April 2017

Legislative Activities of 501(c)(3) Organizations

Lawrence N. Woodworth

Follow this and additional works at: http://scholarship.law.stjohns.edu/tcl

Part of the Legislation Commons

Recommended Citation

This Diocesan Attorneys' Papers is brought to you for free and open access by the Journals at St. John's Law Scholarship Repository. It has been accepted for inclusion in The Catholic Lawyer by an authorized editor of St. John's Law Scholarship Repository. For more information, please contact cerjanm@stjohns.edu.
Mr. Nolan makes it difficult for me to stand up here and address you after all his very kind remarks. I might say that, while I have had some impact on the tax system in the past parade of years, I'm never sure when I'm addressing a group whether I should own up to being a participant in that or not. There seem to be many different ideas as to the quality of our tax system. I, like Jack, prefer to believe it has improved although many of us recognize deficiencies in many areas. Sometimes it's difficult to change the tax system even when you see what some of the deficiencies are.

Working with Jack when he was in the Treasury Department was a real privilege. His performance at the Treasury provides a standard for those of us who work there now.

As to the topic this morning, I should say first that I do not have any prepared remarks. Instead, I'd prefer to spend most of the time seeing if I can answer questions that you may have. But let me begin with a few generalized remarks.

We anticipate that the Administration's tax reform program will be presented later this year. It will have three major objectives: tax simplification, tax fairness, and capital formation. Tax simplification will, I believe, get a much heavier emphasis this time around than has been true in past tax reform proposals. Simplification is always a difficult goal to achieve. Sometimes, when you think you're achieving tax simplification, there is a bend in the procedure somewhere down the line; and the first thing you know, the tax law has become more complicated, rather than less complicated.

We are aiming directly at tax simplification as such. We have pursued that objective already in the Administration's tax stimulus package. The part of the package that was enacted is primarily concerned with tax simplification as well as some modest tax reduction. I'm referring to the flat standard deduction, which results in an increased standard deduction for most taxpayers. This does have the effect of shifting people away somewhat from itemized deductions. We anticipate that we will increase the proportion using the standard deduction from something like 69% to about 75% of the total. I point out, however, that 75% is not as high a proportion as was true at one time. Quite a number of years ago the proportion of non-itemizers was up around 80%. Also, I should add that inflation causes the
amount spent for itemized deductions to increase. Consequently, a standard deduction based on a flat dollar amount tends to be outgrown, and people over a period of time shift out of the standard deduction into itemized deductions unless you keep adjusting the standard deduction amount. Now, we have done that a number of times lately but there was quite a long period of time when there was no adjustment. So in a sense, we're simply coming back to a relationship that existed previously.

As nearly as I can tell, adjustments of the standard deduction really have relatively little impact on charitable giving. I have in my office a table which presents charitable giving as a percent of Gross National Product. It shows that as the tax law changes, the percentage of giving changes hardly at all. In other words, charitable giving seems to bear a relatively uniform relationship to GNP no matter what the tax law is. I should also indicate that religious organizations are probably less impacted by the tax laws than any other charities.

Perhaps, when you're talking about religious schools and colleges, you begin to spill over into the area where the tax law does have some impact as it does in the case of the private educational institutions. In the case of religious schools, I have a feeling that the tax treatment of unrealized appreciation of charitable gifts may have as big an effect as anything. One can argue that this problem is not dealt with adequately under present law. But I don't anticipate, at least for now, that there will be much change in the existing tax inducements to donate appreciated property to charity.

The relationship of itemized deductions and standard deductions has already seen one shift. And I anticipate that there will be consideration of reducing some itemized deductions in exchange for rate reductions. That is a part of the simplification that we hope to achieve: a cutback in itemized deductions in those areas where almost everybody takes them anyway and where it makes more sense to simply have lower rates and less computation for the individual to make.

I doubt, however, if there will be much change in the area of the itemized deduction for charitable contributions. We have looked at this issue. We've toyed with it some and, although I won't give any promises that it will stay the same for all time, I don't anticipate that the charitable deduction will be a subject for major consideration this year. Now, my view may change, but that is my impression as of this time. In the case of exempt organizations other than churches or conventions of churches, we may be looking at the self-dealing rules which presently apply to private foundations, in order to see to what extent extension of similar rules to other types of charitable organizations is desirable.

We also have before us the problem of the solicitation of funds by orders—and this could include religious orders as well as other groups. I'm sure you know some of the cases that gave rise to this consideration. The form that a proposal might take initially is a rather extensive public reporting of the solicitation expenses, including a requirement that the infor-
mation go to those who are being solicited, as well as being available to the general public.

With that, I think that I had better close and ask if you have any questions.

QUESTIONS TO LAURENCE N. WOODWORTH

QUESTION:

Yes, I would like to ask you a question, please. First, it is my understanding that there has been and presently exists a movement in this country to do away with the deduction for charitable gifts. You indicated that you don't foresee any activity along that line in the current session. I'd like to just project to probably the next two or three years, whether or not you believe that this deduction will be abolished, but more importantly, replaced by the theory that is being espoused among certain groups in this country to go along with the federal government in matching the gift made by the taxpayer, based on a formulated basis. I further have reason to believe that there are some groups in this country that are espousing this position to deny grants to religious organizations. I'm wondering whether or not you are aware of this movement, whether or not you have heard of this purported policy, namely, to abolish the deduction for charitable gifts, the government in turn matching the gift in part to the religious donee, thereby excluding religious organizations.

WOODWORTH:

I have heard of this idea, and I think I know some of the sources of it. However, I don't anticipate that anything like this is going to happen in the foreseeable future. The point that you raised is one of the difficulties; in other words, I believe that one of the last things anyone would want to do is to deny a deduction for gifts to a religious organization. The matching technique that you describe would present a problem because of the concept of the separation of church and state. I have real doubts as to whether anything of that type will come as far ahead as I can see.

Now, there have been proposals to put some kind of floor under charitable giving, and, the same time, to treat it as a separate deduction available to both a standard deduction person and an itemizer. This idea has received some consideration, but it's not really a simplifying feature and I doubt if that idea is going to move very far in the near future.

JIM SERRITELLA:

Do you anticipate that the Treasury will propose to treat charities generally the same way that private foundations are now being treated? Sort of eliminate the separate treatment between the two types of organizations?
WOODWORTH:

I'm not suggesting that. There's a whole series of rules that apply to private foundations, and I doubt that all of those rules would be applied to charities generally. Certainly all of those rules would not be extended to churches, conventions of churches and integrated auxiliaries; and I doubt if many of those rules would be applied even to other charitable organizations. At the same time, as I did suggest, consideration has been given to extending the private foundation self-dealing rule to some other types of charitable organizations.

QUESTION:

Would that include churches?

WOODWORTH:

It would not include churches, conventions of churches or integrated auxiliaries—at least in my opinion.

BOB ROBINSON:

Doctor, you just mentioned integrated auxiliaries.

WOODWORTH:

I shouldn't have used that term, should I?

QUESTION:

I'm glad and it's quite apparent that everyone here is also glad you did. Can we anticipate that this term is likely to be used in the legislation that might be presented by the Treasury Department in the near term?

WOODWORTH:

Well, it's possible. If you want to carve out churches and conventions of churches you usually want to carve out integrated auxiliaries as well. And I realize that you may not be entirely happy with the definition in this regard. My recollection is that this concept was first developed in connection with the application of the unrelated business income tax a number of years ago and used again in the charitable lobbying bill where Congress was trying to carve out religious organizations. The question is: exactly how much do you carve out? And that always is a difficult issue because almost every charitable activity that you want to mention can also be associated with a church or convention of churches. It is difficult to draw a line. Now, if you have problems with the way the term "integrated auxiliary" is used, I would suggest that you let us know; but let us know not just that you have a problem but also how you think we might come up with a solution that is more systematic than an arbi-
trary cutout of a particular organization. We have to approach the issue on a general basis, and we're open to suggestions if you think we have applied the definition incorrectly.

**QUESTION:**

How would you go about that?

**WOODWORTH:**

It's a difficult problem. You can take a general charitable organization which has a religious affiliation and cut it out from the application of the new provision. If you can come up with a concept of an integrated activity which is basically religious and not basically charitable or basically educational, then I think we'd like to hear about it. I signed off on those regulations. But I haven't any information which would help us in drawing a different kind of a line. That's really what I was requesting a moment ago. I don't feel that I've received concrete suggestions for distinguishing what is basically a charitable organization or basically an educational organization with some religious organization control.

**QUESTION:**

What about the lobbying bill?

**WOODWORTH:**

Let me say just one thing more about the lobbying bill on charitable organizations. I worked with Jim Robinson of your organization, and I found him as fair as anyone I've dealt with. After having worked with him on that legislation and earlier legislation, I certainly regard him not only as a very capable person, but also a very fair-minded individual, one with whom I'm happy to work.

**TOM RAYER:**

Could you indicate to us whether or not this current Treasury intends to take any positive position with respect to the possibility of legislation which would provide relief to a taxpayer for expenses paid in terms of educational tuition or other things of that nature?

**WOODWORTH:**

Yes, I testified against it. Our feeling is that a tax expenditure is not the best way to spend limited federal funds. It's obviously a worthwhile purpose. I'm well aware of it myself, for I've had three children that have gone through college and a fourth one in college now. I know what a heavy financial burden college expenses can be. Yet, I also know that I'm making the sacrifice, and I think others in a similar situation are doing the same;
so that relief from those expenses, if I were able to retain it, would simply mean that I would have more funds available to spend for something else.

One should also question who would be helped the most by tuition credits. Presumably, the educational institutions will increase their tuition fees by the amount of the credit. You know how hard pressed they are. I think, however, that if there is a credit applicable to tuition and fees, the public educational institutions will get a larger proportion of help than the private ones. Therefore, I think that the tax credit is not the best way to obtain relief for private educational institutions. It seems to me that you should be looking for ways of getting the state to take into account the fact that state expenditures for education are less because some parents are sending their children to private schools. Some states now provide some kind of compensation in that regard. If you're looking at private school costs, it seems to me that such a state compensation mechanism is a more effective approach than the tax credit.

FRANCIS O'CONNOR:

I will let you off the hook for the integrated auxiliary and take you to the church. Now, it seems to me that the Treasury Department in recent months has had at least a couple of opportunities to help us in defining the word “church.” Congress has used it in a good many instances but unless there's something that I don't know about, it seems to me that the word “church” so far hasn't been defined to be helpful to a practitioner of law in two or three areas. We are in a city where there are several women’s religious organizations—all women, devoting their lives strictly to religious activities, and maybe running some schools. Some may be teaching, some may be nursing. So far, I don’t know whether they are part of the church or not. The diocese itself is the legal arm of the church in the civil sense. I don't know of anything in writing from Treasury that says the Archdiocese of New York or the Archdiocese of Dubuque is or is not part of the church. The Christian Brothers have no ordained priests, as I understand it, but have all lay brothers dedicated to poverty, charity and obedience. So far as I know nothing has been said by the Treasury that says they are part of the church. So I mention just three; there are others. Can we anticipate something by way of some help as to what and who is part of the church or is it just something that is going to be an ad hoc decision every time it comes up in the courts?

WOODWORTH:

First of all, I don’t know whether requests for rulings have been made in these areas or not. We don’t usually volunteer definitions of that kind. Decisions are usually made in answer to specific situations. It’s difficult for us to deal in this area because the same kind of people that you’ve mentioned are engaged perhaps in hospital work and in educational work, and the question is whether those functions constitute church activities. I
think distinctions in this area are very difficult to draw without having everybody sweep themselves under the cover of church activity. A good share of the private schools in this country are still maintaining some religious affiliation, and certainly it isn’t the intent that they be characterized as religious organizations. If this is a major problem as far as you’re concerned as a group, it would be well for you to lay out the problem for us as clearly as you can and then write to us with suggestions. It’s difficult for us in the Treasury to give an answer in areas where we don’t know all of the facts and circumstances involved.

**Question:**

May I state just briefly that the Treasury Department through the rules of ERISA has now decided that religious communities of sisters and men are part of the church. And that’s for ERISA purposes, as I understand. Do we find ourselves in the situation that a religious community of sisters or a religious community of men may be part of the church for ERISA but not part of the church for 990 purposes?

**Woodworth:**

I think you should take a closer look at ERISA. In defining a “church plan” for ERISA purposes, there is a special grandfather provision that includes within that definition certain existing plans covering both church employees and employees of church agencies. Now, I don’t know whether that is the situation you are referring to. My recollection is that the last paragraph of the ERISA ruling merely states that members of religious orders of men and women shall be deemed part of the church provided they are an integrated part of the church, or something to that effect, and therefore the plan is exempt.

**John Nolan:**

Could I just make a comment on the subject for a minute. I think we’re in the process of evolution and transition, and people should realize it’s only been in the last few years that it’s become so very important to define the terms “church” and “integrated auxiliary” to the extent that it has become important. This occurred because things have been changing. We now have the unrelated business income tax applicable to church activity. We now have a much greater reporting requirement. We now have ERISA with special rules that affect churches. We now have a lobbying provision, the Conable Bill, which makes the definition of churches and integrated auxiliaries very important. We may have further legislation extending the private foundation rules to charities other than churches, so that all of a sudden within a period of several years a great deal of importance has come to rest on defining a concept which is extremely difficult to define, and we are groping for an answer to this problem. And there is a certain lack of consistency as the Service from time to time issues a regulation which
doesn’t seem comprehensive enough or doesn’t seem consistent enough with other actions. It seems to me that it’s part of the job of all of us to help the IRS and the Treasury to achieve consistency, to achieve a more complete, comprehensive solution to this problem, and that can’t be done overnight. It’s going to have to come slowly, carefully. It’s going to have to be built up over a period of time. We’re going to have to make the IRS realize as they issue a regulation defining one of these terms that it has implications for other areas of the tax law far beyond the specific problem that they’re dealing with in that regulation. Hopefully, over a period of time with a great deal of participation from groups such as this, we’ll evolve a definition in this area, or a series of definitions, which will be a lot more helpful than what we’ve had heretofore.

Woodworth:

Thanks, Jack, I subscribe completely.

Joe McGovern:

I’d like to ask a question along the same lines but a little more specific and with particular reference to the obligation to file Form 990. Take an order or congregation of religious women, a religious community. Now, it does not itself as a separate corporate entity operate any hospitals, welfare agencies or the like, but it does assign its members to hospitals, child care agencies, schools and other separate corporations who conduct specific activities. Now, it would seem to me without doubt under the regulation that the separate organization, the separate hospital, for example, would be obligated to file Form 990. But in my judgment, reading the regulations thus far I would think the religious congregation does not have to file 990. I’d like to know whether I am correct.

Woodworth:

It would be a mistake for me to try to give a ruling from the dais. But I might ask, have you had any indication that it might not be considered integrated?

Question:

No, the problem has come to life because of the fiscal year situation and the obligation to file hasn’t yet arisen.

Woodworth:

Then my initial impression is that the type of organization you’re referring to, if I understand what it is, probably should be considered an integrated part of the church. But I should caution you that I don’t hand out rulings even though I might have something to do with published rulings. There may be other facts and circumstances involved that I don’t
understand. But I’m giving you my general impression, which is that the case you describe does not sound to me like the separate type of organization to which these rules are supposed to apply.

JULES KERNER:

The 1976 Act among other things included an amendment to Section 513 of the Code to exclude the trade show income of Section 501(c)(5) and (c)(6) organizations. That’s the way it was written. After the Act was passed, it developed from some comments of the Senate Finance Committee that perhaps it had been intended to include Section 501(c)(3) organizations, also if not (c)(4)’s and (c)(7)’s, but this might have been omitted through a drafting oversight. There therefore is considerable confusion right now among Section 501(c)(3) organizations because it would appear on the face of it that (c)(3) organizations, having the same type of trade show income as (c)(5)’s and (c)(6)’s, at present are taxable, whereas the (c)(5)’s and (c)(6)’s are not. I have been told that some clarification on this from the Treasury or the Service was going to be forthcoming. Can you bring me up to date on that situation?

WOODWORTH:

We have the matter under consideration. We haven’t reached any conclusion. As far as the drafting error is concerned, my recollection is that this was one of those amendments which came in from the outside already drafted. So I am inclined to say that there may have been a policy error by those who handed the amendment in. It was simply passed out and approved by the committee in one day, and that was it. Whenever you get amendments of that type, I can forecast that they’re going to result in trouble because they haven’t been through staff examination in general terms. Drafted in this manner they start with the idea that somebody with a specific problem is trying to get relief in a specific area, and they could not care less what its impact will be on the tax law as a whole. After such an amendment is enacted, everyone says, “Look what it does in these other areas.” These problems probably existed in the first place and weren’t adequately considered. You’re right that we are left with a difficult problem. I would personally have a hard time explaining why the trade associations are treated better in that regard than 501(c)(3)’s, except perhaps to say that is what Congress saw fit to do.

QUESTION:

Well, then, do I gather that’s going to be the Treasury’s position?

WOODWORTH:

The Treasury has not reached a conclusion. However, it is difficult when the statute is specific to include things that are outside the statutory
language. We have not explored this issue fully, but I do think there are problems extending it beyond the trade association area in view of the way it was drafted when it came in.

**QUESTION:**

Is there going to be any definitive Treasury statement of position on this in the near future?

**WOODWORTH:**

There will be a Treasury statement, but I don't know the timing.

**SISTERS MELANIE:**

I have a simple question, I think. However, I am very confused by it. Earlier in your presentation you described the direction for defining "integrated auxiliaries" as charitable activities with sectarian control. That to me wipes out everything that I think I'm about. If we go back to Vatican II documents, we go back to religious communities and have them define themselves. They are not just doing jobs; they are engaged in apostolates and those are integrally related to the Gospel, to my perception. So what confuses me is why or who made the decision that the direction of the question would be whether you are charities that happen to have sectarian control, and not the reverse proposition that we are religious who happen to be engaged in some of the things that you may define also as charities. Now, when you extend an invitation to us to respond, I have no choice but to react to this rigid definition; you give me no latitude to respond in any other way. So my question gets down to who made that decision, and is that unchallengeable?

**WOODWORTH:**

I recognize your problem. But I really can't help you very much. You state your case very well. However, the difficulty I have is the fact that something which is educational or charitable, even though controlled by a religious organization is, as we understand it, not the type of organization that the Congress intended to cover under this definition of the "integrated auxiliary." In the case that was cited to me earlier, the organization itself didn't have as its principal activity these other charitable or educational activities, although individuals in the organization were perhaps assigned out to work in those activities. Judging from your question, I infer that you don't make this line of demarcation; you want to treat what is essentially an educational school under the auspices of a church differently from an educational organization. Under a contrary view, it isn't as if you are being cast off into utter darkness; these organizations would still get deductions.
They simply have certain reporting to do and have certain other rules which apply to them. What we're trying to do is to maintain the separation of church and state concept, and it's a very hard line to draw. If it is basically a charitable activity or an educational activity, I don't believe that it was intended to come within the integrated auxiliary definition provided by the Congress. Perhaps the Congress will give us more help in explaining that line than it has at the present time.

Kevin Kennedy:

I'm troubled by the fact that Congress, or at least the Internal Revenue people are dealing here with an institution of some 2,000 years in age, which over that period of time has not been concerned only with prayer but with what we call acts of mercy, alms houses, hospices, all the other different medieval institutions were built up and the church at that time was the only entity which actually engaged in this work. Now we come along into the 20th century and secular institutions and government have gotten into this type of work. It seems to me that we're being told that the church now has to be cut back and that these works of mercy are secular works, so that we have the term "integrated auxiliary" to deal with, and it isn't on its face definitive at all. As I understand it from what I've read, there has been no attempt to key it into this history that I speak of, so the result now is that we're going to have to write to Treasury for specific rulings on any vast number of fact situations only because the attitude now is that these works of mercy are of a secular character today. Therefore, these institutions of ours are going to have difficulty in proving that they're a church. We're almost coming to the point where the house of worship is the word "church" because actually we've had no other definition, so, I deplore that situation.

Woodworth:

That is more of a statement than a question. I am certainly well aware of the fact that the church has participated extensively in charitable and educational activities over many centuries. But now it is true that there are many others participating in those kinds of activities as well, and Congress has seen fit to draw a line, specifically intending one type of treatment to apply with respect to churches and another type of treatment to apply to schools, for example. Congress was very explicit in that regard. Our job at the Treasury is to interpret the law as written, and I don't see any possibility of escaping the fact that religious affiliated colleges, for example, are explicitly intended to be covered by the legislation. And I think you can say the same about general charitable activities. There's nothing in this legislation that says a church can't participate in this type of activity—far from it. No one is trying to abolish these types of charitable activities or educational activities. It's simply that certain types of rules and reporting requirements are imposed. That is what is being
asked in these cases, not that the church not participate in other charitable activities. I really think that a technique of reporting will have to be developed in some of these areas, and I don't think you can envelop the cloak of the church around all activities which are somewhat affiliated with the church.

JOHN CONNOR:

I have a quick question. As is obvious from the questions you've gotten so far, there are going to be some instances where we as attorneys representing not only the various dioceses, but various charities, are going to have to make judgment calls as to whether a particular organization should be reporting or not reporting. My question is: What is the policy of the Department going to be with reference to enforcement of penalties, should they disagree with our advice to our clients?

WOODWORTH:

I'd have to see the facts and circumstances involved before I could report on that.

NOLAN:

I think we owe Dr. Woodworth a debt of gratitude for his very frank and helpful explanation.