

# Charitable 501(c)(3) Tax-Exempt Status for Environmental Organizations: Issues and Requirements

Philip A. Moffat, Student  
University of Florida Conservation Clinic<sup>1</sup>  
Fredric G. Levin College of Law

Thomas T. Ankersen, Clinic Director

## Table of Contents

I. Introduction.....	2
II. Discussion.....	3
A. Requirements Applicable to All § 501(c)(3) Organizations.....	3
1. Organizational Test.....	4
2. Operational Test.....	8
3. Political Activities, Action Organizations and the § 501(h) Election.....	10
B. Requirements Applicable to All § 501(c)(3) Organizations Engaged in Litigation.....	19
1. Litigation as a Party Plaintiff.....	19
2. Public Interest Law Firms.....	21
III. Conclusion.....	33
IV. Resources and Application Information.....	33

---

<sup>1</sup> The University of Florida Conservation Clinic is an interdisciplinary legal clinic housed at the College of Law within the Center for Governmental Responsibility. Students from the College of Law and other disciplines within the University of Florida work together under the direction of the clinic director, Tom Ankersen, a licensed legal practitioner within the State of Florida. The clinic utilizes applied education to provide legal assistance to conservation projects of importance to the state.

## **Introduction:**

Thirty years into the environmental movement, the complexity and number of environmental laws continues to grow. Concomitant with this increase, the number of non-governmental organizations (NGOs) involved in environmental protection has also grown. There also appears to be a shift from large institutions, operating out of Washington, D.C. and other metropolitan areas, to smaller grass roots organizations addressing issues of local geographic and thematic importance. Not surprisingly, the complexity of regulations governing how these organizations operate has also increased. Many environmental groups seek to take advantage of tax-exempt status under Internal Revenue Code (I.R.C.) § 501(c)(3). While establishing and maintaining an organization's tax-exempt status provides significant benefits, it also poses significant responsibilities on organizations, particularly start up organizations. This report describes the regulatory requirements applicable to obtaining and maintaining tax exempt status. It does not represent legal advice, which should be sought from a licensed, practicing tax attorney, preferably one specializing in tax-exempt organizations.

This report details the general I.R.C. § 501(c)(3) requirements for all organizations, including those that choose to engage in lobbying for which special rules may apply. It further describes the issues and requirements for those who seek to employ litigation as a means to influence policy. Federal statutory, regulatory and other I.R.S. guidance is summarized. Most states maintain additional filing requirements for non-profit corporations which should be consulted, but are not discussed in this report.

## Discussion:

### A. Requirements applicable to all 501(c)(3) organizations:

All organizations desiring tax-exempt status under the Internal Revenue Code § 501(c)(3) must prove that they are organized for the benefit of a public purpose and not operated for the benefit of private interests.<sup>2</sup> They must be “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 animals.”<sup>4</sup> Furthermore, none of the net earnings may inure “to the benefit of any shareholder or individual.”<sup>5</sup> Nor may a substantial<sup>6</sup> amount of the organization’s<sup>7</sup> activities include carrying on propaganda, attempting to influence legislation, or participation or intervention in a political campaign on behalf

---

<sup>2</sup> Note that organizations qualifying as § 501(c)(3) organizations are presumed to be a private foundation. See I.R.S. Publication 557, *Tax-Exempt Status for Your Organization* (1998). However, § 501(c)(3) organizations receiving more than one-third of their support in each taxable year from grants, gifts, membership fees, etc. are categorically exempt. See I.R.C. § 509(a)(2)(A) (1999).

<sup>3</sup> Depending on their particular activities, environmental organizations may qualify under a number of these categories. The I.R.S. has indicated that some environmental organizations are “charitable.” See Rev. Rul. 75-74, 1975-1 C.B. 152.

<sup>4</sup> I.R.C. § 501(c)(3) (1999).

<sup>5</sup> *Id.*

<sup>6</sup> The meaning of the term substantial remains unclear. Guidance provided by the I.R.S. is discussed later in this report.

<sup>7</sup> "Organization" as used in this paper means corporations, community chests, funds or foundations as specifically set forth under I.R.C. § 501(c)(3). Individuals, partnerships and formless groups of individuals do not qualify.

of any candidate for a public office.<sup>8</sup> The I.R.S. has created two tests along with a limited set of prohibitions for all organizations attempting to qualify for and maintain 501(c)(3) tax-exempt status. These requirements are designed to ensure the appropriateness of the organization's purposes, organizational structure and planned activities in relation to the Congressional intent behind providing the tax exemption.

### **1.) The organizational test**

The organizational test ensures that the organization is organized exclusively for one or more exempt purposes.<sup>9</sup> The test assesses the appropriateness of the organization's purposes and the powers granted to it through its creating documents. The articles of organization (e.g., articles of incorporation, corporate charters, articles of association, etc.) are the sole basis for this assessment.<sup>10</sup> The purposes and powers are appropriate only if the articles both: 1. limit the purposes of the organization to one or more exempt purposes and 2. do not expressly empower the organization to engage in, other than as an insubstantial part of its activities, activities which are not in furtherance of one or more of the exempt purposes.<sup>11</sup>

---

<sup>8</sup> *See Id.* If elected, I.R.C. § 501(h) provides a limited exception to the “influencing legislation” limitations. This exception is discussed later in this report.

<sup>9</sup> *See* Treas. Reg. § 1.501(c)(3)-1(b).

<sup>10</sup> *See Id.*

<sup>11</sup> *See* Treas. Reg. § 1.501(c)(3)-1(b).

a.) Purposes

To satisfy the first requirement, the purposes of the organization can be no broader than those exempted.<sup>12</sup> However, they can be narrower, i.e, a particular subset of activities within those exempted.<sup>13</sup> If the purposes are broader than those exempted, the fact that the actual operations only further exempt purposes will not save the organization.<sup>14</sup> Assurances or statements by the members that they intend to operate the organization only in furtherance of exempt purposes are insufficient.<sup>15</sup> According to the regulations, the articles must pass "muster" based solely on the information contained within the four corners of the document.<sup>16</sup> The I.R.S. will not qualify an organization if it is too broadly empowered even though all of its actual activities may be in furtherance of the exempt purposes.<sup>17</sup>

b.) Powers

In determining whether the second requirement is satisfied, the I.R.S. evaluates the powers granted to the organization. If the articles of incorporation (or creating documents) empower the

---

<sup>12</sup> *See Id.* This suggests the importance of early organizational planning.

<sup>13</sup> *See Id.*

<sup>14</sup> *See Id.*

<sup>15</sup> *See Id.*

<sup>16</sup> *See Id.* *But see* Colorado State Society, 93 T.C. 39 (1989) (holding that the I.R.S. must consider all the facts and circumstances when evaluating the tax-exempt status of an organization. Specifically, the organization's articles did not provide for the distribution of assets upon distribution while the bylaws did.).

<sup>17</sup> *See Id.*

organization to engage in activities, in more than an insubstantial way, that are not in furtherance of one or more of the exempt purposes, the organization will not qualify, even if the articles specify that the organization is created for purposes no broader than those exempted.<sup>18</sup> For example, I.R.C. § 501(c)(3) prohibits "political" activities in more than insubstantial amounts. The organization may not attempt to influence legislation through propaganda or other methods.<sup>19</sup> It may not "directly or indirectly participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of or in opposition to any candidate for public office."<sup>20</sup> Additionally, the organization may not have objectives or engage in activities that would characterize it as an "action" organization.<sup>21</sup>

---

<sup>18</sup> *See Id.* Note, however, that the organization may participate in activities to influence legislation, if it elects to follow the provisions of I.R.C. § 501(h). If so elected, the organization's articles will not be found in violation of the organizational test.

<sup>19</sup> *See Id.*

<sup>20</sup> *Id.* This is a flat prohibition regardless of whether the organization elects to be governed by I.R.C. § 501(h).

<sup>21</sup> *See Id.* An "action" organization is an organization that:

- i.) devotes a substantial amount of its activities to either:
  - influencing legislation through propaganda or other means, i.e., by urging the public to contact a legislative body for the purpose of supporting, opposing or proposing legislation; or
  - advocating the adoption or rejection of legislation; or
- ii.) participates in or intervenes in, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office; or
- iii.) is only able to obtain its main or primary objective(s), and not its incidental or secondary objectives:
  - through the adoption or defeat of legislation, or
  - by advocating or campaigning for the attainment of such main or primary objectives.

*See* Treas. Reg. § 1.501(c)(3)-1(c).

c.) Distribution of Assets

Under the organizational test, the Service also reviews the articles or the applicable state law to ensure provisions for the proper distribution of assets in the event of the organization's dissolution.<sup>22</sup> Acceptable recipients of assets include the federal, state or local governments.<sup>23</sup> Distribution for other exempt purposes, public purposes or to other organizations who most similarly meet the objectives of the dissolved organization is also acceptable.<sup>24</sup> In other words, the articles or the applicable State law cannot provide for distribution to organization members or stakeholders without violating the prohibitions on the inurement of benefits to private interests.<sup>25</sup> Furthermore, the I.R.S. will look to the law of the state of incorporation when interpreting terms within the articles unless the state's interpretation can be proven by clear and convincing evidence as having a special meaning other than that generally accepted.<sup>26</sup>

---

<sup>22</sup> *See Id.* at 1(b). Since Florida Statutes allow for the redistribution of assets to members or other private interests, an organization will want to specify the appropriate distribution method in its articles of incorporation. *See* FLA. STAT. § 617.1406.

<sup>23</sup> *See Id.*

<sup>24</sup> *See Id.*

<sup>25</sup> *See Id.*

<sup>26</sup> *See Id.*

Finally, to establish the exemption, the organization must apply to the Service.<sup>27</sup> The application must include a detailed statement of its proposed activities.<sup>28</sup> Of the two tests, the organization test is more easily passed.<sup>29</sup>

## 2.) The operational test

While the organizational test looks to what the organization says in its papers, the operational test looks to what the organization does or plans to do. To pass the operational test, an organization must operate exclusively for one or more of the exempt purposes specified in § 501(c)(3). However, the I.R.S. defines “exclusively” as “primarily” in its regulations.<sup>30</sup> An organization must engage “primarily in activities which accomplish one or more of . . . [the] exempt purposes.”<sup>31</sup> Not surprisingly, the regulations provide minimal guidance as to what primarily means. This is further explained with the following, “an organization will not be [regarded as primarily engaging in exempt activities] if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.”<sup>32</sup> Hence, the I.R.S. looks to whether the activities are in furtherance of the organization’s

---

<sup>27</sup> *See Id.* See Section IV., *infra*, for a discussion of the application procedure.

<sup>28</sup> *See Id.*

<sup>29</sup> *See* Oliver Houck, *With Charity for All*, 93 YALE L.J. 1415, 1435 (1984).

<sup>30</sup> *See* Treas. Reg. § 1.501(c)(3)-1(c).

<sup>31</sup> *Id.*

<sup>32</sup> *See* Treas. Reg. § 1.501(c)(3)-1(c); *see also* I.R.S. *Exempt Organizations Handbook* § 332 (1983) *cited in* Oliver Houck, *With Charity for All*, 93 YALE L.J. 1415, 1435 (1984) (acknowledging the difficulties associated with defining “insubstantial” and “primarily,” noting that such terms are better defined and applied in the context of a particular factual situation, leaving the Service with considerable discretion).

exempt purpose and not whether the individual activities are charitable and exempt.<sup>33</sup>

The regulations offer an organization two possibilities for conducting activities not directly related to their exempt purpose. First, an organization may engage in a substantial amount of unrelated activities if they are in furtherance of one or more of the exempt purposes and are not the organization's primary purpose. Second, the organization may engage in an insubstantial amount of unrelated activities that are not in furtherance of the exempt purposes. Professor Houck offers the following factors to consider when evaluating whether an organization's activities fit within the regulations.

- i.) The quantum of exempt activities;
- ii.) The quantum of non-exempt activities;
- iii.) The nexus between the non-exempt activities and the organization's exempt purposes (the closer the nexus, the more likely the exemption); and
- iv.) The nexus between the non-exempt activities and traditional, commercial activity (the more commercial in appearance, the less likely the exemption).<sup>34</sup>

Essentially, the Service analyzes the organization's activities to ensure that they are not engaging in those which defeat the purpose of the exemption. e.g., private inurement, unrelated business, politics or substantial lobbying.<sup>35</sup>

---

<sup>33</sup> See Rev. Rul. 80-278. Furthermore, the Service does not assess the particular viewpoint of the organization. See also Rev. Rul. 80-278 (stating that a three-part test will be used in assessing the permissibility of an organization's activities; specifically, the organization's purpose must be charitable, the activities must be in furtherance of that purpose and reasonably related to that purpose, and the activities must not be illegal or contrary to a clearly defined and established public policy or in conflict with express statutory restrictions.) However, Revenue Rulings and Revenue Procedures are not binding.

<sup>34</sup> See Id. at 1437.

<sup>35</sup> See Treas. Reg. § 1.501(c)(3)-1(c). This regulatory section forbids the inurement of net earnings to private interests, activities substantially unrelated to the furtherance of an exempt purpose and prohibiting participation in "political" and other "action" activities. See also Oliver

### 3.) Political activities, action organizations and the 501(h) election

In order to maintain exempt status, I.R.C. § 501(c)(3) requires that an organization have, "no substantial part of [its] activities [devoted to] carrying on propaganda, or otherwise attempting, to influence legislation (except as provided in section (h)), [nor may it] participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office."<sup>36</sup> Such organizations are classified as "action" organizations. If an organization is classified as an "action" organization, it is considered to lack exclusive organization for exempt purposes.<sup>37</sup>

An organization may be classified as an action organization if *any* of the following criteria are satisfied:

- i.) the organization devotes a substantial amount of its activities to:
  - influencing legislation through propaganda or other means, i.e., by urging the public to contact a legislative body for the purpose of supporting, opposing or proposing legislation; or
  - advocating the adoption or rejection of legislation;<sup>38</sup> or
- ii.) by participating in or intervening in, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office;<sup>39</sup> or

---

Houck, *With Charity for All*, 93 YALE L.J. 1415, 1435 (1984).

<sup>36</sup> I.R.C. § 501(c)(3) (1999).

<sup>37</sup> *See* Treas. Reg. § 1.501(c)(3)-1(c).

<sup>38</sup> *See Id.* This regulatory section defines "legislation" to include any action by Congress, by a State legislature, by any local governmental body, or the public through a referendum, initiative, constitutional amendment. It does not include actions by administrative bodies unless the administrative body is being asked to encourage the adoption of legislation.

<sup>39</sup> *See Id.* This regulatory section defines "candidate for public office" as a person that offers himself/herself or is proposed by others as a contestant for either a Federal, State, or local

iii.) by only being able to obtain its main or primary objective(s), and not its incidental or secondary objectives:

- through the adoption or defeat of legislation, or
- by advocating or campaigning for the attainment of such main or primary objectives.<sup>40</sup>

An organization is flatly prohibited from intervening or participating in a campaign for public office. However, it may lobby for legislation and have its tax-exempt status protected so long as it remains within limits.

Organizations who feel the success of their mission depends on influencing legislation may have their activities judged by one of two standards: a.) the insubstantial activities standard (the Service calls this standard the "substantial part test") or b.) the expenditures test. The substantial part test is incorporated into the operational test for tax exempt status previously discussed. It is vague and dependent on the entirety of the circumstances. This is the default standard in the absence of an express election under I.R.C. § 501(h); it leaves the Service and the courts with greater discretion and creates greater uncertainty for an organization.<sup>41</sup> The second standard/test is the political expenditures test elected pursuant to I.R.C. § 501(h). Section 501(h) eliminates much of the uncertainty associated with the insubstantial activities standard. However, it has many drawbacks including excessive reporting and accounting requirements.<sup>42</sup>

---

public office. It also defines participation or intervention in a political campaign to include the publication or distribution of statements on behalf of or against such a candidate.

<sup>40</sup> *See Id.*

<sup>41</sup> *See* Anthony Mancuso, *Guidelines for Nonprofits: Legal Limits on Lobbying*, NOLO NEWS, Spring 1991, at 7. *See also* Treas. Reg. § 1.501(h)-1(a)(4).

<sup>42</sup> Personal conversation with Professor Steven J. Willis, Professor of Law, University of Florida Levin College of Law (April 12, 1999).

I.R.C. § 501(h) may be elected by the organization as a substitute for the substantial part test.<sup>43</sup> In order to elect, an organization must be one of several types of charitable organizations listed.<sup>44</sup> Many § 501(c)(3) organizations are eligible. Environmental organizations meeting the § 501(c)(3) requirements qualify so long as they receive a substantial amount of their support from the general public or qualified governmental entities, excluding moneys received in the exercise of their charitable function.<sup>45</sup> Once § 501(h) is elected, a charity may make lobbying expenditures within specified dollar limits, providing greater certainty.<sup>46</sup> The expenditure test is effective until the organization voluntarily revokes it or it is involuntarily revoked by the Service.<sup>47</sup> Furthermore, once the expenditure test has been elected, an organization may still lose its tax-exempt status if it is viewed as either one of the following two types of "action" organizations, 1.) it participates or intervenes in political campaigns or 2.) its *primary*<sup>48</sup> purpose is to influence legislation.<sup>49</sup>

---

<sup>43</sup> See I.R.C. § 501(h)(c) (1999). Should an organization not elect the § 501(h) exception, the substantial part test will be applied without regard to the provisions of § 501(h). See Treas. Reg. § 1.501(h)-1(a)(4).

<sup>44</sup> See Treas. Reg. § 1.501(h)-1(a)(2).

<sup>45</sup> See Treas. Reg. § 1.501(h)-2(b)(2)(iv) (citing I.R.C. § 170(b)(1)(A)(vi)). Money received in the exercise or performance of an organization's exempt purpose is money received in the exercise of their charitable function.

<sup>46</sup> See Treas. Reg. § 1.501(h)-1(a)(2). An organization must file Form 5768 with the I.R.S. when electing this test. Form 5768 may be filed at any time during an organization's taxable year and be applicable to that taxable year. New organizations may file this along with their Form 1023 application for recognition of exemption. See Treas. Reg. § 1.501(h)-2(a).

<sup>47</sup> See Treas. Reg. § 1.501(h)-2. If voluntarily revoked, an organization may re-elect the expenditure test. However, the test will not be applicable until the beginning of a new tax year.

<sup>48</sup> "Primary" is not defined in the Treasury Regulations. However, the Regulations state that "[i]n determining whether an organization has such characteristics, all the surrounding facts and circumstances, including the articles and all activities of the organization, [will] be

Expenditures to influence legislation under I.R.C. § 501(h) are divided into two categories, lobbying expenditures and grassroots expenditures. Each has its own quantifiable and determinable limit. An organization electing the provisions of I.R.C. § 501(h) must satisfy two general criteria:

- i.) it must not make *lobbying expenditures* in excess of the *lobbying ceiling amount* for its organizational type during each taxable year, and
- ii.) it must not make *grass roots expenditures* in excess of the *grass roots ceiling amount* for its organizational type during each taxable year.<sup>50</sup>

Lobbying expenditures are defined as "expenditures for the *purpose of influencing legislation*."<sup>51</sup>

Grass roots expenditures are defined similarly, excluding communications with members or employees of the legislative body, or government officials and their employees involved in legislative formulation.<sup>52</sup> The lobbying and grass roots ceiling amounts are 150% of the *lobbying and grass roots nontaxable amounts*, respectively.<sup>53</sup> These nontaxable amounts are determined through formulas provided by the I.R.S. For instance, grass roots nontaxable amounts for a taxable year are defined as twenty-five percent of the lobbying nontaxable amount for a given year. The lobbying nontaxable amount is based upon the total of the organization's exempt purpose expenditures.

"Influencing legislation" includes any attempt to affect legislation through public opinion or through communication with a member or employee of a legislative body, or any government official

---

considered." Treas. Reg. § 1.501(c)(3)-1(c)(3)(v).

<sup>49</sup> See Treas. Reg. § 1.501(h)-1(a)(4) (citing Treas. Reg. § 1.501(c)(3)-1(c)(3)(iii)-(iv)).

<sup>50</sup> See I.R.C. § 501(h)(1)(a)(A)-(B) (emphasis added).

<sup>51</sup> See I.R.C. § 4911(c)(1) (emphasis added).

<sup>52</sup> See *Id.* at (c)(3) (referencing I.R.C. § 4911(d)(1)(A)-(B)).

<sup>53</sup> See Treas. Reg. § 1.501(h)-3(c)(3)&(6).

or their employees involved in the formulation of legislation.<sup>54</sup> However, the I.R.S. has provided a generous number of exceptions to the definition of "influencing legislation." including:

- i.) making available the results of a non-partisan analysis, study or research;
- ii.) providing technical advice or assistance to a government body or committee that influences the legislation but which is requested by the government body;
- iii.) appearances before or communications to a governmental body in defense of the organization's existence, tax-exempt status, powers and duties, etc;
- iv.) communications between the organization and its *bona fide* members with respect to legislation or proposed legislation of direct interest to the to the organization and its members; and
- v.) communications with legislative members and government employees that are not designed to influence legislation.<sup>55</sup>

However, the following communications between an organization and its members are not excluded from the definition of "influencing legislation":

- i.) any communication between the organization and its *bona fide* members that are designed to encourage the members to communicate with the legislative member or government employee; and
- ii.) communications between the organization and its *bona fide* members designed to have the members encourage non-members to contact the legislative members or government employees formulating the legislation, or influence legislation through public opinion.<sup>56</sup>

---

<sup>54</sup> See I.R.C. § 4911(d)(1)(A)-(B).

<sup>55</sup> See *Id.* at (d)(2)(A)-(D).

<sup>56</sup> See *Id.* at (d)(3)(A)-(B).

If any of the non-exempt communications between the organization and its members occur, they are considered to be attempts to influence legislation.<sup>57</sup> The former of these nonexempt communications cannot be calculated into the organization's gross roots expenditures and must be considered part of the lobbying expenditures.<sup>58</sup> However, the latter nonexempt communications can be factored into the gross roots expenditures.<sup>59</sup>

The lobbying non-taxable amount affects the entire amount capable of being spent on "influencing legislation", whether gross roots or lobbying, without jeopardizing exempt status or having to pay excise taxes.<sup>60</sup> The I.R.S. provides the following formulas for determining an organization's lobbying nontaxable amount. The lobbying nontaxable amount is the lesser of \$1,000,000 or the amount calculated under the following formula.

- i.) If the exempt purpose expenditures are not over \$500,000 then the lobbying nontaxable amount is 20% of the exempt purpose expenditures.
- ii.) If the exempt purpose expenditures are over \$500,000 but not over \$1,000,000 then the lobbying nontaxable amount is \$100,000 plus 15% of the excess exempt purpose expenditures over \$500,000.
- iii.) If the exempt purpose expenditures are over \$1,000,000 but not over \$1,500,000 then the lobbying nontaxable amount is \$175,000 plus 10% of the excess exempt purpose expenditures over \$1,000,000.
- iv.) If the exempt purpose expenditures are over \$1,500,000 then the lobbying nontaxable amount is \$225,000 plus 5% of the excess exempt purpose expenditures over \$1,500,000.<sup>61</sup>

---

<sup>57</sup> *See Id.*

<sup>58</sup> *See Id.*

<sup>59</sup> *See Id.*

<sup>60</sup> *See* I.R.C. § 4911(a)(1). If an organization exceeds its gross roots or lobbying ceiling expenditure, it must pay an **excise tax** of 25% on the amount spent in excess of the ceiling amount.

<sup>61</sup> *See* I.R.C. § 4911(c)(2).

The grass roots nontaxable amounts are twenty-five percent of the lobbying nontaxable amount.<sup>62</sup> For example, if an organization spent \$500,000 in furtherance of its exempt purpose (including the cost of influencing legislation through either type of expenditure), it would have \$100,000 of the total to spend on lobbying expenditures and \$25,000 on grass roots expenditures.<sup>63</sup> Based on these figures, an organization would have a lobbying ceiling amount of \$150,000 and a grass roots ceiling amount of \$37,500 for this year.

Once the organization exceeds \$150,000 and \$37,500, respectively, it has to pay an excise tax of 25% on the \$50,000 and \$12,500 overruns.<sup>64</sup> Furthermore, it may risk losing its exempt status if it "normally" exceeds its ceiling amounts for the base years.<sup>65</sup> Base years include the determination year and the three taxable years immediately preceding.<sup>66</sup> A determination year is a taxable year for which the expenditure test is in effect and the amount of an organization's expenditures is being assessed.<sup>67</sup> To determine whether an organization normally exceeds its ceiling amounts a four year period is required.<sup>68</sup> A more detailed example, taken from the Treasury Regulations, illustrates the

---

<sup>62</sup> *See Id.* at (c)(4).

<sup>63</sup> *See* I.R.C. § 4911(e)(1)(C). However, the exempt purpose expenditures would not include amounts spent on fund-raising.

<sup>64</sup> *See* I.R.C. § 4911(a)(1).

<sup>65</sup> *See* Treas. Reg. § 1.501(h)-3(a).

<sup>66</sup> *See Id.* at 3(c)(7). This assumes that the organization was a § 501(c)(3) during the three years immediately preceding.

<sup>67</sup> *See Id.* at (3)(c)(8).

<sup>68</sup> *See Id.* at 3(b)(2). This section states that the base years do not include any taxable prior to the taxable year for which the organization receives § 501(c)(3) status. To determine if these new organizations "normally" exceed their ceiling amounts, the I.R.S. looks to the years since the organization received § 501(c)(3) status and elected the expenditure test under § 501(h). .

complexity of calculating an organization's expenditure amounts and whether it "normally" exceeds them. The following discussion accompanies Table 1, *infra*.

In Table I, the hypothetical organization elects the § 501(h) test in taxable year one and has not revoked it as of taxable year four.<sup>69</sup> For simplification, none of its lobbying expenditures are grass roots during this period. During the first three years, the organization is obligated to pay the 25% excise tax imposed on lobbying expenditures in excess of the lobbying nontaxable amount.<sup>70</sup> For year one, the taxable amount is \$20,000 and the excise tax is \$5,000. For year two, the taxable amount is \$40,000 and the excise tax is \$10,000. The same calculation is made for the years thereafter. Each of the four are years of determination for their particular taxable year during which the annual exempt purpose expenditures are made and the applicability of the excise tax is determined.<sup>71</sup>

---

<sup>69</sup> *See Id.* at 3(e)

<sup>70</sup> *See Id.*

<sup>71</sup> *See Id.*

Table 1<sup>72</sup>

Year	Exempt Purpose Expenditures (EPE)	Calculations	<u>Lobbying</u>	
			Nontaxable Amount (LNTA)	Lobbying Expenditures (LE)
Year 1	\$400,000	(20% of \$400,000 = )	\$80,000	\$100,000
Year 2	\$300,000	(20% of \$300,000 = )	\$60,000	\$100,000
Year 3	\$600,000	(20% of \$500,000 = )	\$115,000	\$120,000
Year 4	\$500,000	(20% of \$500,000 = )	\$100,000	\$100,000
<b>Totals</b>	\$1,800,000		\$355,000	\$420,000

For year one, the organization can demonstrate that its lobbying expenditures do not exceed the lobbying ceiling amount, i.e., 150% of the lobbying nontaxable amount.<sup>73</sup> For year two, the organization can prove that the *sum* of its lobbying expenditures for year one and year two do not exceed the *sum* of its lobbying nontaxable amounts for both years.<sup>74</sup> The same summation is made for years three and four.<sup>75</sup> Based on these calculations, the organization does not “normally” make lobbying expenditures in excess of its lobbying ceiling amount, i.e., the sum of its lobbying

---

<sup>72</sup> *See Id.*

<sup>73</sup> *See Id.*

<sup>74</sup> *See Id.*

<sup>75</sup> *See Id.*

expenditures for the four years does not exceed 150% of the sum of its lobbying nontaxable amount.<sup>76</sup>

*B. Requirements applicable to § 501(c)(3) organizations engaged in litigation:*

Environmental organizations looking to effect change through litigation may do so as either a named party plaintiff or a public interest law firm (PILF). A named party plaintiff participates in the litigation using outside counsel. A public interest law firm works similar to the private law firm model, litigating with its own attorneys on behalf of private clients. Depending on the choice made, significant issues arise. Each of these options and their associated tax exempt status consequences are discussed below.

**1.) Litigation as a party plaintiff**

Organizations litigating as a party plaintiff must meet the same § 501(c)(3) requirements as non-litigating tax-exempt organizations. In Revenue Ruling 80-278, the I.R.S. assessed the tax-exempt status of an organization established for the protection and restoration of environmental quality.<sup>77</sup> The group's principal activity included instituting and maintaining environmental litigation as a party plaintiff under state and federal environmental statutes.<sup>78</sup> The suits were typically brought against government agencies and private industries.<sup>79</sup> Furthermore, the organization maintained no

---

<sup>76</sup> *See Id.*

<sup>77</sup> *See Rev. Rul. 80-278, 1980-2 C.B. 175-76.*

<sup>78</sup> *See Id.*

<sup>79</sup> *See Id.*

staff attorneys.<sup>80</sup> Instead, it employed private counsel to bring and maintain the litigation.<sup>81</sup> The litigation was not brought where a substantial purpose was to benefit a private party or interest, and the litigation was financed through membership dues and public contributions.<sup>82</sup>

In its ruling, the I.R.S. articulated a three-part test to determine the permissibility of the organization's activities.<sup>83</sup> The test applied resembled the standard two tests (organizational and operational) applied to all § 501(c)(3) organizations with an additional requirement which is most likely applicable to all § 501(c)(3) organizations, even if not explicitly stated in the regulations. The test ensured that the organization maintained a charitable purpose; its activities were in furtherance and reasonably related to its exempt purpose; and that its activities were not illegal, contrary to a clearly defined and established public policy or in conflict with statutory restrictions.<sup>84</sup> All three parts were considered satisfied.

---

<sup>80</sup> *See Id.*

<sup>81</sup> *See Id.*

<sup>82</sup> *See Id.*

<sup>83</sup> *See Id.*

<sup>84</sup> *See Id.* It is unclear whether this test is an expansion of the operational test or a combination of the organizational and the operational tests. It is most likely a combination of both. However, Revenue Rulings and Revenue Procedures provide useful guidance. They are not binding on the courts or the Service. *See Rev. Rul. 72-1, 1972-1 C.B. 693,694-95* (stating that Revenue Rulings are provided to promote the uniform application of the law and unless the facts of an instant case are substantially similar to those in the Ruling, they should not be too heavily relied upon and that Revenue Procedures enjoy only a slightly elevated status as a generalization of the law designed to assist taxpayers with interpreting the I.R.C. but are also considered non-binding guidance only).

Applying the test, the I.R.S. recognized that efforts to protect the environment and natural resources for public benefit are charitable within the meaning of § 501(c)(3).<sup>85</sup> Furthermore, the I.R.S. noted that Congress and many states had provided for citizen enforcement of various environmental statutes, indicating that citizen enforcement is not contrary to an expressed public policy or other statutory mandate.<sup>86</sup> It concluded that enforcing environmental statutes through litigation provided a reasonable means of accomplishing the environmental organization's exempt purposes.<sup>87</sup>

This Ruling provides the following observations. First, enforcing environmental regulations or environmental protection generally may be considered a charitable purpose. Second, litigation can be considered an activity in furtherance of the exempt purpose, provided other § 501(c)(3) requirements are not violated.

## **2.) Public Interest Law Firms**

### **a.) Background**

Public Interest Environmental Law Firms (PILFs), like other § 501(c)(3) organizations, must be organized and operated exclusively for one of the exempt purposes. PILFs have at least one and perhaps two different exempt purposes, including education and charity.<sup>88</sup> Charity is defined “in its

---

<sup>85</sup> *See Id.* (citing the National Environmental Policy Act of 1969, 42 U.S.C. § 4321).

<sup>86</sup> *See Id.* (citing the citizen suit provisions of the Clean Air Act, 42 U.S.C.A. § 7604 and the Federal Water Pollution Control Act Amendments of 1972, 33 U.S.C. § 1365).

<sup>87</sup> *See Id.*

<sup>88</sup> *See* Richard M. Goldsmith, *The I.R.S. Man Cometh: Public Interest Law Firms Meet the Tax Collector*, 13 ARIZONA LAW REVIEW 857, 859 (1971) (considering PILFs to be

generally accepted legal sense.”<sup>89</sup> Specifically, the term includes, “lessening of the burdens of Government; and promotion of social welfare.”<sup>90</sup> Education includes “[t]he instruction of the public on subjects useful to the individual and beneficial to the community.”<sup>91</sup> The I.R.S. has recognized PILFS as charitable based on their provision of legal representation on issues of broad public importance that might not otherwise be brought by private counsel.<sup>92</sup> It was reasoned that private counsel could not bring the case due to a lack of economic feasibility.<sup>93</sup>

In addition to the standard § 501(c)(3) requirements, the I.R.S. imposed additional requirements on PILFs. Beginning in 1971 under Revenue Procedure 71-39, PILFs were required to satisfy an eight-part test to qualify for the § 501(c)(3) exemption.<sup>94</sup> In 1975 under Revenue Procedure 75-13, the I.R.S. further expanded upon these requirements in regards to the collection

---

organized for charitable and educational purposes).

<sup>89</sup> Treas. Reg. § 1.501(c)(3)-d(2). *See* Houck, *supra* note 23, at 1451. Professor Houck discusses that the entire § 501(c)(3) category is considered “charitable” although the regulation provides a non-exhaustive subcategory listing of charitable purposes which includes charitable, religious, scientific, testing for public safety, literary, educational, prevention of cruelty to animals and fostering national and international amateur sports competition. He notes that these subcategories provide the Service with discretion to establish further requirements.

<sup>90</sup> Treas. Reg. § 1.501(c)(3)-d(2).

<sup>91</sup> *Id.* at (d)(3). Considering PILFS as organized for an educational purpose is a bit of a stretch. However, during litigation an attorney does educate the jury/judge as to the importance of environmental issues within a specific context. The outcome may have serious implications for the public nonetheless, including their perception of the environment.

<sup>92</sup> *See* Rev. Proc. 92-59, 1992-2 C.B. 411 (interpreting the holding of Rev. Rul. 75-74, 1975-1 C.B. 152).

<sup>93</sup> *See Id.*

<sup>94</sup> *See* Rev. Rul. 71-39 (superseded by Rev. Proc. 92-59, 1992-29 I.R.B. 11).

of attorney's fees.<sup>95</sup> In 1992, the Service modified or superseded both Revenue Procedures.<sup>96</sup>

In this instance, the I.R.S. presented and discussed Revenue Rulings 74-75, 75-75 and 75-76 concurrently to resolve specific issues not adequately addressed within the prior Revenue Procedures or within these Revenue Rulings. In Revenue Ruling 74-75, the I.R.S. had been asked to rule on the tax exempt status of a PILF engaged in public interest litigation involving environmental protection, urban renewal and other social issues.<sup>97</sup> The I.R.S. concluded that the PILF was organized for charitable purposes because it provided a service to the entire community through the provision of legal services not ordinarily provided by traditional law firms.<sup>98</sup> Furthermore, the organization afforded courts and administrative agencies the opportunity to review issues of public importance.<sup>99</sup> The charitable character rested not on the particular position advocated by the organization, but instead on the "provision of a facility for the resolution of issues of broad public importance."<sup>100</sup> In essence, the PILF provided access to the administrative and judicial systems that would not otherwise be provided by private lawyers due to a lack of economic feasibility.<sup>101</sup>

---

<sup>95</sup> See Rev. Proc. 75-13, 1975-1 C.B. 662 (modified and superseded by Rev. Proc. 92-59, 1992-29 I.R.B. 11).

<sup>96</sup> See Rev. Proc. 92-59, 1992-2 C.B. 11 (revoking Rev. Rul. 75-75, 1975-1 C.B. 154, while amplifying Rev. Rul. 76-75, 1975-1 C.B. 154).

<sup>97</sup> See Rev. Rul. 74-75, 1975-1 C.B. 152, 153.

<sup>98</sup> See *Id.*

<sup>99</sup> See *Id.*

<sup>100</sup> *Id.*

<sup>101</sup> See *Id.* For this reason public interest litigation does not include environmental litigation of which the financial interests of private persons would be better served by private law firms.

Revenue Ruling 75-75 analyzed the status of a PILF similar to the one described in 74-75. However, the organization wanted to collect attorneys' fees from willing clients.<sup>102</sup> The I.R.S. reasoned that the collection of attorney's fees made a PILF indistinguishable from a private law firm and would invalidate its tax exempt status.<sup>103</sup> This policy was revoked in Revenue Procedure 92-59, creating greater flexibility and improving the success of PILFs.

Revenue Ruling 75-76 allowed PILFs to collect attorneys' fees when they were part of a court or agency award.<sup>104</sup> The fees had to be paid by the opposing party and used by the recipient for general operating expenses.<sup>105</sup> The I.R.S. approved these awards as consistent with the statutory and public policy objectives for establishing these awards, so long as the possibility of the award did not *substantially* motivate the firm's decision to take the case.<sup>106</sup> Furthermore, the award of attorney's fees did not indicate the economic interests were great enough to warrant the retention of private counsel.<sup>107</sup>

#### b.) Recent Guidance

In 1992, the I.R.S. established new guidelines for assessing the tax exempt status of PILFs,

---

<sup>102</sup> See Rev. Rul. 75-75, 1975-1 C.B. 154.

<sup>103</sup> See *Id.*

<sup>104</sup> See *Id.*

<sup>105</sup> See *Id.*

<sup>106</sup> See *Id.* (emphasis added). The "substantial motivation" prohibition is not repeated in Revenue Procedure 92-59.

<sup>107</sup> See *Id.*

revoking previous guidance documents and modifying others.<sup>108</sup> Revenue Procedure 92-59 established new procedures for determining whether a PILF was organized exclusively for charitable purposes, for the acceptance of court-awarded attorney's fees, and for the acceptance of client-paid fees.<sup>109</sup> The bulk of the new requirements are contained in Sections Three, Four and Five of the Procedure.

i.) Revenue Procedure 92-59 Section Three - General Guidelines

Section Three of Revenue Procedure 92-59 provided ten guidelines for PILFs to maintain their tax exempt status. The first guideline re-stated previous guidance under Revenue Procedure 71-39 which it superseded. Under **Guideline One**, litigation is acceptable if it can “reasonably be said to be in representation of a broad public interest rather than a private interest.”<sup>110</sup> In other words, the litigation “must be designed to present a position on behalf of the public at large on matters of public interest.”<sup>111</sup> Guideline One has been criticized on several grounds including standing, the definition of “broad public interest” and who decides what is in the public interest.<sup>112</sup>

---

<sup>108</sup> Note that the majority of the guidelines re-established do not significantly modify a majority of the previous guidelines. However, the guidelines regarding the collection of attorney's fees have been significantly modified, providing greater flexibility to PILFs.

<sup>109</sup> See Rev. Proc. 92-59, 1992-2 C.B. 411.

<sup>110</sup> *Id.*

<sup>111</sup> *Id.*

<sup>112</sup> See Goldsmith, *supra* note 8, at 861 (arguing that the technicalities of standing requirements may necessitate the assertion of a private interest and encouraging courts to look beyond simple technicalities to the purpose being served by the litigation; stating that is for the courts and not the I.R.S. to determine what is in the public interest). For these reasons, many PILFs team up with local organizations and citizens who are adversely affected by the

During Senate hearings in 1970, IRS Commissioner Thrower acknowledged that every legal action implicates some public interest and opted to define broad public interest in terms of what it was not, i.e., a substantial private interest.<sup>113</sup> He went on to explain that the financial interests of no single or small group should predominate in order to qualify.<sup>114</sup> This requirement is merely a restatement of the general § 501(c)(3) requirements for organizations to serve a public and not a private interest.<sup>115</sup>

**Guideline Two** was also originally provided in Revenue Procedure 71-39. It allows PILFs to serve as a friend of the court in certain actions. PILFS are allowed to participate in this capacity where there are significant private financial interests involved, warranting private representation, along with issues of broad public interest.<sup>116</sup>

---

environmental harm for which enforcement is sought.

<sup>113</sup> *See Id.* (citing *Hearings on Tax Exemptions for Charitable Organizations Affecting Poverty Programs Before the Subcommittee on Employment, Manpower, and Poverty of the Senate Committee on Labor and Public Welfare*, 91<sup>st</sup> Cong., 2d Sess. 16 (1970)).

<sup>114</sup> *See Id.*

<sup>115</sup> *See Id.* (questioning the necessity of this guideline or the usefulness of the Commissioner's explanation).

<sup>116</sup> *See Rev. Proc. 92-59*, 1992-2 C.B. 411-12.

**Guideline Three** is also a restatement from 71-39. It prohibits PILFs from “attempt[ing] to achieve its objectives through a disruption of the judicial system, illegal activity, or violation of applicable canons of ethics.”<sup>117</sup> This guideline has been criticized for creating the possibility that the I.R.S. and not the Bar will evaluate attorneys’ actions.<sup>118</sup>

**Guideline Four**, also a restatement, requires the PILF to file an annual report along with other required annual information, describing the cases litigated and the rationale for deciding that they would benefit the public generally.<sup>119</sup> This requirement enables the I.R.S. to ensure compliance with Guideline One.<sup>120</sup> Critics have questioned the necessity of requiring a submission of the rationale for taking the case.<sup>121</sup>

**Guideline Five** repeats the previous requirement that the policies, programs, and compensation plans of the organization are the responsibility of a committee (e.g., the Board) representative of the public interest.<sup>122</sup> Furthermore, the committee or board may not be *controlled* by employees of the PILF who litigate on behalf of the organization nor may they be members of any organization

---

<sup>117</sup> *Id.* at 412.

<sup>118</sup> *See* Goldsmith, *supra* note 81, at 862 (arguing that the I.R.S. is not the proper entity to assess the ethics of an attorney’s actions).

<sup>119</sup> *See* Rev. Proc. 92-59, 1992-2 C.B. 411-12.

<sup>120</sup> *See* Goldsmith, *supra* note 81, at 874 (citing I.R.S. Commissioner Thrower’s testimony in *Hearings on Tax Exemptions for Charitable Organizations Affecting Poverty Programs Before the Subcommittee on Employment, Manpower, and Poverty of the Senate Committee on Labor and Public Welfare*, 91<sup>st</sup> Cong., 2d Sess. 16 (1970)).

<sup>121</sup> *See Id.* (criticizing the notion that the I.R.S. is the proper judge of whether an individual is representative of the public interest; arguing that the guideline creates a significant obstacle to sole practitioners from being able to participate in public interest litigation).

<sup>122</sup> *See* Rev. Proc. 92-59, 1992-2 C.B. 412.

litigating on behalf of the PILF that is not itself a § 501(c)(3) organization.<sup>123</sup> The PILF may pick its board and decide whether the members are representative of the public interest.<sup>124</sup> However, the I.R.S. appears to reserve final judgement as to whether the public interest is actually represented.<sup>125</sup>

This Guideline is perhaps the most troubling of all the requirements for it creates the potential for the unauthorized lay control of legal professionals. It subjects attorneys to potential violations of the *Code of Professional Responsibility* which requires that attorneys exercise their professional judgement solely on behalf of their client and not at the direction of third parties.<sup>126</sup> This is particularly problematic where, as with PILFs, the third parties control the policies of the organization, including attorneys' salaries.<sup>127</sup> However, if the attorney fully discloses the situation (e.g., Board-controlled salary establishment) to a consenting client with the client maintaining the final voice in the disposition of the case, a violation will likely not result.<sup>128</sup> Courts who have allowed this limited form of lay control, look to the nonprofit nature of the attorney's services as a further justification for not finding an ethical violation.<sup>129</sup> However, the establishment of an independent legal

---

<sup>123</sup> *See Id.* Nothing in this guideline prevents employees involved in litigation from advising the board or committee on the merits of a cause of action. However, the board or committee should exercise its own independent judgement in order to avoid the appearance of control by the litigating employees.

<sup>124</sup> *See* Goldsmith, *supra* note 81, at 874.

<sup>125</sup> *See Id.*

<sup>126</sup> *See* Dennis G. Katz, *The Public's Interest in the Ethics of the Public Interest Lawyer*, 13 ARIZONA LAW REVIEW 886, 898 (1971) (citing MODEL CODE OF PROFESSIONAL RESPONSIBILITY, EC 5-21).

<sup>127</sup> *See Id.*

<sup>128</sup> *See Id.* (citing MODEL CODE OF PROFESSIONAL RESPONSIBILITY, EC 5-23).

<sup>129</sup> *See Id.*

committee, staffed by attorneys who choose the litigation and establish attorney salaries but do not litigate on behalf of the PILF, offers the greatest degree of prevention and certainty.

**Guideline Six** requires that the organization not be operated in a manner which would create confusion between the identity of a private firm and the PILF.<sup>130</sup> This guideline has been criticized for limiting the opportunities for sole practitioners or smaller firms from assisting with public interest concerns.<sup>131</sup> In these instances it would be difficult for the public not to associate the small firm or sole practitioner with their public interest work and have some private benefit inuring to the firm or individual.<sup>132</sup> Nonetheless, the current regulations do allow for PILFs to contract out work to private organizations so long as they do not create the identity confusion and they maintain control over the use of those funds for § 501(c)(3) purposes.<sup>133</sup>

**Guideline Seven** states that a PILF cannot have an “arrangement to provide, directly or indirectly, a deduction for the cost of litigation that is for the private benefit of the donor.”<sup>134</sup> This guideline appears unnecessary since it merely reiterates the basic requirements under § 501(c)(3), “an organization . . . [may not be] organized or operated for the benefit of private interests such as designated individuals.”<sup>135</sup> Problems result in trying to distinguish public from private interests. Presumably, if the donation is coordinated through a large number of individuals with the litigation

---

<sup>130</sup> *See Id.*

<sup>131</sup> *See* Goldsmith, *supra* note 81 *at*, 877.

<sup>132</sup> *See Id.*

<sup>133</sup> *See Id.* (citing Rev. Rul. 68-489, 1968-2 C.B. 210).

<sup>134</sup> *See* Rev. Proc. 92-59, 1992-2 C.B. 412.

<sup>135</sup> *See* Treas. Reg. § 1.501(c)(3) -1(d)(1)(i).

benefits inuring to a majority of the public, such an arrangement would be acceptable.<sup>136</sup> In practice, this means that a particular donor may not *expressly* tie the donation to particular litigation.

**Guidelines Eight, Nine and Ten** are simple as written. Eight requires that PILFs comply with the guidelines established in Sections Four and Five of Revenue Procedure 92-59, discussed below, for the collection of fees for service. Section Nine merely repeats the prohibitions found in §501(c)(3) and the exemptions of § 501(h) regarding lobbying and campaigning activities.<sup>137</sup> Guideline Ten allows PILFs to accept reimbursement from clients for out-of-pocket expenses associated with litigation.<sup>138</sup> Out-of-pocket expenses do not include attorneys' fees, but do include such costs as travel, filing fees and expert witnesses.<sup>139</sup> The provisions for the collection of attorney's fees are established in Section Four.

ii.) Revenue Procedure 92-59 Section Four - Acceptance of Attorney's Fees

Section Four of Revenue Procedure 92-59 contains eight guidelines concerning the collection of attorneys' fees. Most of these are new. Similar to the prior Revenue Ruling 75-76, the I.R.S. allows for the collection of attorneys' fees from opposing parties if awarded by a court or administrative agency or approved by such a body as part of a settlement agreement.<sup>140</sup> The PILF may accept attorneys' fees from its clients if it adopts Section Five described herein. Furthermore,

---

<sup>136</sup> See Goldsmith, *supra* note 81 at, 878.

<sup>137</sup> See *Id.*

<sup>138</sup> See *Id.*

<sup>139</sup> See *Id.*

<sup>140</sup> See Rev. Proc. 92-59, 1992-2 C.B. 412.

the possibility of a fee, however collected, may not be a consideration in the selection of cases.<sup>141</sup> The I.R.S. prohibits a PILF from taking a case in which the litigants have a sufficient financial interest to warrant the retention of private counsel.<sup>142</sup> However, in such cases that have a broad public interest, the PILF may represent that interest as amicus curiae or intervene in the case.<sup>143</sup> Perhaps the most interesting requirement for the collection of attorneys' fees mandates that all attorneys' fees, no matter how collected, may not exceed fifty percent of the total cost of operating the organization's legal functions averaged over a five year period.<sup>144</sup> This is measured in reference to the taxable year in which the fees are received and the four preceding taxable years.<sup>145</sup> Legal functions are defined broadly to include: attorneys' salaries, non-professional salaries, overhead and other costs incurred as the result of the organization's legal functions.<sup>146</sup> However, exceptions to the fifty percent rule are available at the request of the PILF, if warranted.<sup>147</sup>

---

<sup>141</sup> *See Id.* Note that in Revenue Ruling 75-76 it could not be a "substantially" motivating factor. The I.R.S. appears to have closed this loophole by raising the standard to a near prohibition.

<sup>142</sup> *See Id.* This is very similar to Revenue Ruling 75-74.

<sup>143</sup> *See Id.*

<sup>144</sup> *See Id.*

<sup>145</sup> *See Id.*

<sup>146</sup> *See Id.*

<sup>147</sup> *See Id.*

iii.) Revenue Procedure 92-59 Section Five - Additional Rules Applicable to Client-Paid Fees

Section Five prevents a PILF from making a profit on any particular case, limiting the collection of fees to the actual cost of the litigation.<sup>148</sup> Such costs would include salaries and overhead and other costs “fairly allocable to the litigation in question.”<sup>149</sup> This section also allows the costs to be charged against a retainer with any residual balance returned to the client.<sup>150</sup> Furthermore, once undertaken, the PILF cannot withdraw from a case on the basis of a client’s inability to pay.<sup>151</sup> All attorneys’ fees must be paid to the organization and not to the individual.<sup>152</sup> Instead, attorneys must be compensated through the organization on a reasonable flat salary basis, irrespective of the cases they have handled.<sup>153</sup> Furthermore, a PILF must not seek or accept fees in cases in which it would result in an a state statutory or ethical violation.<sup>154</sup> Finally, the organization must file a report along with its other annual information, detailing the attorneys’ fees sought and recovered.<sup>155</sup>

---

<sup>148</sup> *See Id.*

<sup>149</sup> *Id.*

<sup>150</sup> *See Id.*

<sup>151</sup> *See Id.*

<sup>152</sup> *See Id.*

<sup>153</sup> *See Id.* Note in Revenue Procedure 75-13 “reasonable” was equated with a government salary.

<sup>154</sup> *See Id.*

<sup>155</sup> *See Id.*

**Conclusion:**

Environmental organizations wanting to obtain and maintain tax exempt-status face similar requirements as other charitable organizations. First, they must be organized and operated exclusively for an exempt purpose while satisfying other prohibitions on the inurement of private benefit and the allocation of assets upon dissolution. Second, they must not campaign for candidates for public office and they must either devote an insubstantial amount of their activities to influencing legislation or adopt the provisions of § 501(h). Considering many environmental organizations' interests to influence legislation, electing the provisions of § 501(h) may provide the greatest flexibility and certainty before the I.R.S., although it creates an additional reporting requirement.

Litigation to enforce environmental statutes provides another opportunity for organizations to further their exempt, charitable purpose. Organizations may choose to litigate as a party plaintiff, or participate as a public interest environmental law firm (PILF). Litigating as a party plaintiff creates no significant requirements for maintenance of § 501(c)(3) status. Public interest law firms have additional requirements primarily regarding control of the organization, and collection and reporting of attorneys' fees. The I.R.S. has provided a great deal of flexibility while ensuring that public interest law firms are distinguishable from private firms, thus protecting the purpose of the § 501(c)(3) exemption.

**Resources and Application Information:**

The I.R.S. or other entities provide the following sources of information on the establishment and maintenance of a § 501(c)(3) organization.

*A. Publications*

*Publication 557, Tax-Exempt Status of Your Organization*

*B. Websites*

The University of Florida LL.M. Program in Taxation maintains an excellent site at the following address: <<http://nersp.nerdc.ufl.edu/~acadian/taxsites/presites.htm>>. This website will automatically link you to many I.R.S. sites, publications and forms.

The I.R.S. maintains the following website with many of the same materials provided by the University of Florida: <[http://www.irs.ustreas.gov/bus\\_info/eo/index.html](http://www.irs.ustreas.gov/bus_info/eo/index.html)>.

*C. Phone Numbers*

- 1.) Free Publications and Forms - (800) 829-3676
- 2.) Tax Questions - (800) 829-1040

