

Trade Associations/Business Leagues: Lobbying Activities and its Reporting Requirements



ARTICLE 07.20.22 BRYAN PAUTSCH, ALEX BRAMER

Trade associations and business leagues that are tax-exempt under Internal Revenue Code Section 501(c)(6) are allowed unlimited lobbying. In fact, many of these organizations have a significant amount of legislative and executive advocacy activities and expenditures. However, trade associations and business leagues must follow certain IRS rules and regulations.

Generally, membership dues associated with trade associations and business leagues are deductible as an ordinary and necessary business expense. However, when these organizations are involved with lobbying activity, a portion of the dues attributable to lobbying expenditures may not be deductible. The remainder of this article will discuss these rules and its exceptions.

First, let's explore the definition of lobbying. For purposes of determining the nondeductibility of dues, lobbying is generally defined as expenditures paid or incurred for the purposes of attempting to influence legislation:

- Through communication, any member or employee of a federal or state legislative or any federal or state employee who may participate in the formation of legislation;
- Through grassroots lobbying communication, which is any attempt to affect or influence the opinions of the general public or any part of the general public.

Note: Engaging in nonpartisan analysis, study or research and making its results available to the general public or segment thereof is not lobbying.

If you have engaged with an outside lobbyist firm, the outside firm can assist you in determining the amount of lobbying expenditures. Any reasonable method may be used to calculate the amount spent on lobbying. Time spent by employees on lobbying, along with an allocation of overhead, are included in lobbying expenditures, including any out-of-pocket costs such as travel and payments to lobbyists. However, if a person's time spent lobbying is less than 5% of their total time and, there is no direct contact lobbying, the organization may treat that person's time spent on lobbying activities as zero.

Trade associations and business leagues must report their lobbying activity and the amount of the dues that are allocable to their lobbying expenditures on their Form 990 Schedule C Part III. Part III-A provides the exceptions to the general rule that a portion of the dues paid to a trade association or business league will be nondeductible for the organization lobbying expenditures. These types of dues will be fully deductible if:

- Line 1 – Substantially all (90% or more) of the dues received by the trade association/business league were paid by certain tax-exempt organizations; OR
- Line 2 – The trade association or business league made only in-house lobbying expenditures of \$2,000 or less; AND
- Line 3 – (applies to Line 1 and Line 2 above) The trade association or business league did not agree to carry any lobbying or political activity expenditures from a prior year

Form 990 Schedule C Part III-B provides for the Dues Notice, Reporting Requirements and Proxy Tax. The organization that answers “No” to both in Line 1 and Line 2 above are subject to the general rule that a portion of the dues paid by the members are nondeductible. These organizations must decide whether to notify its members of the nondeductible portion of their dues or pay the proxy tax themselves. Notification can be rather simple and is usually on the annual dues notices.

The notification is an estimate, generally a percentage, of the dues the organization believes will be spent on lobbying and political activities. Disclosure amounts are estimates based upon the organization's budget for the next dues period. The amount reported to members and the amount expended are rarely the same. Further, to avoid the proxy tax on any lobbying expenditures that exceeded what was budgeted and reported to members on the last dues statement, the organization must also include the amount by which Line 2c (current year estimated lobbying expenditures plus the excess lobbying expenditures from the prior year) exceeds the amount on Line 3 in its nondeductible dues calculation for the following year.

If the member organization elects to disclose rather than pay the proxy tax, the amount the organization agrees to carry over to the following year should be entered on Part III-B, Line 4. Note that the difference between Line 2c and Line 3 may be negative, which simply means less was spent on lobbying activities than was budgeted or reported to members. This amount, whether positive or negative, is “trued up” with the dues notices in the following year. The result is an increase or decrease in the amount the organization will notify its members they may deduct on their respective income tax returns.

The alternative option for the organization is to pay the proxy tax. The proxy tax is at the highest corporate tax rate, currently 21 percent. This area can be complex, please contact your tax advisor with any questions.