
LITIGATION AS A TOOL FOR ACHIEVING PUBLIC POLICY GOALS: THE US EXPERIENCE

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EDITOR'S INTRODUCTION

WHILE CANADIAN CHARITIES HAVE SOMETIMES USED THE COURTS TO ACHIEVE their purposes, they have done so far less than their American counterparts. There are likely several reasons for this, including the cost of litigating, a generally less litigious culture, and courts that have been reluctant to usurp the role of legislators and render policy decisions. Nevertheless, litigation can be a valuable tool to effect public policy change, to improve decision making, or to clarify the law.

It is now well settled in the US that charities can use litigation as a tool to achieve their public policy objectives, but that has not always been the case. The evolution of litigation as a public policy tool for charities in the US, as described in the article below, is informative for the Canadian context.

INTRODUCTION

IF ONE ACCEPTS THAT CHARITIES ARE CHARGED WITH OPERATING FOR THE public benefit, as distinguished from private benefit, then the question of the tools by which the public benefit is secured should be essentially irrelevant, as long as the chosen path is legal. In the United States, the history of charities using litigation as a tool to achieve public policy goals that the charity deems to be for public benefit has its roots in civil rights and civil liberties struggles in the nineteenth century.

As might be expected, initial efforts by charitable trusts to advance public policy objectives were turned aside by the courts. Early court decisions, such as *Jackson v. Phillips* (1867) in Massachusetts, concluded that the promotion of women's suffrage and the abolition of slavery were political in nature, and that efforts to further those goals were not charitable, as they were intended to "modify or subvert" the law. While the purposes of the specific testamentary trusts at issue in *Jackson* did not contemplate litigation as a means to achieve the trusts' goals, the trusts did contemplate using education and similar efforts at public persuasion. By the early twentieth century, groups like the American Civil Liberties Union and the National Association for the Advancement of Colored People had begun using those same educational and lobbying tools to advance their goals of social change. Frustration with the effectiveness and the pace of those efforts, and aggressive efforts by opponents to block them through legal and extra-legal means, led the ACLU and the NAACP to use litigation as a step towards social change (Rabin, 1976).

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This article provides an overview of the legal context for those early efforts and traces their evolution into general acceptance in the United States today of social change as a valid charitable goal and litigation as an appropriate tool for achieving that goal.

CHARITY LAW IN THE US

In order to understand the evolution of social change as a valid charitable goal and litigation as an appropriate tool to achieve that end, it is important to have a general understanding of the nature of charity law in the US. There are essentially two sets of charity law that are loosely related: 1) at the federal level, Congress has enacted standards for charities as part of the Internal Revenue Code, which is applicable in all 50 states as an overlay on state law; and 2) each of the 50 states has its own standards and rules, as well as common law precepts, with the exception of Louisiana, where, because of its history as a French colony, the legal tradition is drawn from the Napoleonic Code (Yiannopolous, 1999).

At the federal level, the Internal Revenue Service is charged with administering the Internal Revenue Code, including the provisions dealing with the 29 types of tax-exempt organizations, of which charities are the largest component. At the state level, enforcement is generally housed in the State Attorney General's Office, although some functions, such as fundraising regulation, may be housed in the Secretary of State's Office or in a Consumer Protection Agency.

While this regulatory scheme suggests a tangle of 51 different legal regimes, in fact, common law concepts, drawn from historic English common law, serve as a common core (with the exception of Louisiana) on which occasional state-level or federal-level variations have been engrafted to address specific issues. For example, in its official interpretation of section 501(c)(3) of the Internal Revenue Code, which is the statutory provision exempting charities from federal income tax, the US Treasury Department has issued regulations that closely track the preamble to the 1601 English Statute of Charitable Uses (*Treas. Reg. Sect. 1.501(c)(3)-1(d)(2)*).

The Treasury Department and the Internal Revenue Service issue "revenue rulings," which are condensed statements of fact, followed by the government's interpretation of how the tax law would apply to the facts. Such pronouncements are binding on the Treasury and IRS, but not on courts or citizens. An additional form of guidance is found in "general counsel memoranda," which are legal analyses prepared by IRS attorneys as advice to the agency's administrators. The memoranda are not binding on either the IRS or Treasury, but they do outline the general approach to legal analysis and the legal theories that the government believes are appropriate for a given factual situation. Over the years, a number of revenue rulings and general counsel memoranda have dealt with charities, litigation, and public policy.

LITIGATION AS AN APPROPRIATE TOOL: THE FEDERAL STANDARD

The primary way in which US law at the federal level endorses the aims of organizations formed for the purpose of litigation is by exempting them, under certain conditions, from federal taxation. Organizations seeking to obtain or maintain tax-exempt status under section 501(c)(3) must be "engage[d] primarily in activities that accomplish one

or more ... exempt purposes specified in section 501(c)(3),” a list that includes “charitable” purposes (*Treas. Reg. § 1.501(c)(3)-1(c)(1)*). The Treasury Regulations define the term “charitable” to include “the promotion of social welfare by organizations designed ... to defend human and civil rights secured by law” (*Treas. Reg. § 1.501(c)(3)-1(d)(2)*). The Internal Revenue Service has long maintained that “the scope of the term ‘human and civil rights secured by law’ should be construed quite broadly ... to include such rights provided not only by the Constitution of the United States or of a state, but also by federal or state statutes” (Gen. Couns. Mem. 38468, 1980).

The Service has explicitly recognized that “litigation activities are a reasonable means of accomplishing ... exempt purposes,” where such activities are “reasonably related to the accomplishment of the [organization’s] charitable purpose, and are not illegal or contrary to public policy” (Revenue Ruling 80-278, 1980). For example, the Service held that an environmental organization whose principal activity consisted of instituting litigation to enforce environmental legislation was operated exclusively for charitable purposes. In so ruling, the Service pointed out that Congress “provided for private litigation to enforce federal laws in numerous environmental statutes.” The Service inferred from these private rights of action that Congress “approv[ed] of private litigation as a desirable and appropriate means of enforcing” those statutes and protecting the environment (Revenue Ruling 80-278, 1980).

Consistent with the Regulations and principles articulated above, the Service and courts have ruled that supporting or conducting litigation to defend “human and civil rights secured by law” is a charitable activity. For example, the Service ruled that an organization whose “sole activity” was to fund litigation to defend the members of a particular religious sect in prosecutions that threatened to abridge their First Amendment right to religious freedom was “promoting social welfare by defending human and civil rights secured by law” (Rev. Rul. 73-285, 1973). Similarly, the IRS Counsel’s Office has concluded that an organization funding litigation on behalf of victims of discrimination in employment based on sex – an act prohibited by Title VII of the Civil Rights Act of 1964 – “operates to defend civil and human rights” within the meaning of section 501(c)(3) (Gen. Couns. Mem. 38578, 1980). The scope of “civil and human rights” is further illustrated by *Nat’l Right to Work Legal Defense & Educ. Found. v. U.S.*, (1979), in which a federal district court held that an organization whose primary activity was to initiate litigation on behalf of workers whose employment was jeopardized by compulsory unionism was a charitable organization because its primary activity was to protect and defend the right to work – a “fundamental” right.

It should be noted, however, that the US Tax Court, in *Retired Teachers Legal Defense Fund v. Comm’r* (1982), ruled that an organization protecting the financial stability of the New York City Teachers’ Retirement System is not a charitable organization because it serves private interests of its members rather than “human [or] civil rights.” This suggests that the courts will draw a distinction between a litigation charity that restricts its activities to a particular organization, and an organization that litigates on behalf of an indefinite group of organizations.

Being engaged in a recognized charitable activity is necessary, but not sufficient, to ensure that a litigation organization is treated as tax exempt for the purposes of US federal

law. As the Service has explained, “any organization seeking exemption on the basis that it provides legal representation in the defense of ‘human and civil rights secured by law’ must comply with all of the other rules governing charitable entities, such as the rule of Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii) that the organization serve a public rather than a private purpose” (Gen. Couns. Mem. 38468). The Service has articulated several factors that may be relevant when analyzing whether an organization that conducts or supports human rights litigation serves a public purpose, namely whether:

- the litigation engaged in can reasonably be said to promote human and civil rights secured by law (broadly construed);
- the litigation will have a substantial impact beyond the interests of litigants;
- the selection of cases by the organization for its support is made by a board or committee that is representative of the public and is not controlled by employees, persons who litigate on behalf of the organization, or by any commercial entity;
- the primary source of financial support of the organization is from the persons being represented, which would suggest a “quid pro quo” arrangement with those individuals akin to the private practice of law; and
- the organization has an arrangement permitting a donor to claim, directly or indirectly, a charitable deduction for the cost of litigation that serves the donor’s private benefit (Gen. Couns. Mem. 38638, 1981). This scenario would, of course, suggest that the organization was providing a form of tax shelter, enabling a litigant to take a tax deduction for expenses that would otherwise not likely qualify as deductible business expenses or charitable contribution deductions to reduce taxable income.

LITIGATION AS AN APPROPRIATE TOOL: THE STATE STANDARD

While organizations that litigate to achieve public policy goals for the public benefit have also received favourable treatment under state charity law, that viewpoint has not escaped challenge. In the relatively few instances where state courts have been tasked with deciding the issue, they have held that litigation intended to impact public policy does fall within the meaning of “charitable” under state law, at least after first resolving the issue of whether litigation is intended to change law or merely improve the interpretation of existing law. For example, in *New England Legal Found. v. City of Boston* (1996), a Massachusetts state court considered whether a certain public interest law firm was entitled to exemption from property taxes. The law firm considered its mission to be “promoting public discourse on the proper role of free enterprise in our society and advancing free enterprise principles in the courtroom” (New England Legal Foundation, 2013).

Arguing against the organization’s petition for exemption, the City of Boston reasoned that the New England Legal Foundation did not qualify because the group’s “program of test-case litigation attempts to effect immediate changes in the law,” suggesting that the organization was intending to supplant the legislature. This argument was premised on the traditional English and Massachusetts rule governing charitable trusts. According to

the rule, if a trust is organized for the purpose of altering existing laws, then it is not entitled to the favourable vesting, perpetuities, and alienation rules attaching to charitable trusts, as held in *Jackson v. Phillips* (1867): “[T]rusts whose expressed purpose is to bring about changes in the laws or the political institutions of the country are not charitable in such a sense as to be entitled to peculiar favor, protection and perpetuation from the ministers of those laws which they are designed to modify or subvert” (citing *De Themines v. De Bonneval*, (1828) 38 Eng. Rep. 1035 (Ch); 5 Russ. 288; *Habershon v. Vardon*, (1851) 4 De Gex & Smale 467).

In *New England*, the court rejected this argument, explaining that “[c]ourts interpret and apply law already enacted or made part of a constitution by appropriate means. A public interest law firm communicating with judicial officers (acting in their core capacity of deciding cases) does not attempt to change the law, but only aids the court in interpretation. Thus *pro bono* legal activities and legal services organizations generally aid in the vindication of legal rights.” While cautioning that an organization lobbying for a change in existing law would not qualify for charitable treatment under the traditional rule, the court made clear that this was not a correct or appropriate characterization of impact litigation. Rather, the court held that the purpose of litigation is to ensure compliance with *existing* legal obligations and to vindicate *existing* legal rights. A court in Illinois recently agreed, affirming that “a public interest law firm, undertaking impact litigation that affects minorities” is, in fact, “an Illinois charitable corporation” for the purposes of state law (*United Legal Found. v. Pappas*, 2011).

The reasoning of the *New England* court is consistent with the exemption at the federal level for organizations formed for the purpose of obtaining “rights secured by law” described above (Revenue Ruling 80-278). It also illustrates that even jurisdictions adhering to the traditional proscription against charitable legislative advocacy have recognized the charitable *bona fides* of impact litigation organizations. Although there is little case law directly on point, it is likely that most US jurisdictions treat these kinds of organizations even more favourably than Massachusetts. After all, the majority of US states do not follow the traditional English rule in the first place, instead allowing charities to advocate freely for changes in the status quo. For example, in a Pennsylvania case, *Taylor v. Hoag*, (1922), the court noted that “to hold that an endeavor to procure ... a change in a law is, in effect, to attempt to violate that law would discourage improvement in legislation and tend to compel us to continue indefinitely to live under laws designed for an entirely different state of society.”

As under federal law, a *bona fide* charitable purpose is necessary but not generally sufficient for favorable state law treatment. Organizations whose primary mission is to litigate for charitable causes must meet, as all charities must, all other requirements in order to guarantee their state tax exempt status. For example, in the *New England* case, the court concluded that work performed must be in the public interest, rather than merely addressing private legal claims of the organization’s members.

To my knowledge, no state court has yet held that the use of litigation as a primary vehicle for advancing charitable aims disqualifies an organization for legal treatment as a charity. Certainly, *New England* and *United Legal* establish that there is affirmative precedent for treating these groups as possessing legitimately charitable missions.

A HURDLE OVERCOME

In the early 1900s, courts throughout the US uniformly rejected the practice of law by for-profit corporations, mainly out of concern that lawyers would be beholden to the profit motive rather than their clients' best interests, the profession's ethical standards, or the administration of justice.¹ Such a restriction also applied to nonprofit corporations.

However, many states now permit exemptions from these requirements for organizations engaged in public benefit-oriented impact litigation. In California, for example, nonprofit legal organizations are treated as exempt from the usual restrictions on the corporate practice of law under an official opinion of the California Attorney General (55 *Ops. Cal. Atty. Gen.* 39 (1972)). Although there is little case law directly on point, the California Attorney General also considers nonprofit corporations to be exempt from the requirements of the state's Professional Corporation Act, which regulates and restricts the extent to which corporations can engage in the practice of law. The Attorney General's opinion states, "We conclude therefore that certain nonprofit associations which employ counsel to represent their members in matters of common interest ... or which are established and operated for the purpose of preserving and defending the constitutional and legal rights and interests of the indigent or oppressed ... do not fall within the proscription against the corporate practice of law." According to the Attorney General, groups that are "established and operated for the purpose of preserving constitutional and legal rights," conduct impact litigation, or engage in litigation not simply as a "technique of solving private differences ... [but as] a form of political expression" are among the types of legal organizations expressly exempt from the requirements. Based on this express exemption, it is reasonable to infer that California considers impact litigation to be a *bona fide* charitable activity, standing in contrast to "the oppressive, malicious, or avaricious use of the legal process for purely private gain."

While the California example is illustrative, the policy of exempting litigation-focused charities from the usual ban on the corporate practice of law is not confined to that state alone. Similar exemptions can be found in Michigan, Illinois, and Louisiana, among other states.

If states were hostile or apathetic towards organizations formed for the purposes of conducting test case or impact litigation, they would likely not have given these organizations the benefits of the corporate form. Because they increasingly *do* grant such a benefit, it is reasonable to assume that these statutes and administrative opinions reflect a public endorsement of these organizations' charitable aims, as well as recognition that they provide a public benefit deserving of preferential legal treatment.

CONCLUSION

In sum, despite the cacophony of overlapping state and federal legal regimes in the US, it is now well settled that charities can utilize litigation to achieve an impact on public policy, providing that the goal is a public, rather than private, benefit. That outcome survived challenges based on assertions that litigation was a form of lobbying or legislative activity in disguise, that it bore the characteristics of the ordinary practice of law, particularly when plaintiff organizations received fees or other remuneration as part of a successful challenge, and hurdles found in the ethical rules relating to the corporate practice of law.

NOTE

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1. See, for example, *People ex rel. Illinois State Bar Ass'n v. People's Stock Yards State Bank*, (1931); *In re Otterness*, (1930); *People v. Merchants Protective Corp.*, (1922); and *In re Co-operative Law Co.*, (1910).

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