) status and engage in political activity, and that the choice did not burden its free exercise rights. Applying an unusual strict scrutiny analysis to the claim, the court explained that even if the plaintiffs were substantially burdened, “the government has a compelling interest in maintaining the integrity of the tax system and in not subsidizing partisan political activity, and Section 501(c)(3) is the least restrictive means of accomplishing that purpose.”¹⁴⁸ The D.C. Circuit Court subsequently upheld the constitutionality of the ban on intervention in a political campaign by 501(c)(3) organizations.¹⁴⁹

B. IRS GUIDANCE

In closer cases, 501(c)(3) organizations are forced to rely on IRS revenue rulings and other guidance for an interpretation of where the line is drawn between permissible and impermissible political activities. The IRS has issued election year advisories to the nonprofit sector since 1992 on the state of the law for exempt entities,¹⁵⁰ and in the last three years it has taken concerted steps to provide even more detailed guidance to help nonprofits identify the political lines they are not allowed to cross without

¹⁴⁴ The court also held that the corporation had improperly influenced legislation by attempting to sway public opinion through published speeches. *Id.* at 855.

¹⁴⁵ *Id.* at 857.

¹⁴⁶ *Branch Ministries*, 40 F. Supp. 2d at 15.

¹⁴⁷ *Id.* at 20.

¹⁴⁸ *Id.* at 25. The standard of review adopted by the U.S. District Court is discussed in further detail in Part IV.C of this Note.

¹⁴⁹ See *Branch Ministries v. Rossotti*, 211 F.3d 137 (D.C. Cir. 2000) (holding that the IRS has authority to revoke exempt status under § 501(c)(3) and that the statute did not create a substantial burden on the church’s free exercise rights, without resolving the question of whether the government had a compelling interest).

¹⁵⁰ See Murphy, *supra* note 8 at 229.

jeopardizing their exempt status.¹⁵¹ In 2006, the IRS published a Fact Sheet for nonprofit organizations, which explains “what [they] can and cannot do when an election campaign is underway.”¹⁵² In the same year, they published the *Tax Guide for Churches and Religious Organizations: Benefits and Responsibilities under the Federal Tax Law* (“Guide”) “in recognition of [churches’] unique status in American society and of their rights guaranteed by the First Amendment of the Constitution of the United States.”¹⁵³ In June 2007, the IRS issued Revenue Ruling 2007-41, focusing specifically on intervention into political campaigns.¹⁵⁴ It largely replaced, without altering, much of the Fact Sheet. These documents, although not binding, “reflect the IRS interpretation of the tax laws enacted by Congress, Treasury regulations, and court decisions.” They provide detailed tests and explanations, including generic hypothetical fact patterns, for how churches can avoid jeopardizing their exempt status.¹⁵⁵ These efforts take a significant step in bridging the gap between the IRS position with regard to political activity and churches’ and nonprofits’ comprehension of and compliance with that position.

Interference in a political campaign “is considered, at least by the IRS, to be absolute, yet there is very little law and guidance as to the scope of the prohibition . . . this scope is believed to be very broad—even though there is considerable difference between political campaign activities and political activities.”¹⁵⁶ Similarly, the Fact Sheet provides that 501(c)(3) organizations are “absolutely prohibited from directly or indirectly participating in, or intervening in” political campaigns.¹⁵⁷ Former IRS Commissioner Mark W. Everson provided a somewhat softened definition, in congressional testimony, describing the limitation thus:

If political intervention is involved, the prohibition is absolute; however, some consideration may be given to whether, qualitatively or quantitatively, the organization is in the circumstance where the activity is so trivial it is without legal significance and, therefore, de minimus.¹⁵⁸

Of consternation to organizations hoping to apply a simple or straightforward rule, the IRS emphasizes that they do not apply a “bright line” for identifying violations of the Code. Rather, the IRS must interpret the law and “apply the ‘facts and circumstances’ test,” which emphasizes

¹⁵¹ See, e.g., GUIDE, *supra* note 118. In addition to these publications, the IRS has developed an online workshop for exempt organizations advising them on how they can “stay exempt” and participated in a phone forum meant to educate those organizations on the rules for involvement in elections. See Internal Revenue Service, *Election Involvement by Section 501(c)(3) Organization (including Churches)*, available at <http://www.irs.gov/charities/article/0,,id=162606,00.html>; Internal Revenue Service, *Stay Exempt: Tax Basics for 501(c)(3)s*, available at <http://www.stayexempt.org/>.

¹⁵² FACT SHEET, *supra* note 24.

¹⁵³ GUIDE, *supra* note 118.

¹⁵⁴ Rev. Rul. 2007-41, 2007-25 I.R.B. 1421.

¹⁵⁵ See Rev. Rul. 2007-41, 2007-25 I.R.B. 1421; FACT SHEET, *supra* note 24; GUIDE, *supra* note 118.

¹⁵⁶ See HOPKINS, *supra* note 16 at 505.

¹⁵⁷ FACT SHEET, *supra* note 24. See also Gregory L. Colvin, *How Well Does the Tax Code Work in Regulating Politics?*, 12 J. TAX’N EXEMPT ORGS. 66, 75 (2000) (discussing whether the complete ban on political involvement in a campaign reflects a low regard for politics).

¹⁵⁸ See HOPKINS, *supra* note 16, at 504–05.

that each investigation into the activities of nonprofits must be examined on a case-by-case basis.¹⁵⁹

Intervention in a campaign can be manifested through speech by organization leaders or representatives, through published or distributed written materials, through broadcast media including the internet, or through activities that otherwise clearly indicate partisan activity on organization property.¹⁶⁰ As discussed further in Part IV of this Note, the frequency of violations by churches and nonprofits in this area will be instructive in informing the IRS where the guidance could be clearer. The guidelines are reviewed in detail below.

1. *Voter Education, Voter Registration, and Voter Guides*

The concept of voter education is specifically addressed in the CFR. An organization may “instruct the public on matters useful to the individual and beneficial to the community.”¹⁶¹ One example is an organization “whose activities consist of presenting public discussion groups, forums, panels, lectures, or other similar programs,” where issues of social, political or international significance are discussed.¹⁶²

Section 501(c)(3) organizations are free to set up voter registration booths and to provide information about candidates; they may also assist members in getting to the polls. However, such activities must be carried out in a nonpartisan, unbiased manner. No references should be made to political parties.¹⁶³

Voter guides are extremely popular around election time, and are often used as a way of informing voters of the list of candidates who fall in line with a particularly conservative or liberal agenda. Compliance issues with voter guides arise not just around their content, but also around their distribution, as they are often sent or distributed directly to targeted religious congregations or organizations.¹⁶⁴

Published voter guides often contain voting records of incumbent candidates, positions taken or statements made by candidates on particular issues, and sometimes the positions taken on those issues by the organization. It is fairly clear that if an organization publishes information on officeholders’ or candidates’ voting records or the positions they take with regard to particular issues, it should refrain from selecting only one or a small number of issues or candidates that are of particular importance to

¹⁵⁹ See Rev. Rul. 2001-41; Rev. Rul. 2007-41; Internal Revenue Service, *supra* note 151, at 4; GUIDE, *supra* note 118, at 7–11.

¹⁶⁰ See Slevin, *supra* note 73; Rev. Rul. 2007-41, 2007-25 I.R.B. 1421 at 1–13. If an organization’s website includes links to other sites, the organization must be careful to screen the contents of those linked sites. *Id.* at 11–13.

¹⁶¹ See Slevin, *supra* note 73.

¹⁶² *Id.*; Rev. Rul. 86-95, 1986-2 C.B. 73.

¹⁶³ See GUIDE, *supra* note 118, at 7–8; FACT SHEET, *supra* note 24. See also Allison Kennedy, *When Church, State Collide: Congregations Across Columbus Handle Campaign Visits in Different Ways*, COLUMBUS LEDGER, Nov. 6, 2006 (discussing various approaches to the rules on inviting politicians to speak).

¹⁶⁴ See Rev. Rul. 2007-41; GUIDE, *supra* note 118, at 10; FACT SHEET, *supra* note 24; Simon, *supra* note 67, at A1.

the organization and which would signal voters that one candidate is favored over another.¹⁶⁵ A brochure that contains voting records or candidate responses on a broad range of issues, if published outside of an election season and distributed to the organization's normal readership, is likely permissible, even if the organization expresses its own positions on those issues.¹⁶⁶ The use of rating or ranking systems, as well as any indication of bias, in a voter guide is usually impermissible.¹⁶⁷ Finally, the timing of any publication in relation to an election is also an important consideration, because it seems to indicate whether the speaker was motivated to address the issue because of its relevance to candidate platforms in an election.¹⁶⁸

It is uncertain whether or to what extent organizations can publish their own views in a voter guide. The CFR states, "[a]n organization may be educational even though it advocates a particular position or viewpoint so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion."¹⁶⁹ However, this rule seems to conflict somewhat with the Fact Sheet, which states that "[i]f the organization's position on one or more issues is set out in the [voter] guide so that it can be compared to the candidates' positions, the guide will constitute political campaign intervention."¹⁷⁰

2. Candidate Appearances

Organizations may invite candidates to speak or to participate in a public forum so long as opposing candidates have an equal opportunity to

¹⁶⁵ See Rev. Rul. 78-248, 1978-1 C.B. 14 (providing that compiling voting records of all members of Congress on wide range of subjects, or collecting statements by candidates on wide range of topics, is permissible, but focusing on one topic of interest to organization or biased questioning by organization indicates non-partisan purpose); Situation 1 of Rev. Rul. 78-248, 1978-1 C.B. 154 (discussing, (1) how the fact that an organization published voter guides annually, regardless of whether an election was taking place, could have impact on the determination; (2) how it is permissible to publish voting records of members of Congress during a campaign if all are included and a wide range of subjects is covered; and (3) how voter guides may include candidate information as long as no approval or disapproval is voiced, but that there could be an issue of bias if it comes out right around election time).

¹⁶⁶ See Rev. Rul. 80-282, 1980-2 C.B. 178 (providing that limited distribution of an organization's newsletter containing voting records of all incumbent members of Congress as well as organization views on a wide range of topics is probably not a violation of prohibition against intervention in political campaign if not published to coincide with the timing of an election). This is especially true if the organization has a history of speaking out on a particular issue.

¹⁶⁷ See I.R.S. Tech. Adv. Mem. 9635003 (Apr. 19, 1996) (relying for definition of neutrality on Rev. Rul. 86-95, 1986-2 C.B. 73); *Association of Bar of City of New York v. Comm'r*, 858 F.2d 876 (2d Cir. 1988).

¹⁶⁸ IRS Tech. Adv. Mem. 9609007 (Dec. 6, 1995) (relying on Rev. Rul. 80-282). *But see* Wendell R. Bird, *The IRS Offers Guidance on 'Election Year Issues' for Exempt Organizations*, 15 TAX'N OF EXEMPTS 269, 273 (2004) ("In other words, a newsletter must be published only when it is not news, and crosses the line when it is news."). Whether a political statement occurs "close in time to an election" is hard to measure. The 30- and 60-day windows utilized by McCain-Feingold to identify the window of an election season could be used by 501(c)(3) organizations to define the IRS's use of that phrase (p. 11 n. 56).

¹⁶⁹ I.R.C. 1.501(c)(3)-1(d) (2007).

¹⁷⁰ See Rev. Rul. 2007-41, 2007-25 I.R.B. 1421 at 8-10 (evidence of violation of political campaign prohibition where an advertisement "is not part of an ongoing series of substantially similar advocacy communications by [the organization] on the same issue"). See also GUIDE, *supra* note 118 at 10; Rev. Rul. 80-282, 1980-2 C.B. 178. This latter ruling is frequently relied upon for evidence that wide disseminations of voter guides are appropriate. See Halloran, *supra* note 25, at 73.

participate and as long as the questions are presented in an unbiased manner. The Revenue Ruling does not provide examples of biased questioning, but suggests that if an independent, nonpartisan panel designs the questions to cover a broad range of issues (the scope of which is consistent with those the candidate would face while in office),¹⁷¹ the organization is less likely to violate the rule.¹⁷² In one example, the *Guide* emphasizes that when a church invites only one candidate to a church-sponsored event, and that candidate uses the opportunity to campaign, the church has participated in campaign intervention.¹⁷³ Candidates should not be asked if they agree or disagree with the positions of the organization, and the moderator should refrain from commenting on candidate responses. If candidates participate in separate events, the events themselves must be roughly equal in terms of attendance.¹⁷⁴ A candidate's decision not to accept an invitation to participate in such a forum should not be viewed as an indication of bias.¹⁷⁵

If a candidate is invited to speak in his or her individual capacity by virtue of that candidate's status as a public figure, expert, or holder of public office, the speaker and the organization are precluded from mentioning the speaker's candidacy or political party, from indicating any support for or opposition to that candidate, and from fundraising.¹⁷⁶ Factors that determine whether an organization has participated in campaign intervention during a candidate-guest's speech include whether the organization maintains a nonpartisan atmosphere and the reasons why the organization chose that particular speaker. A candidate's mere presence at an organization event absent an invitation to speak or participate does not by itself indicate that the organization has violated the rule.¹⁷⁷

3. *Organization Leaders*

Although organization leaders have freedom in their capacity as individuals to endorse candidates, they should attempt to clarify that their comments are personal and not intended as an expression of the views of their organization.¹⁷⁸ As individuals they may nevertheless identify themselves or be identified using the name of the organization of which they are a part, as long as the identification is not part of their organization's publication or sponsored event.¹⁷⁹ The line is drawn between official organization activities or publications and those where organization members are present or involved, but not acting in their official capacity.¹⁸⁰

¹⁷¹ GUIDE, *supra* note 118, at 8–9; FACT SHEET, *supra* note 24.

¹⁷² Rev. Rul. 2007, 2007-25 I.R.B. 1421 at 1–13. If an organization's website includes links to other sites, the organization must be careful to screen the contents of those linked sites. *Id.* at 11–13.

¹⁷³ GUIDE, *supra* note 118, at 9.

¹⁷⁴ *Id.* at 8; FACT SHEET, *supra* note 24; Revenue Ruling 2007, 2007-25 I.R.B. 1421 at 5–6.

¹⁷⁵ Rev. Rul. 2007-41, 2007-25 I.R.B. 1421 at 5–6.

¹⁷⁶ *Id.*; FACT SHEET, *supra* note 24.

¹⁷⁷ Rev. Rul. 2007-41, 2007-25 I.R.B. 1421 at 6–7; GUIDE, *supra* note 118, at 7.

¹⁷⁸ GUIDE, *supra* note 118; FACT SHEET, *supra* note 24.

¹⁷⁹ Rev. Rul. 2007-41, 2007-25 I.R.B. 1421 at 4. For example, the CEO of a 501(c)(3) hospital may endorse a candidate in a newspaper advertisement and be identified as the CEO of the hospital, particularly if the advertisement contains the language, "Titles and affiliations of each individual are provided for identification purposes only."

¹⁸⁰ *Id.*

In their official capacity, organization leaders are free to speak or publish on behalf of the organization on matters of public policy as long as they avoid campaign-like activities.¹⁸¹

4. Issue Advocacy

The CFR provides, “The fact that an organization, in carrying out its primary purpose, advocates social or civic changes or presents opinions on controversial issues with the intention of molding public opinion or creating public sentiment to an acceptance of its views does not preclude such organization from qualifying under section 501(c)(3)”¹⁸² Revenue Ruling 2007-41, as well as a series of revenue rulings published in the 1970s, helped to outline some of the contours of the political activity prohibition with regard to issue advocacy. Organizations are free to participate in the public dialogue around social and political issues. However, they must be careful not to use those issues as a way of indicating support for or opposition to candidates.¹⁸³ This is a fine line: organizations must avoid any direct or indirect references to candidates, voting, or an election while in the process of discussing issues.¹⁸⁴ Indirect references include showing pictures of candidates, referring to political parties or other distinctive features of a candidate’s campaign or platform, and expressing approval or disapproval of a candidate’s positions.¹⁸⁵ Organizations that speak out on issues only around election time are more likely to have their statements scrutinized carefully; however, even during an election season, consideration is given to those organizations that mobilize to address a particular issue being voted on by current officeholders.¹⁸⁶ Lastly, organizations must be careful not to alter their messages according to a sympathetic or unsympathetic audience, for example by reminding only certain types of audiences to vote.¹⁸⁷ A General Counsel Memo from 1971 concluded that exempt organizations are free to picket the government or other organizations so long as their activities are lawful.¹⁸⁸

Issue advocacy, and its relationship to endorsements, is perhaps the most complex rule for churches and other nonprofits because of the difficulty in distinguishing between the advocacy of an issue and the advocacy of a candidate through his or her position on an issue. The guidelines instruct that “organizations may take positions on public policy issues, including issues that divide candidates in an election for public office. However, [they] must avoid any issue advocacy that *functions as*

¹⁸¹ See GUIDE, *supra* note 118, at 7–8.

¹⁸² I.R.C. 1.501(c)(3)-1(d)(2) (2007).

¹⁸³ Rev. Rul. 2007-41, 2007-25 I.R.B. 1421 at 8–10.

¹⁸⁴ *Id.* For example, the statement, “We will need [the mayor’s] help if we want these [free city park] concerts to continue next year so please support Mayor G in November as he has supported us,” qualifies as intervention in a political campaign.

¹⁸⁵ *Id.*

¹⁸⁶ *Id.* at 8–9. For example, it is permissible for a university to publish an advertisement in a newspaper encouraging voters to contact Senator X regarding an education-related bill pending, even if Senator X is currently running for reelection. However, it may not be permissible to do so if educational issues have already been raised as a way of distinguishing Senator X from his opponent.

¹⁸⁷ *Id.* at 3–4.

¹⁸⁸ Gen. Couns. Memo. 34631 (1971).

political campaign intervention.”¹⁸⁹ This includes indirect identification of candidates, including “referring to . . . distinct features of a candidate’s platform or biography.”¹⁹⁰ The IRS must, in effect, make a determination of intent, taking into account factors such as proximity to an election or in what manner the statements take place.¹⁹¹

5. *Business Activities*

Business activities that benefit candidates can also be construed as political activity if one candidate is being favored over another candidate or over the general public.¹⁹² This includes selling or renting the organization’s mailing lists to candidates, leasing office space to or from candidates, or accepting paid political advertising.¹⁹³

C. SANCTIONS

The *Guide* lists revocation of exempt status and/or the imposition of excise taxes as consequences that “may be imposed” as a result of improper involvement in political activity.¹⁹⁴ The excise tax is imposed at a rate of ten percent of the organization’s political expenditures and five percent of its lobbying expenditures.¹⁹⁵ Organization managers who agreed to the expenditures with knowledge that the expenditure was for a political purpose are subject to a similar tax as individuals.¹⁹⁶ If the expenditures are not corrected within a set time period, an additional tax of 100% of the organization’s expenditures is imposed on the organization and a tax of 50% of its expenditures is imposed for managers, up to a maximum of \$10,000. To correct the expenditure, organizations must recover the expenditure, to the extent possible, and establish safeguards to prevent future violations.¹⁹⁷

Consequences under the Code often sound more serious than they are in reality. For example, excise taxes only apply where an organization has spent money to engage in the speech act in question. Additionally, revocation of an organization’s exempt status does not bar it from operating under the exemption in the future.¹⁹⁸ The Court in *Branch Ministries II* described the sanction as “more symbolic than substantial.” A church or

¹⁸⁹ FACT SHEET, *supra* note 24 (emphasis added). See also Stephen H. King, ‘Political Correctness’ for Section 501(c)(3) Organizations, 18 TAX’N OF EXEMPTS 75 (distinguishing the Fact Sheet’s “fairly bright lines” for voter mobilization and individual activity compared to “the more troublesome question of when voter education and issue advocacy can cross the line . . .” and advocating a system that allows organizations to “connect the dots between candidate positions and a church’s theological beliefs”).

¹⁹⁰ FACT SHEET, *supra* note 24.

¹⁹¹ GUIDE, *supra* note 118, at 7. See also Halloran, *supra* note 25 (discussing indirect statements of support for or opposition to candidates).

¹⁹² See Rev. Rul. 2007-41, 2007-25 I.R.B. 1421; GUIDE, *supra* note 118, at 10.

¹⁹³ Rev. Rul. 2007-41.

¹⁹⁴ GUIDE, *supra* note 118, at 11; accord. I.R.C. § 4958 (2000).

¹⁹⁵ GUIDE, *supra* note 118, at 11. In the NAACP case, the NAACP was required to estimate the cost of Bond’s speech. They estimated that they spent \$176.48, including the costs for photocopying and posting the speech on their website. Accordingly, they paid \$17.65 in tax. Jones, *supra* note 8.

¹⁹⁶ GUIDE, *supra* note 118, at 11; I.R.C. § 4958.

¹⁹⁷ *Id.*

¹⁹⁸ See *Branch Ministries v. Comm’r*, 211 F.3d at 142–43.

other nonprofit can once again declare itself to be a 501(c)(3) organization as soon as it refrains from the prohibited political activity.¹⁹⁹ Further, even if the organization's exempt status has been revoked, donations are likely to be considered gifts and therefore not includable as income under the Code.²⁰⁰ Finally, donors are often protected by being allowed to take a deduction in instances where they made contributions to an exempt organization before they knew that the church or other nonprofit had lost its exemption.²⁰¹

IV. ENFORCEMENT

It is not only the letter of the law that tells the story of whether the IRS and tax exempt organizations are successful in achieving the policy goals. The true test lies in the enforcement of the Code by the IRS.²⁰² The historical patterns of IRS enforcement actions as well as its most recent summary reports are useful to a discussion of whether IRS communication and execution systems are effective. The most important questions are, do they allow exempt organizations to productively engage in a debate over the substance of the rules, and can the goals of the tax exempt status help us to shape that debate?

A. PUBLIC REFERRALS AND THE POLITICAL ACTIVITIES COMPLIANCE INITIATIVE ("PACI")

The IRS relies mostly on reports by third parties to police unlawful activity among exempt entities, a policy which is understandably vulnerable to criticism that it can produce uneven results or make exempt organizations susceptible to politically-motivated harassment.²⁰³ The IRS is sometimes also spurred to investigate a church or other organization by media reports. This was the case for All Saints' Rector Regas, whose sermon was described by the Los Angeles Times as "a searing indictment of the Bush administration's policies in Iraq."²⁰⁴ According to the article, the sermon denounced those policies as "inimical to the values of Jesus."²⁰⁵ The IRS is often criticized for what some consider uneven responses to reports or allegations of inappropriate behavior by organizations. One journal offered a baseball analogy, wherein IRS officials are "stretched thin across the vast expanse of green . . . catch[ing] pop flies hit by Jimmy Swaggart, Jerry Falwell, and Pat Robertson." It presents the IRS "shading its fielders to the right" and "sometimes . . . the IRS 'reluctantly' reports,

¹⁹⁹ *Id.*

²⁰⁰ *Id.* at 143; I.R.C. § 102 (2000).

²⁰¹ I.R.C. § 102.

²⁰² See James, *supra* note 67, at 69–74.

²⁰³ IRS U.S., DEP'T OF TREAS., FINAL REPORT: PROJECT 302, POLITICAL ACTIVITIES COMPLIANCE INITIATIVE (2006), http://www.irs.gov/pub/irs-tege/final_paci_report.pdf [hereinafter FINAL REPORT]. See OMB WATCH, REPORT, THE IRS POLITICAL ACTIVITIES ENFORCEMENT PROGRAM FOR CHARITIES AND RELIGIOUS ORGANIZATIONS: QUESTIONS AND CONCERNS (2006), available at <http://www.ombwatch.org/pdfs/paci.pdf> [hereinafter OMB WATCH].

²⁰⁴ Getlin, *supra* note 72, at A1.

²⁰⁵ See *id.*

the ball goes over the fence.”²⁰⁶ Possibly in response to this sentiment, the website RatOutAChurch.org offers people an opportunity to “fight back against vicious left-wing attempts to silence conservative, Bible believing pastors.”²⁰⁷ Visitors to the site are encouraged to attend services at liberal churches and report back on any comments that could be construed as political endorsements.²⁰⁸

Three recent IRS referrals demonstrate that the process is as active as ever. In the first, the group Americans United for Separation of Church and State (“Americans United”) asked the IRS to investigate whether Southern California Pastor Wiley Drake violated the Code when he used his church’s letterhead and a church-supported radio program to endorse a candidate for the 2008 Republican primary.²⁰⁹ In the second referral, Americans United reported televangelist Bill Keller to the IRS after he wrote a message on his website expressing the view that a vote for presidential candidate Mitt Romney was a vote for Satan.²¹⁰ In the third, the IRS has been asked to investigate whether the Wichita, Kansas-based church, Spirit One, violated the rules banning involvement in a campaign when it distributed voter guides and posted messages on its marquee critical of pro-choice candidates.²¹¹

Although the temptation to “rat out” an organization with the opposite ideological or political view will never disappear, the IRS could take steps to alleviate the problem. First, although the IRS is precluded from investigating churches without a report from the public that leads them to believe there is a violation, it could balance the non-church referrals with IRS-initiated investigations, to the extent it is feasible. The IRS could also develop and publish a system for deterring and screening referrals that are solely meant to harass.²¹² Similarly, they could develop a system for monitoring the inevitable biases of investigators, and for balancing inquiries between churches and non-churches and conservative and liberal organizations.

As referrals have increased, so too have IRS investigations. The IRS traces the increase to the dramatic rise in funding for political campaigns.²¹³ For the 2004 election cycle, the Federal Election Commission reported that \$10 billion was spent on campaign funding, more than twice what was spent during the 2000 election cycle. This, the IRS says, is naturally tied to the rise in the number of allegations that

²⁰⁶ See Colvin, *supra* note 157, at 75. But see Slevin, *supra* note 73 (discussing whether the IRS is acting as aggressively in the Ohio case as in the NAACP and All Saints cases).

²⁰⁷ RATOUTACHURCH.ORG, *Why We Are Doing This*, available at <http://www.ratoutachurch.org/why.aspx> (last visited Dec. 20, 2007).

²⁰⁸ *Id.*

²⁰⁹ See Dave McKibben, *Pastor Asks Followers to Pray for the Death of His Critics*, L.A. TIMES, Aug. 16, 2007, at B1.

²¹⁰ See Sherri Day, *TV Station Pulls Plug on Keller*, ST. PETERSBURG TIMES, Aug. 24, 2007 at 1B.

²¹¹ See Joe Rodríguez, *Audit May be Part of IRS’ Investigation of Church*, WICHITA EAGLE, Aug. 17, 2007 at 4B.

²¹² See OMB WATCH, *supra* note 203, at 2.

²¹³ I.R.S. U.S. DEP’T OF TREAS., POLITICAL ACTIVITIES COMPLIANCE INITIATIVE EXECUTIVE SUMMARY (2006), available at http://www.irs.gov/pub/irs-tege/exec_summary_paci_final_report.pdf [hereinafter PACI EXECUTIVE SUMMARY].

501(c)(3) organizations are breaking the law.²¹⁴ The IRS's introduction of its new Political Activities Compliance Initiative ("PACI") during the 2004 election cycle was one response to the increased activity. In addition to initiatives discussed in Part III aimed at educating the nonprofit sector as to its rights and limitations, the IRS created, through PACI, some set procedures for identifying and investigating potential violations of the Code.²¹⁵

The results of the PACI system help to provide a big-picture overview of IRS investigation patterns during the election cycles of 2004 and 2006. According to the 2004 report, the IRS received 166 referrals regarding 127 organizations.²¹⁶ A total of 132 cases were "forwarded to the field," including some cases that were identified by the IRS without a referral. Twenty-two were closed immediately, leaving forty-seven church cases and sixty-three non-church cases.²¹⁷ Cases were then organized into Type A and Type B, the latter being reserved for complex, multi-issue cases; the vast majority of these did not involve churches.²¹⁸ For the 2006 cycle, the IRS received 237 referrals (albeit over a longer time period) but selected only 100 of those to be "forwarded to the field."²¹⁹ In 2006, the IRS placed four organizations into a third category, Type C, which is reserved for particularly egregious or repetitive alleged violations. None of the Type C cases involved churches.²²⁰

Of the eighty-two cases from the 2004 election cycle that had been concluded or were in appeals at the time of the 2006 PACI report, the IRS took steps to revoke the exempt status of only four organizations, with an additional two revocations proposed. None of those six were churches.²²¹ At the time of the 2006 report, only forty of the 100 cases for the 2006 election cycle had been closed, and none of those forty had resulted in a revocation of exempt status.²²² IRS Commissioner Everson reported in February 2006 that "nearly three quarters" of the remaining eighty-two investigations resulted in a finding of prohibited behavior.²²³ The actual number is lower, however, if you count those referrals that were immediately dismissed, raising the question of whether such inflated summaries of violations give nonprofits the impression that the problem is more widespread than it actually is.²²⁴

²¹⁴ *Id.*

²¹⁵ See FINAL REPORT, *supra* note 203, at 2–5.

²¹⁶ *Id.* at 4.

²¹⁷ See *id.* at 7, 9.

²¹⁸ See *id.* at 6.

²¹⁹ I.R.S. U.S. DEP'T OF TREAS., 2006 POLITICAL ACTIVITIES COMPLIANCE INITIATIVE I (2007), available at http://www.irs.gov/pub/irs-tege/2006paci_report_5-30-07.pdf [hereinafter PACI 2006].

²²⁰ *Id.* at 2. Type C requires immediate action by the IRS. Examples include widespread advertising supporting a candidate, political contributions that could drain a group's treasury, or clear and continued support of or opposition to a candidate. See OMB WATCH, *supra* note 203, at 4.

²²¹ Five organizations had their exempt status revoked, but one was for "other operational issues." *Id.* at 5.

²²² *Id.*

²²³ Remarks of IRS Comm'r Mark W. Everson at the City Club of Cleveland, Ohio, Feb. 24, 2006, available at <http://www.irs.gov/irs/article/0,,id=154788,00.html>.

²²⁴ According to OMB, only 30.3% of all referred cases and 35.5% of completed investigations resulted in conclusions of violations if dismissed cases were included, compared to the IRS Commissioner's

In 2006 the IRS also instituted the Political Contribution Sub-Project, which uses the internet to research illegal campaign contributions by 501(c)(3) organizations. It identified 269 possible cases, with contributions totaling \$343,963.²²⁵

Sanctions for nonprofit organizations found to have engaged in prohibited behavior varied, depending largely on whether the behavior was “one-time” in nature or reflected a pattern of prohibited activity.²²⁶ In 2004, sixty-nine organizations received written advisories and twenty-three were found not to have engaged in any prohibited activity. Churches received written advisories for minor violations 84% of the time, much more often than non-church organizations, which received written advisories only 45% of the time.²²⁷ Of the forty closed cases from the 2006 election cycle, written advisories were issued in twenty-six cases and fourteen organizations were cleared of the allegations of prohibited activity.²²⁸ The written advisories are a construction of the PACI program and not explicitly authorized by the Code. They have been widely utilized, however, as an alternative to revocation of exempt status or imposition of the excise tax, and, according to a review of advisories issued in 2004, no organizations that received written advisories intervened in a political campaign in 2006, suggesting that they have a deterrent effect.²²⁹ In 2004, the largest category of violations were endorsements made by officials of nonprofit organizations, with eighteen occurrences, followed by improper distribution of materials and displaying of signs, with nine occurrences each.²³⁰ These results may suggest that the guidelines should be revisited to address the rules related to the most common infractions.²³¹ At the time of publication, violations by type were not yet available for the 2006 election cycle.

The PACI results accomplish a few significant things. First, they give exempt organizations a good sense of the scope of this issue and serve as a reminder that, despite the large amount of media attention, these cases represent but a small fraction of churches and other nonprofits operating in America.²³² Second, the report allows us a glimpse into the procedures used by the IRS to respond to referrals and to process cases, which will help exempt organizations to know what to expect in the event they are ever reported to the IRS or otherwise become the subject of an IRS

statement suggesting that 74% of investigations resulted in violations. *See id.*; OMB WATCH, *supra* note 203 at 9; FINAL REPORT, *supra* note 203 at 13.

²²⁵ See PACI 2006 *supra* note 219, at 6.

²²⁶ PACI EXECUTIVE SUMMARY, *supra* note 213 at 3.

²²⁷ See FINAL REPORT, *supra* note 203, at 9, 20–21; OMB Watch, *IRS Investigations of Political Activity Heat Up*, available at <http://www.ombwatch.org/article/artircleprint/3606>; Pamela J. Gardiner, Deputy Inspector General for Tax Administration, *Review of Exempt Organizations Function Process for Reviewing Alleged Political Campaign Intervention by Tax Exempt Organizations* 15 (2005), available at <https://www.ustreas.gov/tigta/auditreports/2005reports/200510035fr.pdf>.

²²⁸ PACI 2006 *supra* note 219, at 5.

²²⁹ See OMB WATCH, *supra* note 203, at 15; PACI 2006 at 5.

²³⁰ See FINAL REPORT, *supra* note 203, at 16–17.

²³¹ See OMB WATCH, *supra* note 203, at 21.

²³² See FINAL REPORT, *supra* note 203.

investigation. Third, the results reveal some trends,²³³ allowing both the IRS and the public to examine those trends for any imbalance or bias.

B. THE NEED FOR TRANSPARENT PROCESSES AND TRANSPARENT LEGAL REASONING

The PACI results alone are not a sufficient means of informing exempt entities as to how their actions will be evaluated. The IRS could take a number of steps to improve the transparency of the systems they use to carry out investigations.

First, there are no official deadlines for concluding an investigation.²³⁴ Many groups, in large part as a response to the years-long investigations in the NAACP and All Saints cases, point to the lack of deadlines to support the argument that PACI improperly restricts the free speech of nonprofits.²³⁵ A recent report by the Treasury Department's Inspector General agreed, reporting that enforcement of IRS regulations in this area is "marred by tardiness and lack of clear guidelines."²³⁶ In January 2006, thirty-one clergy members of Christian and Jewish faiths submitted a joint complaint to the IRS, alleging that two churches engaged in prohibited political activity related to a Republican gubernatorial candidate's campaign, including an allegation that one church improperly held political activities and allowed Republican organizations to use their facilities.²³⁷ After three months, there was no indication from the IRS that any action was being taken to investigate the allegation, so the group filed a second document. As of January 2007, this issue was yet to be resolved by the IRS.²³⁸ Perhaps in response to this issue, the PACI 2006 report emphasized that it "included expedited timeframes for classification and case assignment . . . directed at providing swift notice to organizations with the hope of stopping political intervention as quickly as possible."²³⁹ PACI now includes a goal that organizations are to be contacted within sixty-five days of the IRS's receipt of the referral, but there is no stated goal regarding response time to organization queries or a timeframe for resolution of the entire matter.²⁴⁰

A significant change included in PACI is that the IRS no longer waits until the end of the tax year to launch an investigation, but may do so at any

²³³ *Id.* For example, although churches cases are typically graded Type B simple cases, they are much more likely to result in a finding of a violation.

²³⁴ See OMB WATCH, *supra* note 203, at 4.

²³⁵ See OMB WATCH, *IRS Investigations of Political Activity Heat Up*, available at <http://www.ombwatch.org/article/artircleprint/3606>; Stephen Clark, *IRS Warns Churches to Stay Neutral on Politics*, L.A. TIMES, July 18, 2006, at B3.

²³⁶ See David C. Kohler, *Free Speech Put to the Test in Pulpit*, FULTON COUNTY DAILY REPORT, VOL. 117, NO. 187, Sept. 28, 2006.

²³⁷ See Slevin, *supra* note 73. The complaint asks how one nonprofit obtained its nonprofit status considering one of its stated goals is "to create an army of 'Patriot Pastors'" to increase voting among church members. See Stephanie Strom, *Group Seeks I.R.S. Inquiry Into 2 Ohio Churches Accused of Improper Campaigning*, N.Y. TIMES, Jan. 16, 2006, at A9.

²³⁸ Dan Gilgoff, Editorial, *Turning a Blind Eye, IRS Enables Church Politicking*, USA TODAY, Jan. 29, 2007, at 13A, available at http://blogs.usatoday.com/oped/2007/01/turning_a_blind.html.

²³⁹ See PACI 2006, *supra* note 219, at 1.

²⁴⁰ *Id.* at 2.

time throughout the cycle, even close to election time.²⁴¹ This comes as a mixed blessing to the nonprofit organizations. On the one hand, election time is the most active time for political activity and referrals, and many groups feel that the IRS has a responsibility to get involved before the election has passed and the damage has been done.²⁴² But many are concerned that delayed investigations, especially during the election cycle, reveal an improper purpose on the part of the IRS and result in a dilution of advocacy, voter education, and voter mobilization for organizations that have been alerted by the IRS that their actions may violate the law.²⁴³ Similarly, some argue that it is unfortunate enough that the IRS has not made it clear to exempt organizations whether and how an organization can get into trouble for criticizing a current politician's policies during an election cycle, and for the IRS to initiate investigations during the election cycle would further muddy the waters.²⁴⁴

In addition to a lack of transparency concerning IRS procedures and timelines, there is little information available on what contributes to the substance of investigative determinations.²⁴⁵ Organizations and onlookers are often forced to rely upon media reports, or upon information volunteered by those filing complaints or being targeted by them.²⁴⁶ For example, in the Operation Rescue West investigation, although the IRS did not provide grounds for the decision, the group Catholics for Free Choice issued a statement indicating that they filed the complaint after Operation Rescue West purchased its advertisement.²⁴⁷ The IRS relies on § 6103 of the Code to justify its refusal to make public its standards, the facts of individual cases, and the reasoning underlying investigation results.²⁴⁸ Section 6103 requires that "return information" be kept confidential, which includes information and data related to exemptions or investigations.²⁴⁹ This privacy rule creates a barrier for nonprofits to understanding how the IRS applies the law and its own rules. Because the results of investigations are not made public, and the "facts and circumstances" test allows the IRS broad latitude in distinguishing one case from another, there is no developing consensus on what the law is.²⁵⁰ All of these issues "[have] a chilling effect on charities and religious organizations that want to express a point of view on current issues of interest to their constituencies."²⁵¹ The lack of information "raise[s] serious questions about the agency's interpretation of the law, about evenhanded enforcement, and about the

²⁴¹ See Slevin, *supra* note 73.

²⁴² See Release, Americans United, Americans United Announces National Campaign to Alert Churches to the Dangers of Partisan Politicking (Sept. 18, 2006), available at <http://www.au.org/sit/News2?abbr=pr&page=NewsArticle&id=8537>.

²⁴³ See Gardiner, *supra* note 227, at 15; OMB WATCH, *supra* note 203, at 10.

²⁴⁴ OMB WATCH, *supra* note 203, at 6; IRS Tech. Adv. Mem. 96-09-007 (Dec. 6, 1995) (relying on Rev. Rul. 80-282, *supra* note 184). The Fact Sheet indicates, with regard to issue advocacy, that "[k]ey factors in determining whether a communication results in political campaign intervention include . . . whether the statement is delivered close in time to the election." FACT SHEET, *supra* note 24.

²⁴⁵ OMB WATCH, *supra* note 203, at 13.

²⁴⁶ *Id.*

²⁴⁷ See Strom, *supra* note 12.

²⁴⁸ OMB WATCH, *supra* note 203, at 10.

²⁴⁹ I.R.C. § 6103 (2007).

²⁵⁰ OMB WATCH, *supra* note 203, at 3.

²⁵¹ *Id.*

appropriateness of an approach aimed at deterring speech.”²⁵² Despite these concerns, however, a recent audit by the Treasury Department’s Inspector General for Tax Administration found that the IRS behaves impartially in its investigation of prohibited political activity.²⁵³

Finally, the question of the substance of the IRS’s reasoning raises the issue of scope; without knowing whether investigations tend to reveal egregious behavior or “close cases,” an aggressive IRS stance or a lenient one, it is impossible to assess the true size of the problem. With such limited information the argument cuts both ways. On the one hand, critics argue that, contrary to IRS statements on the matter, charities and religious organizations are well aware of the law and its limits when it comes to political activity and tend to be overly cautious.²⁵⁴ On the other hand, many believe not only that the IRS is reluctant to enforce its own rules, but that hundreds or possibly even thousands of organizations have made the conscious decision to “walk on the razor’s edge of the law.”²⁵⁵ Many reports of unaddressed violations confirm this. For its part, the IRS has admitted that it can be lenient, contending that it prefers to bring organizations into compliance rather than punishing them.²⁵⁶

C. A BRIGHT LINE RULE?

In response to this general lack of transparency, the push for a bright line rule defining political activity is widespread.²⁵⁷ One popular approach to developing a bright line is to focus on eliminating the exemption entirely, and with it the potential problem of government subsidization of a campaign. For example, the IRS could delineate an organization’s funds between those that are used for political purposes and those that are not, and tax the former.²⁵⁸ It could also institute a wholesale taxation of nonprofit entities and churches, or grant exempt status only to those organizations offering substantial services to the community, to whom the government would typically provide grants.²⁵⁹ House Resolution 235, which circulated through Congress in late 2006, would have created half of

²⁵² *Id.*

²⁵³ See FINAL REPORT, *supra* note 203, at 22; Gardiner, *supra* note 227.

²⁵⁴ See FINAL REPORT, *supra* note 203, at 9. One report found that 87% of exempt organizations were aware they could not endorse political candidates, and 43% believed they could not sponsor a candidate debate or forum. *Id.*

²⁵⁵ See Simon, *supra* note 67. Americans United for the Separation of Church and State is a group actively engaged in the task of informing churches of the restrictions on their speech rights. In September of 2006, they sent over 100,000 letters to churches in eleven targeted states. See Americans United, *supra* note 242.

²⁵⁶ See Gilgoff, *supra* note 5.

²⁵⁷ See, e.g. Kemmitt, *supra* note 33, at 179 (“Simply allowing churches to engage in political activity so long as they avoid spending tax-exempt money on those activities solves all of these problems. It ensures ministers and worshipers the free exercise rights guaranteed them . . . , provides a bright-line test that allows churches to adhere to IRS guidelines and for the IRS to enforce those guidelines, and avoids Establishment Clause concerns by prohibiting the use of tax-exempt dollars.”).

²⁵⁸ *See id.*

²⁵⁹ See Adler, *supra* note 86, at 916–17 (“The system Congress has enacted provides this kind of subsidy to nonprofit civic welfare organizations generally, and an additional subsidy to those charitable organizations that do not engage in substantial lobbying. In short, Congress chose not to subsidize lobbying as extensively as it chose to subsidize other activities that nonprofit organization undertake to promote the public welfare.”).

a bright line, allowing the tax exemption for religious institutions, but not for secular nonprofits.²⁶⁰ These suggestions create administrative problems and fail to accommodate the policy goals set in place for religious and nonprofit institutions. The current system of taxation supports the fundamental relationship between donors, exempt organizations, and their beneficiaries, and gives those players freedom to make decisions and to spend money on an overwhelming number of charitable services. They are able to provide these benefits because of the funding stream created by exemption and because they are not overly burdened by accounting mechanisms or oversight. Additionally, a revocation of tax exempt status for churches, or for churches or organizations that do not provide substantial services to the community, impinges on the goal of freedom of religious and social purpose. Government interference with this goal is both improper and harmful.

The other approach offered in support of the bright line rule is to amend the prohibition itself, creating a single, objective standard that designates in detail the activities that do and do not constitute prohibited political activity, so that religious and other nonprofit organizations are no longer walking that razor's edge.²⁶¹ But these ideas betray the policy priorities, too. First, the assumption inherent in the approach is that exempt entities are simple or similar. They are not, and certainly their political speech cannot be quickly placed on one side or another. It is only through a careful analysis of the facts of a particular case that is it possible to properly protect that speech. In the case of All Saints, for example, the church's speech may have been viewed differently after uncovering the church's vibrant history as an active promoter of peace.²⁶² For this reason it is necessary to maintain the case by case analysis, carefully keeping sight of the balancing required by the policy goals.

Even if one accepts that the IRS can be an evaluator of political speech, however, that does not mean the result will always come out correctly. The question then becomes, how do the policy goals help the IRS to resolve a "close case," and how do they encourage the public to accept it? Do the policy goals instruct that we err on the side of preventing some political speech by exempt organizations that comes too close to an endorsement or lobbying, or do we allow some of that speech in order to protect our interest in the involvement of exempt organizations in the civic dialogue? Each has its consequences. The latter seems to acknowledge the goal that churches and other nonprofits are in touch with the public, and have created a mechanism for speaking for them.²⁶³ Especially because so many recipients of services no longer receive them directly from government, but instead from charitable organizations, political speech by those organizations may act as an additional benefit to recipients—even

²⁶⁰ See Henriques, *supra* note 79, at A20.

²⁶¹ See, e.g., Colvin, *supra* note 157; James, *supra* note 67, at 74; Simon, *supra* note 67, at A1 (quoting Matthew Staver, founder of non-profit law firm Liberty Counsel) (discussing the view that "Preachers ought to put their toe right on the line").

²⁶² All Saints Church, Ed Bacon's First Announcement to the Congregation on Nov. 6, 2005, available at http://www.allsaints-pas.org/site/PageServer?pagename=IRS_Exam_splash.

²⁶³ See BERRY & ARONS, *supra* note 37, at 60.

if that speech sometimes crosses the line. The former aims to resist the wave of increasing political speech and activity by churches and other nonprofits, and is willing to sacrifice some legitimate speech on political issues in favor of keeping endorsements and lobbying in the private, individual realm along with private dollars.²⁶⁴ In the end though, a careful review of the policy goals must bring both the IRS and the public to the conclusion that we should err on the side of allowing some prohibited political speech by exempt entities. This is because, on balance, the goals protect the freedom of religious and other nonprofit institutions to perform their work more than they protect the private political contribution or the sanctity of a political process free of government subsidization. In a close case, the freedom to speak out, to worship, and to serve society trumps the mandate to refrain from unfair and inefficient politicking.

Similarly, when close cases are contested and ultimately make their way into the courtroom, these policies instruct that the legal analyses of judges must also err on the side of the exempt entity. When scrutinizing the application of § 501(c)(3) by the IRS or determining the reasonableness of the rule itself, courts must take into account the policy priorities articulated above. This is not to say that the policy priorities should prevent the government from trying to define its relationship with nonprofits and the limits on political activity, however. In light of this, the application of a strict scrutiny analysis in *Branch Ministries* is unusual for two reasons. First, strict scrutiny was used in *Branch Ministries* to uphold restrictions on political activity by those receiving a subsidy, when the result of strict scrutiny is almost always to strike down the law in question.²⁶⁵ Second, the Supreme Court has held that where a legislature, through a statute, elects not to subsidize a fundamental right, that right is not infringed upon and so does not require a strict scrutiny analysis.²⁶⁶ Accordingly, the argument presented in this Note is not that the attempt by Congress to find the right balance between government interests and the religious and social interests of exempt organizations is suspect, but rather that judges should be careful to review whether those attempts reasonably take into account the priorities articulated herein.

D. THE ALL SAINTS CASE AND THE UNIQUE TREATMENT OF CHURCHES

Within the framework of PACI is the Church Audit Procedures Act (“CAPA”), which mandates special guidelines for the investigation of a church. CAPA instructs that a church tax inquiry may be initiated only upon the “reasonable belief” by a high-level Treasury official that the church may not be exempt from taxation under § 501(c)(3).²⁶⁷ Such inquiry

²⁶⁴ See Gilgoff, *supra* note 5.

²⁶⁵ KATHLEEN M. SULLIVAN & GERALD GUNTHER, *FIRST AMENDMENT LAW*, 8–13 (Foundation Press 2nd Ed. 2003).

²⁶⁶ *Regan*, 461 U.S. at 549.

²⁶⁷ I.R.C. § 7611 (2007). The public law doesn’t include any reasoning for the inclusion of the restrictions into the code. Pub. L. 98-369, 1984 H.R. 4170, Section 1033. According to a letter from the IRS to All Saints, “In passing [CAPA], Congress intended to ensure that the [IRS] carry out its obligation to resolve questions concerning the tax liability, if any, and the tax-exempt status of churches and organizations claiming to be churches, with due regard for both the rights of church organizations

typically requires a church to respond to IRS questions and serves as the basis for determining whether a church is (1) exempt from tax under § 501(a) by reason of its status as a church, or (2) is engaged in activities which may be subject to taxation.²⁶⁸ Inquiries are initiated by written notice to the church from the IRS.²⁶⁹

For All Saints, the inquiry by the IRS came in the form of a June 2005 letter, which stated that a “reasonable belief” existed that All Saints had engaged in political campaign intervention. The letter included a list of eleven questions regarding the nature of the relationship between Regas and All Saints, including whether All Saints’ governing body approved or had knowledge of the sermon, whether materials were distributed, and whether any other All Saints sermons or activities constituted political intervention in a campaign.²⁷⁰ The letter went on to state, “If your response resolves our questions concerning activities which may constitute intervention in a political campaign, it will not be necessary to pursue this matter further.”²⁷¹ This type of language prompts critics to suggest that the IRS infringes on due process by encouraging organizations to admit to wrongdoing in exchange for an expedited investigation.²⁷² The IRS, the argument goes, has made it clear that refusing to admit wrongdoing and continuing the activity that sparked the investigation makes it more likely that the investigation will result in revocation of exempt status.²⁷³

All Saints responded to the inquiry through an attorney, but did not actually answer the questions.²⁷⁴ In an announcement to the congregation in November 2005, Bacon said,

It is important for everyone to understand that the IRS’s concerns are not supported by the facts. George Regas’s sermon upheld the core values of this church as a Peace Church. We have been a self-identified Peace Church since a resolution was adopted by the Vestry in 1987. The sermon in question explicitly stated, ‘I don’t intend to tell you how to vote.’ We at All Saints, of course, will continue from a nonpartisan perspective to teach and proclaim with vigor the core values of Christianity as we stand in the prophetic tradition of Jesus the peacemaker. This is our responsibility as followers of Christ and as Americans who claim our freedom of speech and freedom of religion.²⁷⁵

If an inquiry into church activities does not yield the desired resolution of the issue, or if the church does not respond, the IRS may launch a church tax examination, whereby the IRS is authorized to obtain and review

and the responsibility of the Service to enforce the Internal Revenue laws.” Letter from R.C. Johnson, Director, Exempt Organizations Examinations, Internal Revenue Service, to All Saints Church (2005), available at <http://aschu.convio.net/pdf/IRS%20Letter%20to%20All%20Saints.pdf>.

²⁶⁸ I.R.C. § 7611 (2007).

²⁶⁹ See GUIDE, *supra* note 118, at 22.

²⁷⁰ See R.C. Johnson, *supra* note 267.

²⁷¹ *Id.*

²⁷² OMB WATCH, *supra* note 203, at 10–11.

²⁷³ *Id.*

²⁷⁴ See Letter from Marcus S. Owens, Attorney, Caplin & Drysdale, to Pat Schneiders, Exempt Organizations Specialist, IRS (Oct. 11, 2005), available at http://aschu.convio.net/pdf/DOCS-IRS_letter%20FINAL.pdf.

²⁷⁵ Ed Bacon, *supra* note 262.

church records or examine its activities in order to determine “whether the church is a church.”²⁷⁶ The IRS made a request of All Saints for such detailed records in July 2006.²⁷⁷ In response to a request by All Saints regarding the feasibility of fulfilling the request, the IRS then reformulated the request in the form of an administrative summons.²⁷⁸ In September 2006, the All Saints Vestry voted unanimously to contest the summons,²⁷⁹ forcing the IRS to either drop the case or request that the Justice Department take All Saints to court.²⁸⁰ The examination of a church’s books and records must be completed within two years of the notice of examination, and if at any time the IRS’s concerns are alleviated by new information, the matter will be closed without examination.²⁸¹ Unless the examination results in a revocation or notice of deficiency, or the church has undergone a significant change in operations, the IRS may not conduct another examination of the church for at least five years.²⁸²

The September 2007 letter from the IRS to All Saints was cursory at best, noting that the intervention appeared to be one-time in nature and that the IRS believed the necessary policies were in place at All Saints to prevent further noncompliance in the future. The IRS told All Saints that it must inform future guest speakers of its policies, and to be mindful of the contents of their website.²⁸³ In a responsive press release, All Saints accused the IRS of closing the examination “without the audit ever actually taking place,” and expressed frustration over the IRS’s utter lack of reasoning for its conclusion. “Synagogues, mosques, and churches across America have no more guidance about the IRS rules now than when we started this process over two long years ago.”²⁸⁴

In the end, exempt organizations waited in vain for an explanation from the IRS on how Regas’s statement, ‘I’m not advising you how to vote,’ could or could not be reconciled with the *Guide*’s warning that the IRS scrutinizes election-time statements more critically, as it does statements that seem to ask listeners to interpret loosely veiled intent.²⁸⁵ Some waited to see whether the IRS might review its policy with regard to organizations who refuse to comply and decide, in light of its statements that it intends to step up enforcement, to take a firmer stance. Alas, no help came to clear “the murky waters of the IRS rules distinguishing between issue advocacy and partisan intervention.”²⁸⁶

²⁷⁶ See GUIDE, *supra* note 118, at 22.

²⁷⁷ See R.C. Johnson, *supra* note 267.

²⁷⁸ See OMB WATCH, *supra* note 203.

²⁷⁹ All Saints Church, The IRS Returns (2007), available at <http://www.allsaints-pas.org/site/PageServer?pagename=IRSExamplash>.

²⁸⁰ See Greg Mathis, *Is IRS Being Used Politically?*, CHI. DEFENDER, Oct. 13, 2006.

²⁸¹ See GUIDE, *supra* note 118, at 22.

²⁸² *Id.*

²⁸³ See Ramirez, *supra* note 4.

²⁸⁴ See Press Release, All Saints Church, All Saints Church, Pasadena Demands Correction and Apology From the IRS (Sept. 23, 2007), available at <http://www.allsaints-pas.org/site/DocServer/IRSPressReleaseSept232007.pdf?docID=2521>. See also Gilgoff, *supra* note 5.

²⁸⁵ See Bird, *supra* note 168, at 278.

²⁸⁶ See Press Release, *supra* note 284, at 2.

V. CONCLUSION

From any perspective, it will be difficult to view the story of All Saints Church as a success. If nothing else, it stands for today's unresolved debate over whether the drafting and enforcement of tax rules can better enable us to fulfill our social, religious, and legal objectives. The growing media attention around IRS investigations of political activity, coupled with the rise in stature of the nonprofit sector and its tendency to apply its money and power to the social and political dialogue, are clear signposts that the IRS must adapt its current systems in ways that better serve the public.²⁸⁷ In order to do that well, the IRS will have to review the six policy goals that convey our interest in churches and other nonprofits and our contention that they add value to society.

The policy goals do not require that Congress amend the Code language for § 501(c)(3) organizations, or put into place a bright line rule. Rather, the IRS must hone its processes and its communication. First, the IRS should evaluate its referral system and attempt to balance church and non-church investigations. It must better police both politically-motivated harassment of exempt organizations and the tendency of organizations to assume that the rules will never catch up with them. Second, the IRS should build on recent successes in the area of educating exempt organizations as to their rights and responsibilities by creating and sharing internal timelines and better articulating them during election cycles. Third and finally, the IRS must take steps to consider how to create a public record of investigative results and investigative reasoning while maintaining the integrity of the privacy statute. This will allow organizations to better understand their limits, and will make the IRS accountable for creating clear and consistent standards and enforcing those standards when necessary.

²⁸⁷ See BERRY & ARONS, *supra* note 37, at 11.

