
SENATE COMMITTEE ON APPROPRIATIONS

Senator Anthony Portantino, Chair
2021 - 2022 Regular Session

SB 834 (Wiener) - Tax-exempt status: insurrection

Version: May 2, 2022

Policy Vote: GOV. & F. 4 - 0, PUB. S. 4 - 0

Urgency: No

Mandate: No

Hearing Date: May 9, 2022

Consultant: Robert Ingenito

Bill Summary: SB 834 would allow the Attorney General (AG) and Franchise Tax Board (FTB) to determine that an organization is no longer eligible for tax-exempt status if it has engaged in acts of criminal conspiracy, as specified.

Fiscal Impact:

- The Department of Justice (DOJ) indicates that it would incur first-year costs of \$719,000, and about \$1 million annually thereafter, to implement the provisions of the bill (General Fund).
- FTB would incur minor and absorbable administrative costs.
- FTB further notes that the bill could result in an unknown revenue increase, as revoked nonprofits would (1) become subject to corporate income and franchise tax provisions, and (2) be taxed at the applicable corporate tax rate. FTB estimates that each additional \$1 million dollars of taxable income resulting from the revocation of tax-exempt status would result in a General Fund revenue gain of \$90,000.

Background: 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 Internal Revenue Service (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 regulation 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 purposes. 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).

Proposed Law: This bill would, among other things, do the following:

- Authorize the AG to make a finding that a tax-exempt organization has actively engaged in, or incited the active engagement in, acts or conspiracies defined as criminal under specified federal law, and likely to produce imminent violation of that federal law.

- Require the Attorney General to notify FTB of such a finding, and require the existing authority FTB to revoke the tax-exempt status of the organization found to be in violation.
- Provide that FTB's authority to revoke an exemption from tax, as specified, does not constitute a change in, but is declaratory of, existing law.

Staff Comments: According to DOJ, the Charitable Trusts Section within its Public Rights Division would be responsible for the bill's enforcement. Cost divers would include: (1) investigation of charities alleged to be involved in the January 6, 2021 insurrection and other attempts to overthrow the government, (2) sending audit letters and subpoenas, (3) reviewing responsive record, (4) subpoenaing bank records, (5) interviewing witnesses and victims, (6) preparing settlement or enforcement actions, (7) engaging in litigation and enforcement actions, and (8) responding to discover and Public Records Act requests. DOJ anticipates that this workload would require one deputy attorney general, one investigative auditor, and one legal secretary. In addition, annual resources for consultants, legal experts and witnesses would be required.

Moreover, DOJ's California Justice Information Services Division (CJIS) anticipates an increased amount of investigatory work that would require it to perform public internet research into these organizations, as well as deep and dark web investigations. DOJ indicates that such workload would require very innovative and time-consuming methods in order to infiltrate and capture information as evidence. Ongoing costs would include one information technology specialist, \$15,000 in annual travel, and \$40,000 in one-time specialized training. Finally, the bill would result increased costs to CJIS of \$150,000 one-time for IT hardware/software/storage, and \$50,000 annually thereafter for support and maintenance.

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