
SENATE COMMITTEE ON GOVERNANCE AND FINANCE

Senator Anna M. Caballero, Chair

2021 - 2022 Regular

Bill No: SB 834
Author: Wiener
Version: 4/18/22
Consultant: Deitchman

Hearing Date: 4/20/22
Tax Levy: Yes
Fiscal: Yes

TAX-EXEMPT STATUS: INSURRECTION

Allows the Franchise Tax Board to revoke tax exempt status for non-profit entities upon notification from the Attorney General that the non-profit engaged in certain illegal activities.

Background

Exempt entities. Federal law allows an organization to apply with the Internal Revenue Service (IRS) for tax-exempt status when the entity is organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, educational, or other specified purposes and that meet certain other requirements. When these conditions are met, these entities are tax exempt under the Internal Revenue Code (IRC), meaning that the net income of the organization is not subject to federal corporate income tax, and taxpayers can deduct contributions to the organization from taxable income. Most exempt entities are qualified under IRC section 501(c)(3).

To keep exempt status, entities must operate within their defined charitable purpose. According to the IRS, “A section 501(c)(3) organization will jeopardize its exemption if it ceases to be operated exclusively for exempt purposes. An organization will be operated exclusively for exempt purposes only if it engages primarily in activities that accomplish the exempt purposes specified in section 501(c)(3). An organization will be disqualified if more than an insubstantial part of its activities does not further an exempt purpose.” 501(c)(3) states that organizations:

- Must refrain from participating in the political campaigns of candidates for local, state, or federal office;
- Must restrict its lobbying activities to an insubstantial part of its total activities;
- Must ensure that its earnings do not benefit any private shareholder or individual;
- Must not operate for the benefit of private interests such as those of its founder, the founder's family, its shareholders or persons controlled by such interests;
- Must not operate for the primary purpose of conducting a trade or business that is not related to its exempt purpose, such as a school's operation of a factory;
- May not provide commercial-type insurance as a substantial part of its activities;
- May not have purposes or activities that are illegal or violate fundamental public policy;
- Must satisfy annual filing requirements.

In addition to loss of the organization's tax-exempt status, activities that constitute any personal gain by one of the organization's members, or misuse of the organization's assets may result in the imposition of penalty excise taxes on individuals benefiting from excess benefit transactions.

A tax-exempt organization that does not file a required annual return or notice for three consecutive years automatically loses its tax-exempt status.

California generally conforms to the tax-exempt status provided by the IRS. However, state law permits FTB to determine independently if an exempt organization preforms the actions required to maintain their tax-exempt status, and revoke its status for state purposes if it does not.

The California Attorney General's Office (AG) regulates charities and the professional fundraisers who solicit on their behalf. The purpose of this oversight is to protect charitable assets for their intended use and ensure that the charitable donations contributed by Californians are not misapplied and squandered through fraud or other means¹.

January 6, 2021 Capitol riot. According to the United States Department of Justice², “Wednesday, April 6, 2022, marked 15 months since the attack on the U.S. Capitol that disrupted a joint session of the U.S. Congress in the process of affirming the presidential election results. The government continues to investigate losses that resulted from the breach of the Capitol, including damage to the Capitol building and grounds, both inside and outside the building. According to a May 2021 estimate by the Architect of the Capitol, the attack caused approximately \$1.5 million worth of damage to the U.S. Capitol building.”

To date, the criminal charges filed in connection with the Capitol riot are as follows:

- More than 250 defendants have been charged with assaulting, resisting, or impeding officers or employees, including over 85 individuals who have been charged with using a deadly or dangerous weapon or causing serious bodily injury to an officer.
- Approximately 140 police officers were assaulted Jan. 6 at the Capitol, including about 80 U.S. Capitol Police and about 60 from the Metropolitan Police Department.
- Approximately 10 individuals have been arrested on a series of charges that relate to assaulting a member of the media, or destroying their equipment, on Jan. 6.
- Approximately 695 defendants have been charged with entering or remaining in a restricted federal building or grounds.

According to a February 2022 article reported by NPR³, “The nonprofit Patriot Freedom Project became one of the most prominent groups supporting the "political prisoners" criminally charged in the Jan. 6, 2021 attack on the U.S. Capitol.” This group has applied for non-profit status with the IRS, the status of that application is unknown.

The United States Department of Justice reported⁴ that on January 3, 2022, “the federal grand jury in the District of Columbia returned an indictment charging 11 defendants with seditious conspiracy and other charges for crimes related to the breach of the U.S. Capital on January 6.” According to court documents, among those charged is Elmer Stewart Rhodes III, the founder and leader of the “Oath Keepers.” The Oath Keepers group was granted tax exempt status by the IRS in 2019. That status of that tax-exempt status today is unclear.

¹ [Charities | State of California - Department of Justice - Office of the Attorney General](#)

² [15 Months Since the Jan. 6 Attack on the Capitol \(justice.gov\)](#)

³ [Controversial nonprofit for Jan. 6 riot defendants makes changes after criticism : NPR](#)

⁴ [Leader of Oath Keepers and 10 Other Individuals Indicted in Federal Court for Seditious Conspiracy and Other Offenses Related to U.S. Capitol Breach | OPA | Department of Justice](#)

Seeking to clarify FTB's ability to revoke the tax exempt status of organizations that engaged in illegal activity, the author wants to explicitly allow the AG's office to make a determination allowing FTB to revoke an organization's tax exempt status. .

Proposed Law

Senate Bill 834 provides that the FTB has the authority to revoke an exempt organization's tax exempt status when the AG notifies the FTB that is has determined that an exempt organization has actively engaged in, or incited the active engagement in, any of the acts or conspiracies defined as criminal under the following United States Code Sections and that is directed to, and likely to produce, imminent violation of one or more of these sections:

- Section 2381: Treason;
- Section 2382: Misprison of Treason;
- Section 2383: Rebellion or Insurrection;
- Section 2384: Seditious Conspiracy;
- Section 2385: Advocation Overthrow of Government;
- Section 2387: Activities Affecting Armed Forces Generally.

The bill states that the authority of the Franchise Tax Board to revoke an exemption from tax, as a result of an AG notification does not constitute a change in, but is declaratory of, existing law.

SB 834 states that the AG and the FTB may prescribe rules, guidelines, procedures, or other guidance to carry out the purposes of this section.

State Revenue Impact

Pending.

Comments

1. Purpose of the bill. According to the author, "SB 834 revokes the California tax-exempt status of a nonprofit organization if the Attorney General determines that the nonprofit has actively engaged in or incited treason, misprison of treason, insurrection, seditious conspiracy, advocating overthrow of the government or the government of any State, or advocating mutiny by members of the military or naval forces of the United States. If the Attorney General finds that a nonprofit organization has incited or actively engaged in an act that is directed and likely to imminently violate one or more of these crimes, they shall notify the Franchise Tax Board (FTB), who shall revoke the nonprofit's tax-exempt status.

"On January 6, 2021, pro-Trump extremists and insurrectionists – incited by the 'Big Lie' (the fraudulent notion that the 2020 election was stolen) and then-President Donald Trump – breached the United States Capitol. Five people were killed and hundreds were injured as a result of this insurrection. A variety of individuals and organizations – including nonprofits participated in the events on January 6th. Nonprofits raised millions of tax-free dollars off the 'Big Lie' that the 2020 presidential election was stolen.

"SB 834 fills an important gap. While the FTB is currently directed to suspend the tax-exemption of a nonprofit supporting international terrorism, there is no clear authority concerning

nonprofits that support insurrection. SB 834 will ensure that nonprofit organizations engaged in insurrection-related offenses will be held to the same standard as those that engage in or support international terrorist activity, and also have their exemption revoked.

“As the United States Supreme Court held in *Bob Jones University v. United States* (1983), it is permissible for the IRS to deny tax-exempt status to a private school with explicitly racist policies. The Court held that entitlement to tax exemption depends on meeting certain common-law standards of charity, namely, that a nonprofit organization seeking tax-exempt status must serve a public purpose and not be contrary to established public policy.

“Tax-exempt status is a privilege, not a right. Organizations that engage in, or incite the active engagement of insurrection-related offenses – both of which are illegal – should not be given this special status to help them fundraise.”

2. Current law. Current federal and state law require that an exempt organization only carry out activities that are for their charitable purpose, as defined in the articles of incorporation provided to the IRS and FTB. The IRS, FTB, and the AG have the authority to question the activities of any exempt organization to ensure that the funds collected from donors are being used for the activities that the entity has promised to promote and encourage. An IRS regulation⁵ states that “an organization will not be regarded as operated ‘exclusively’ for IRC 501(c)(3) purposes if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.” The presence of a single non-charitable purpose, if substantial in nature, can result in the revocation of tax-exempt status regardless of the number or importance of truly charitable purposes⁶. Therefore, if an organization engages in illegal acts that are a substantial part of its activities, it does not qualify for exemption under IRC 501(c)(3). The Committee may wish to consider the need for the bill when the authority to revoke an exempt organization’s status for the illegal activities listed in the bill already exists.

3. Who decides? The bill requires the AG to determine whether an exempt entity had participated in the prohibited activities to the extent that the AG determines that their exempt status should be revoked. The bill states that FTB may revoke the organization’s exempt status upon notification from the AG. The measure does not require a conviction after a criminal trial for the AG to notify FTB, only an administrative determination. Additionally, while the bill contains criteria that the AG should use to make the determination, it does not set forth a process for making it, or for those determined by the AG to meet the bill’s criteria to process an appeal or challenge that determination. While the bill does allow the AG and FTB to issue regulations, the Committee may wish to consider whether the measure would benefit from additional procedural detail.

4. Double referral. The Senate Rules Committee has ordered a double referral of SB 834 first to the Senate Governance and Finance Committee to hear issues of tax exempt status and then to the Senate Public Safety Committee.

⁵ Regulation 1.501(c)(3)-1(c)(1)

⁶ *Better Business Bureau v. United States*, 326 U.S. 279 (1945)

Support and Opposition (4/18/22)**Support:**

All Rise Alameda	Indivisible OC 46
Anti-Defamation League	Indivisible OC 48
Building the Base Face to Face	Indivisible Petaluma
Change Begins With ME	Indivisible Sacramento
Cloverdale Indivisible	Indivisible San Bernardino
Contra Costa MoveOn	Indivisible San Jose
Defending Our Future: Indivisible in CA 52nd District	Indivisible San Pedro
East Valley Indivisibles	Indivisible Santa Barbara
El Cerrito Progressives	Indivisible Santa Cruz County
Feminists in Action Los Angeles (Indivisible CA 34 Womens)	Indivisible Sausalito
Hillcrest Indivisible	Indivisible Sebastopol
Indi Squared	Indivisible SF
Indivisible 30/Keep Sherman Accountable	Indivisible SF Peninsula and CA-14
Indivisible 36	Indivisible Sonoma County
Indivisible 41	Indivisible South Bay LA
Indivisible Auburn CA	Indivisible Stanislaus
Indivisible Beach Cities	Indivisible Suffragists
Indivisible CA-3	Indivisible Ventura
Indivisible CA-7	Indivisible Windsor
Indivisible CA-25 Simi Valley-Porter Ranch	Indivisible Yolo
Indivisible CA-29	Indivisible: San Diego Central
Indivisible CA-33	Indivisibles of Sherman Oaks
Indivisible CA-37	Livermore Indivisible
Indivisible CA-39	Mill Valley Community Action Network
Indivisible CA-43	Mountain Progressives
Indivisible Claremont/Inland Valley	Nothing Rhymes with Orange
Indivisible Colusa County	Orchard City Indivisible
Indivisible East Bay	Orinda Progressive Action Alliance
Indivisible El Dorado Hills	Our Revolution Long Beach
Indivisible Elmwood	RiseUp
Indivisible Euclid	Rooted in Resistance
Indivisible Lorin	San Diego Indivisible Downtown
Indivisible Los Angeles	SFV Indivisible
Indivisible Manteca	Tehama Indivisible
Indivisible Marin	The Resistance Northridge
Indivisible Media City Burbank	Together We Will Contra Costa
Indivisible Mendocino	TWW/Indivisible - Los Gatos
Indivisible Normal Heights	Vallejo-Benicia Indivisible
Indivisible North Oakland Resistance	Venice Resistance
Indivisible North San Diego County	Women's Alliance Los Angeles
	Yalla Indivisible
	2 Individuals

Opposition:

2 Individuals

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