



May 31, 2012

**VIA CERTIFIED MAIL AND E-MAIL**

The Honorable J. Russell George  
Treasury Inspector General for Tax Administration  
Department of the Treasury  
1401 H Street, NW, Suite 469  
Washington, DC 20005  
E-mail: [Complaints@tigta.treas.gov](mailto:Complaints@tigta.treas.gov)

**RE: REQUEST FOR INVESTIGATION OF TEXAS ORGANIZING PROJECT AND TEXAS ORGANIZING PROJECT EDUCATION FUND**

Dear Inspector General:

We write on behalf of Cause of Action, an independent 501(c)(3) public interest group that uses public advocacy and legal reform strategies to ensure greater transparency in government and protect taxpayer interests and economic freedom.

The Internal Revenue Service (IRS) has recently indicated that it is investigating the abuse of charitable organizations and deductions.<sup>1</sup> We therefore write to request that the IRS open an investigation into the Texas Organizing Project (TOP), which is not a 501(c)(3) entity, and Texas Organizing Project Education Fund (TOP ED), a 501(c)(3) charitable foundation that acts as TOP's fiscal sponsor.<sup>2</sup> As we show herein, TOP ED's fiscal sponsorship of TOP may be improper. It appears that TOP could be using the funds it receives from TOP ED to engage in political activities, which, as you know, are not (c)(3)-exempt activities.

For example, TOP recently posted an event announcement on its website, seeking volunteers to "phone-bank and door knock for Mary Ann Perez, candidate for State Rep HD-

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<sup>1</sup> Paul Streckfus, *Email Update 2012-31*, EO TAX J., (Feb. 17, 2012), *citing* IR-2012-23 ("IRS examiners continue to uncover the intentional abuse of 501(c)(3) organizations, including arrangements that improperly shield income or assets from taxation and attempts by donors to maintain control over donated assets or the income from donated property. The IRS is investigating schemes that involve the donation of non-cash assets -- including situations in which several organizations claim the full value of the same non-cash contribution. Often these donations are highly overvalued or the organization receiving the donation promises that the donor can repurchase the items later at a price set by the donor. The Pension Protection Act of 2006 imposed increased penalties for inaccurate appraisals and set new standards for qualified appraisals.")

<sup>2</sup> It appears that TOP is either a 501(c)(4) exempt organization or a non-exempt organization.

144.”<sup>3</sup> This is an explicit electioneering communication. TOP is a self-professed community and electoral organizing “non-profit” organization that “promotes social and economic equality for low to moderate income Texans.”<sup>4</sup> Although TOP also calls itself a “non-profit,” it is unclear whether the IRS has so designated it. In 2010, TOP received over \$640,000 from TOP ED.<sup>5</sup>

While fiscal sponsorships are legal, it is not legal for a 501(c)(3) organization, such as TOP ED, to give any money to an organization that engages in political activity, without triggering various tax consequences. Moreover, TOP either *is* or *is not* a 501(c)(4) organization. If TOP *is not* a (c)(4) organization, then it should be taxed according to its status, including any applicable back taxes, and any taxes that may be triggered by its electioneering communications. If TOP *is* a (c)(4) organization, the IRS should revoke its tax-exempt status because electioneering communications are not permissible activities for a 501(c)(4) organization; rather, these communications are non-taxable events only for a Section 527 organization. Communications such as the one explained above, therefore, would be inconsistent with any (c)(4) status held by TOP.

As we have explained, we believe TOP ED may be improperly fiscally sponsoring TOP. Below, we provide background information on the permissible and impermissible uses of a fiscal sponsorship and request investigation and action by the IRS.

## I. GENERAL PRINCIPLES

As the IRS has stated, a “fiscal sponsorship” occurs “when one or more charities choose to financially support another charity or nonexempt project.”<sup>6</sup> According to Gregory Colvin, a leading exempt organizations attorney who is counsel to the Alliance of Californians for Community Empowerment (“ACCE”), the rebranded California ACORN chapter,<sup>7</sup> these arrangements “typically arise when a person or group (we will call this a project) wants to get support from a private foundation, a government agency, or tax-deductible donations from individual or corporate donors,” and “[b]y law or preference, the funding source will only make payments to organizations with 501(c)(3) tax status.”<sup>8</sup> Fiscal sponsorships have also been known as “fiscal agents,” but practitioners disagree on the proper nomenclature.<sup>9</sup>

A fiscal sponsorship relationship can be effectively and lawfully utilized in a variety of situations where a person or group intending to engage in charitable activities wishes to attract tax-deductible contributions without having official exemption by the IRS under § 501(c)(3) of the Internal Revenue Code.<sup>10</sup> For example, “[f]iscal sponsorship is often temporary, used for

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<sup>3</sup> Press Release, Texas Organizing Project Website, (May 19, 2012), *available at* <http://www.organizetexas.org/node/1078>

<sup>4</sup> About, “Mission,” Organizetexas.org, last accessed May 24, 2012, *available at* <http://www.organizetexas.org/about/mission>.

<sup>5</sup> TOP ED’s 2010 Form 990, attached hereto as Exhibit A.

<sup>6</sup> 94 TNT 71-46.

<sup>7</sup> Matthew Vadum, *ACORN’s California Makeover*, AMERICAN SPECTATOR, (Jan. 21, 2010), *available at* <http://spectator.org/archives/2010/01/21/acorns-california-makeover>.

<sup>8</sup> GREGORY L. COLVIN, FISCAL SPONSORSHIP: 6 WAYS TO DO IT RIGHT, 3 (1993) [hereinafter “COLVIN”].

<sup>9</sup> *Id.* For clarity, we will refer to such arrangements as fiscal sponsorships.

<sup>10</sup> TAX ECON. CHAR. GIVING § 3.02



that period before a new organization obtains its own tax exemption. Other variations occur when a small 501(c)(3) group needs a larger 501(c)(3) organization to manage its financial affairs or seeks IRS classification as a public charity based on its relationship with the sponsor.”<sup>11</sup>

While the IRS has yet to provide concrete guidance on the issue, it has indicated approval of fiscal sponsorships by 501(c)(3) organizations only if certain conditions are satisfied. Specifically, a 501(c)(3) organization is allowed to accept tax-deductible funds on behalf of a non-501(c)(3) entity if the following three conditions are satisfied:<sup>12</sup>

1. The project being carried out by the non-501(c)(3) organization is “in furtherance of [the 501(c)(3)’s] own exempt purposes”;
2. The 501(c)(3) organization “retains control and discretion as to the use of the funds”;
3. The 501(c)(3) organization “maintains records establishing that the funds were used for section 501(c)(3) purposes.”

The IRS has provided examples of appropriate uses of fiscal sponsorships:

1. C, an individual, desires to start a tutoring program in the inner city but does not have sufficient resources or the sophistication needed to apply for tax exemption. C submits a grant application to X Community Foundation for financial support for the tutoring program. X approves the grant, establishes a fund called the C Fund, and solicits contributions for this fund. X is C's fiscal sponsor.
2. X community foundation approaches S Private Foundation soliciting for C's fund. S makes a grant to X designated for the C Fund. S, in the instrument of transfer, gives X full control over the investment decisions concerning the grant and full discretion in determining how much and when distributions from the fund will be made.
3. X Community Foundation receives a grant request from Z Charity. X reviews and approves the request. X establishes the Z Fund, and solicits contributions for this fund.

In each of the above situations, X acts as a fiscal sponsor; notice that in the second situation, S, a private foundation, is relieved of exercising expenditure responsibility because it gave X full control over the grant's income and corpus.<sup>13</sup>

## **II. MISUSE OF FISCAL SPONSORSHIP**

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<sup>11</sup> COLVIN, *supra* note 7 at 4.

<sup>12</sup> Rev. Rul. 68-489, 1968-2 C.B. 210.

<sup>13</sup> 94 TNT 71-46.

Several legal experts have opined that fiscal sponsorship can be misused by organizations wishing to skirt various Federal laws. For instance, such arrangements can be used as a “passthrough, or conduit, or laundering arrangement where the (c)(3) is really doing no more than receiving money from a donor or foundation and passing it on to a person or an organization that does not have (c)(3) status.”<sup>14</sup> John Edie, a leading nonprofit tax attorney, described a fiscal agent as a “laundering agent,” and added, “[i]f you’re going to use a fiscal agent, to me you’re saying, ‘Well, I’m going to launder the money through somebody.’”<sup>15</sup>

According to Lee Sheppard, an editor at *Tax Analysts*, “[a] fiscal agent is a money laundry. People who want to finance projects that would not, if separately incorporated, have a charitable purpose often form an exempt organization . . . to act as a conduit[ ] for the money used to finance the project so that its backers can claim a charitable deduction.”<sup>16</sup> Mr. Sheppard noted that “fiscal sponsorship . . . is a common practice, and one that the IRS should shut down.”<sup>17</sup>

Even Gregory Colvin, a leading proponent of fiscal sponsorship relationships, has voiced concerns over their misuse: “[i]f the control mechanisms are not administered properly, [a fiscal sponsorship arrangement] can collapse into a ‘conduit’ or ‘step transaction’ in which the IRS will disregard the role of the sponsor and declare that the funding source has, in effect, made a payment directly to a non-501(c)(3) project.”<sup>18</sup>

Distressingly, fiscal sponsorships can and have been used as conduits for political activity. I.R.C. § 501(c)(3) prohibits (c)(3) organizations from engaging in political activity.<sup>19</sup> However, the IRS itself has recognized the potential for misuse of fiscal sponsorships, particularly by using a 501(c)(3) organization as a conduit for an improper transaction, and has provided potential examples:

1. X, a philanthropist, wants to give to Z, an individual who is poor. X knows that a transfer directly to Z lacks the necessary public benefit to be considered charitable. X would not be entitled to a charitable tax deduction. To avoid this result, X donates money to Y Community Foundation with instructions to distribute it to Z. Y has no discretion as to the distribution of the funds. Here, Y is nothing more than a conduit. X is not entitled to a deduction.
2. C, a private foundation, wishes to support a nonexempt charitable project. (A nonexempt project, as used in this context, is a charitable activity of an

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<sup>14</sup> COUNCIL ON FOUNDATIONS, TOP TEN WAYS FOUNDATIONS GET INTO TROUBLE (2008), available at [http://www.washingtongrantmakers.org/s\\_wash/images/client/TopTenTrouble.pdf](http://www.washingtongrantmakers.org/s_wash/images/client/TopTenTrouble.pdf).

<sup>15</sup> *Transcript of the Winter ABA EO Committee Meeting: Panel Six: The Use and Misuse of Fiscal Sponsorship Arrangements*, 7 EXEMPT ORG. TAX REV. 570, 571(1992).

<sup>16</sup> Lee Sheppard, *Charitable Money Laundering*, 8 EXEMPT ORG. TAX REV. 645 (1993).

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

<sup>18</sup> COLVIN, *supra* note 7, at 28.

<sup>19</sup> See I.R.C. § 501(c)(3) (1986) (providing that an organization qualifies for exemption only if it “does not participate in, or intervene in (including the publishing or distributing of statements) any political campaign on behalf of (or in opposition to) any candidate for public office.”)

organization that does not have an IRS determination letter.) C does not want the burden of exercising expenditure responsibility, but wishes to maintain continuing supervision of the project. C gives the money to Y Community Foundation after Y has agreed that C will maintain continuing control and that the money will be used solely for the project.

3. S, a fledgling organization, is struggling to maintain public charity status. T, a wealthy donor, wants to give S a large contribution. If T gives it directly to S, the contribution will be subject to the two percent of total support limitation and S would fail the public support test. To avoid this, T "earmarks" the money for S and runs it through the Y Community Foundation. Y has no discretion but to distribute the money to S.

In the preceding three examples, Y Community Foundation has no control over the donations. Y is acting as a mere conduit in a transfer between the donor and the ultimate recipient. The donor and the recipient are the only beneficiaries in these transactions.<sup>20</sup>

According to Professor Frances Hill, 501(c)(3) organizations can be attractive for political donors because of the tax deduction they provide. She wrote, "the most likely [corporate-candidate] conduit, and the one offering the greatest benefits, is a 501(c)(3) organization that is absolutely prohibited from supporting or opposing candidates for public office."<sup>21</sup> As Professor Hill noted, 501(c)(3) organizations are attractive due to lax reporting standards: "Because 501(c)(3) contains the absolute prohibition, 501(c)(3) organizations are not subject to the tax reporting requirements imposed on other 501(c) organizations by 527 and they are not required to register with and report to the FEC."<sup>22</sup> In other words, a donor wishing to engage in political activities could funnel his money through a 501(c)(3) fiscal sponsor to a third organization and still potentially receive a tax deduction for his contribution.

### **III. Request for Investigation**

On October 21, 2011, Cause of Action wrote to you requesting an investigation into the Association of Community Organizations for Reform Now (ACORN), a non-exempt organization, and several of its 501(c)(3) affiliates, including the New York Agency for Community Affairs, Inc. (NYACA), ACORN Institute, Inc. (now renamed the Alliance Institute), American Institute for Social Justice (AISJ), and the Affordable Housing Centers of America (AHCOA, formerly ACORN Housing).<sup>23</sup> Evidence uncovered and submitted to you suggested that ACORN had instructed its affiliates to funnel tax-deductible and/or taxpayer dollars to ACORN over a forty year period.

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<sup>20</sup> 94 TNT 71-46.

<sup>21</sup> Frances R. Hill, *Corporate Philanthropy and Campaign Finance: Exempt Organizations As Corporate-Candidate Conduits*, 41 N.Y.L. SCH. L. REV. 881, 927 (1997).

<sup>22</sup> *Id.* at 927-928.

<sup>23</sup> Letter from Keith Gates, Senior Attorney, Cause of Action to Douglas Shulman, Commissioner, IRS, (Oct. 21, 2011) (attached as Exhibit B).



After ACORN became subject to public scrutiny, and eventually filed for bankruptcy, it rebranded many of its state chapters in order that those organizations could continue pursuing ACORN's goals. TOP is the reconstituted ACORN in Texas. The findings regarding ACORN contained in our letter are therefore highly relevant to any investigation of the activities of TOP, and are incorporated into this request.<sup>24</sup>

The activities and interests of TOP are similar and aligned with that of ACORN, as TOP acknowledges on their website. Because TOP is not a 501(c)(3) organization and is a fiscal client of TOP ED, the Internal Revenue Code imputes the activities of the fiscal client to the fiscal agent; any organization that acted as a fiscal sponsor for TOP therefore engaged in political activity if TOP engaged in political activity.

Therefore, we respectfully request that the IRS investigate both TOP and TOP ED violations of the tax code, specifically violations of Sections 501(c)(3) and, if applicable, 501(c)(4) of the Internal Revenue Code. We further request that the IRS determine whether civil and criminal fraud penalties are appropriate in light of any revealed violations.

Should you have any questions, comments, or concerns, please do not hesitate to contact me (Karen.Groen.Olea@causeofaction.org) or Adam Butschek (Adam.Butschek@causeofaction.org) at 202-507-5880. Thank you for your attention to this matter.

Sincerely,

  
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KAREN GROEN  
SENIOR COUNSEL

cc.: Hon. Douglas Shulman, IRS Commissioner  
Hon. Lanny A. Breuer, Assistant Attorney General, Criminal Division, U.S. Department  
of Justice

Encl.: As stated.

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<sup>24</sup> See Exhibit B.