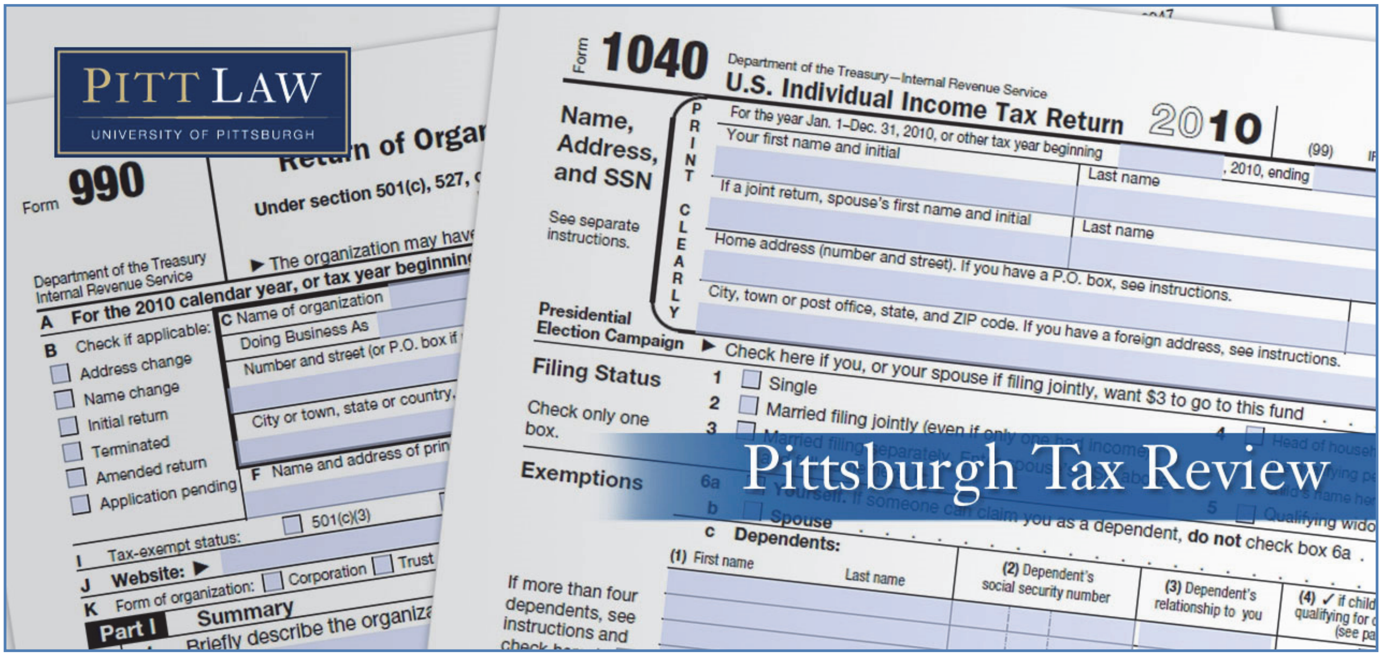

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THE PRIVATE FOUNDATION EXCISE TAX ON SELF-DEALING: CONTOURS, COMPARISONS, AND CHARACTER

*Ellen P. April*l

THE PRIVATE FOUNDATION EXCISE TAX ON SELF-DEALING: CONTOURS, COMPARISONS, AND CHARACTER

Ellen P. Aprill[*]

I. Introduction

In 2014, I published a paper comparing federal self-dealing tax provisions to state law provisions and recommending a procedure permitting pre-approval of beneficial self-dealing transactions by private foundations like that available for transactions between certain insiders and qualified pension plans.[1] Those suggestions, like much academic work, went nowhere. In this piece, I return to consideration of § 4941 of the Internal Revenue Code ("Code"), the excise tax on self-dealing by private foundations, on the occasion of its fiftieth anniversary with hope, but not expectation, that its recommendations will find some traction.

The rules for § 4941 have not changed, but legal developments regarding self-dealing by public charities, particularly supporting organizations and donor-advised funds ("DAFs"), as well as enforcement data provide an updated lens for evaluating § 4941. Part I gives background on § 4941, the excise tax on private foundation self-dealing. Part II compares its rules to the parallel ones applicable to public charities. Both Part I and II, as well as tables in the Appendix to this piece, include Statistics of Income ("SOI") data[2] important to consideration of these excise taxes.

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[*] John E. Anderson Professor of Tax Law, LMU's Loyola Law School. The author thanks Leslie Book, Roger Colinvaux, Philip Hackney, Sanford Holo, Erik Jensen, Stephen Schwarz and participants in both the October 2019 National Center for Philanthropy and Law conference, "Reconsidering Private Foundations after Five Decades: Lessons for the Future" and the *Pittsburgh Tax Review* symposium, "The 1969 Tax Act and Charities: Fifty Years Later," for comments on earlier drafts.

[1] *See generally* Ellen P. Aprill, *Reconciling Nonprofit Self-Dealing Rules*, 48 ABA Real Prop., Tr. & Est. L.J. 411 (2014). Parts I and II *infra* rely heavily on this earlier piece.

[2] *See infra* Tables A and B (giving SOI and other IRS data on § 4941 and § 4958 from 2003 to 2015).

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The fiftieth anniversary of the private foundation excises taxes is also an appropriate time to confront two foundational questions. I do so in Part III. Part III first asks whether we can view the private foundation taxes in general and § 4941 in particular as constitutional exercises of Congress's taxing power under the tests announced in *National Federation of Independent Businesses v. Sibelius*.[3] Second, it considers whether we should characterize the § 4941 excise tax as a Pigouvian tax—a hot category among economists but less familiar to lawyers. It answers "maybe not" to the first and "yes but" to the second.

Inconsistent congressional treatment of self-dealing by § 501(c)(3) organizations and the low level of enforcement lead me to question the effectiveness of our current self-dealing rules. Thus, this examination concludes by suggesting a number of possible changes to the excise taxes applicable to tax-exempt organizations. They range from a relatively small change, expanding abatement rules, to a very large one, considering approaches outside of the Internal Revenue Service ("IRS" or "Service") for regulating the sector.

II. BACKGROUND OF § 4941

A. Summary of § 4941

Since the Tax Reform Act of 1969, § 4941 of the Code has, as a practical matter, forbidden almost all self-dealing, direct or indirect, between a disqualified person and a private foundation.[4] Under this provision, it does not matter whether the transaction results in a "benefit or a detriment to the private foundation."[5] The Code lists five broad categories of self-dealing transactions: (1) sale or exchange, or leasing of property; (2) lending of money or other extension of credit; (3) furnishing of goods, services or facilities; (4) payment of compensation (or payment or reimbursement of

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[3] *See* Nat'l Fed'n of Indep. Bus. v. Sebelius, 567 U.S. 519 (2012).

[4] *See generally* I.R.S., *IRC 4941—The Nature of Self-Dealing*, *in* EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION (CPE) TECHNICAL INSTRUCTION PROGRAM FOR FISCAL YEAR 1985 (1985), https://www.irs.gov/pub/irs-tege/eotopicq85.pdf.

[5] Treas. Reg. § 53.4941(d)-1(a) (as amended in 1973). Private foundation excise taxes, including § 4941, generally also apply to split-interest trusts. *See* I.R.C. § 4947. I do not here discuss split-interest trusts separately.

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expenses); and (5) transfer or use of the income or assets of the private foundation.[6] Importantly, the prohibition on self-dealing does not apply to the payment of reasonable compensation to a disqualified person for reasonable and necessary personal services.[7]

For purposes of the self-dealing rules of § 4941, the category of disqualified persons reaches broadly. The term includes a "substantial contributor"; a "foundation manager"; a more than 20% owner of a business entity that is a substantial contributor; a member of the family; corporations, partnerships, trusts, or estates in which any of the foregoing (as a group) have a greater than 35% ownership interest; and a government official.[8]

The initial tax on the self-dealer is 10% of the "amount involved" with respect to the act of self-dealing for each year or part of a year in the taxable period.[9] The initial tax on a foundation manager who knowingly engages in the act for each year (or part thereof) is 5% of the amount involved up to a maximum of $20,000.[10] The "amount involved" is the greater of the amount of money and the fair market value of the other property given or the amount

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[6] I.R.C. § 4941(d)(1)(A)–(E). Some categories, particularly "use of the income or assets," are inherently ambiguous. Moreover, self-dealing includes both direct and indirect transactions, and the reach of "indirect" is uncertain. *See infra* note 173. Section 4941 also includes a separate category for payment of money or other property to a government official. *See* I.R.C. § 4941(d)(1)(F).

[7] *See* I.R.C. § 4941(d)(2)(E). Examples of personal services in the applicable regulations include brokerage, legal, investment counseling, and general banking services. *See* Treas. Reg. § 53.4941(d)-3(c) (as amended in 1984). Under this exception, members of a family that control a private foundation can receive compensation from the private foundation. Many believe that this personal services exception permits abuses. Thus, in her contribution to this symposium, *The Five Percent Fig Leaf*, Ray Madoff suggests that salaries and travel for family members, among other administrative expenses, not count toward satisfying the § 4942 payout requirement. Ray Madoff, *The Five Percent Fig Leaf*, 17 PITT. TAX REV. 341 (2020).

[8] I.R.C. § 4946(a). Some proposals for change have also recently surfaced. For example, some believe that, in light of the growth of private related investments and mission related investments, the 20% and 35% limitations be lowered. *EO Tax Journal* 2019-173 (Sept. 5, 2019) (on file with author).

[9] I.R.C. § 4941(a)(1).

[10] *Id.* § 4941(a)(2), (c)(2). Foundation managers, including directors, can generally avoid liability for self-dealing transactions if they base their determination that an act was not self-dealing upon "a reasoned, written opinion legal opinion," or if they have exercised "responsibility on behalf of the foundation with ordinary business care and prudence." Treas. Reg. § 53.4941(a)-1(b)(5), (6).

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of money and the fair market value of the other property received, valued as of the date of the act of self-dealing.[11]

The self-dealing transaction must be corrected to avoid the second-tier taxes of 200% of the amount involved for the self-dealer and of 50% of the amount involved for a foundation manager who refuses to agree to all or part of the correction of the amount involved up to a maximum of $20,000.[12] "Amount involved" means the greater of the amount of money paid or the highest fair market value during the taxable period.[13] The statute defines correction as "undoing the transaction to the extent possible, but in any case placing the private foundation in a financial position not worse than that in which it would be if the disqualified person were dealing under the highest fiduciary standards."[14] As a leading textbook explains, the regulations "provide amplification, essentially imposing a restitution plus profits (if any) requirement."[15]

The structure of the private foundation two-tier excise taxes, including § 4941, took shape in the Tax Reform Act of 1969. From 1969 forward, private foundations could engage in no self-dealing with disqualified persons, other than limited exceptions, without imposition of onerous excise taxes. Despite a detailed Treasury study that preceded adoption of these rules, there is much controversy as to whether the 1969 rules were adopted on the basis of animus, anecdote, or evidence.[16] In any case, this set of rules followed attempts to take another approach, an approach similar to that we have adopted for most public charities today.

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[11] I.R.C. § 4941(e)(2). The taxable period begins with the act of self-dealing and ends on the earliest of (1) the date of mailing of an IRS deficiency notice (2) the date on which the first-level tax is assessed, or (3) the date on which the act of self-dealing is fully corrected. *Id.* § 4941(e)(1).

[12] *Id.* § 4941(b), (c)(2).

[13] *Id.* § 4941(e)(2).

[14] *Id.* § 4941(e)(3).

[15] Fishman et al., Nonprofit Organizations: Cases and Materials 711 (5th ed. 2015) (citing Treas. Reg. § 53.4941(e)-1(c)).

[16] *See* James J. Fishman, *The Private Foundation Rules at Fifty: How Did We Get Them and Do They Meet Current Needs?*, 17 Pitt. Tax Rev. 247 (2020).

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B. History of § 4941

A long history of congressional examination preceded the Tax Reform Act of 1969.[17] The Revenue Act of 1950[18] introduced a category of "prohibited transactions" between organizations that today we call private foundations and their creators and substantial contributors, members of their families, and entities controlled by them.[19] The restrictions were limited to private foundations, although not referred to as such, because churches, schools, hospitals, and charities supported by contributions from the public were not subject to them.[20] The 1950 private foundation rules closely resembled the current rules under § 4958 for public charities. Self-dealing transactions were not forbidden, but they could not harm the organization.

At the beginning of 1964, after many years of controversial hearings,[21] the Senate Finance Committee and the House Ways and Means Committee asked the Treasury Department to study and report on possible tax abuses by what are now private foundations.[22] In preparing its report, the Treasury conducted a special canvass of approximately 1,300 foundations.[23] Although by and large the *Treasury Report* praised foundations and their role in American society,[24] the *Treasury Report* described six areas of concern.[25] Self-dealing was key.[26] The *Treasury Report* found the 1950 self-dealing

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[17] MARION R. FREMONT-SMITH, FOUNDATIONS AND GOVERNMENT 159–61 (1965).

[18] *See* Revenue Act of 1950, Pub. L. No. 81–814, 64 Stat. 906, 947.

[19] I.R.C. of 1954, §§ 503–04.

[20] *Id.* I.R.C. § 503(b) (1954).

[21] *See* FREMONT-SMITH, *supra* note 17, at 180.

[22] S. COMM. ON FIN., 89TH CONG., TREASURY DEPARTMENT REPORT ON PRIVATE FOUNDATIONS 1 (Comm. Print 1965) [hereinafter TREASURY REPORT].

[23] Foundations were chosen from information from the Internal Revenue Service and the Foundation Library Center as well as other sources. The study used a stratified sampling designed to produce the 1,300 samples of Form 990-A for 1962. It included, however, 100% of foundations of over $10,000,000. Smaller percentages were obtained of smaller foundations. *Id.* at 77.

[24] According to the TREASURY REPORT, private foundations "constitute a powerful instrument for evolution, growth, and improvement in the shape and direction of charity." *Id.* at 5.

[25] *Id.* at 5–10.

[26] The other areas identified as problematic were foundation involvement in business, and family use of foundations to control corporate and other property, delay in benefit to charity, financial

rules, which relied on such inherently ambiguous terms as "substantial," "adequate," and "reasonable," were unsatisfying and unworkable. They left too much discretion to donors as to what is reasonable and requiring too much expensive effort by the IRS to administer such a vague standard.[27] The *Treasury Report* recommended an absolute ban on self-dealing.[28]

As Fremont-Smith has discussed, the *Treasury Report* did not propose any sanctions for violations.[29] The *Treasury Report* simply observed in a footnote that the sanction of current law—denial of exemption—would have to be scrutinized carefully to determine its adequacy for securing adherence to the new rules.[30] In 2000, Thomas Troyer, who helped draft the *Treasury Report*, recalled, "Treasury worked extensively with the Joint Committee staff between 1965 and 1969 to devise appropriate sanctions, and by the Spring of 1969 the present enforcement regime for the Chapter 42 rules had been developed."[31]

In 1969, the new Nixon administration, at the request of the tax-writing committees, recommended that Congress act on the *Treasury Report*. The Committee on Ways and Means held four days of hearings. The House hearings ended on April 25, 1969, and the Tax Reform Act of 1969 was introduced on August 1, 1969. Along with establishing the private foundation excise taxes, it formally defined private foundations, differentiated treatment of public charities and private foundations, and gave the IRS additional tools regarding information from private foundations and public charities. The

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transactions unrelated to charitable functions, and broadening of foundation management. Self-dealing and these other categories often overlap.

[27] *Id.* at 18.

[28] As others have noted, the TREASURY REPORT "provides a fuller and more accurate statement of the purposes and intent" of the 1969 private foundation excise tax rules than do than the official committee reports, which "are little more than executive summaries of the more detailed consideration of the germane topics provided four years earlier by Treasury." Richard Schmalbeck, *Reconsidering Private Foundation Investment Limitations*, 58 TAX. L. REV. 59, 68 (2004).

[29] Fremont-Smith also notes that the year studied, 1962, might not be typical and that the TREASURY REPORT never gives the extent of abuse by citing the amount of assets under examination. FREMONT-SMITH, *supra* note 17, at 378.

[30] TREASURY REPORT, *supra* note 22, at 3.

[31] Thomas A. Troyer, *The 1969 Private Foundation Law: Historical Perspectives on Its Origin and Underpinnings*, 27 EXEMPT ORG. TAX REV. 52, 58 (2000).

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House bill defined § 4941 in terms we know it today, although with an initial tax of 5% per year on a self-dealer until correction and a 2.5% tax on a knowing foundation manager, limited to $10,000. A 1983 Joint Committee Report stated that the excise tax regime of the 1969 Act was "substituted for the principal penalties imposed under prior law for foundation misuse, i.e., loss of the foundation's exempt status and its eligibility to receive the deductible contributions. In the case of relatively minor abuses, the prior-law penalties seemed unduly harsh" and "resulted in extensive litigation."[32]

The Conference Committee working on the Tax Reform Act of 1969 completed its work on December 23, 1969. The Joint Committee explained the basis for the self-dealing rules as follows:

> To minimize the need to apply subjective arm's length standards, to avoid the temptation to misuse private foundations for noncharitable purposes, to provide a more rational relationship between sanctions and improper acts, and to make it more practical to properly enforce the law, the Act generally prohibits self-dealing transactions and provides a variety and graduation of sanctions. . . . This is based on the belief by Congress that the highest fiduciary standards require complete elimination of all self-dealing rather than arm's length standards.[33]

Thus, the Tax Reform Act of 1969 established a two-tier excise tax on self-dealing transactions between disqualified persons and private foundations for the same categories we have today. The taxes were imposed at the rates found in the House bill—a first level tax on self-dealers of 5% on the amount of the self-dealing from the date of the transaction for each year or part of a taxable year for the taxable period and a second tier tax of 200% if the transaction was not corrected within ninety days of the mailing of a deficiency tax.[34] For knowing managers, the first level tax was 2.5% with a maximum of $10,000 and the second-tier tax 50% was up to $10,000 if the

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[32] STAFF OF JOINT COMM. ON TAXATION, JCS-31-83, DESCRIPTION OF INCOME TAX PROVISIONS RELATING TO PRIVATE FOUNDATIONS, SCHEDULED FOR HEARINGS BEFORE THE SUBCOMMITTEE ON OVERSIGHT OF THE COMMITTEE ON WAYS AND MEANS, JUNE 27, 28 and 30, at 6 (1983).

[33] *Id.* at 15–16.

[34] STAFF OF JOINT COMM. ON TAXATION, JCS-16-70, GENERAL EXPLANATION OF THE TAX REFORM ACT OF 1969, at 33–34 (Comm. Print. 1970).

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manager refused to correct the transaction.[35] The self-dealing tax was to be imposed regardless of fault.[36]

These rules were adopted against a background of criticism of the Treasury for its lackadaisical oversight of private foundations. The Treasury responded, and the strict liability of the self-dealing rules and the initial two-tier excise tax levels were enacted in the context of high levels of audit. The *Treasury Report* stated that audits of § 501(c)(3) organizations had increased from approximately 2,000 in the 1950s to over 10,000 in fiscal year 1964.[37] Moreover, "[a]fter the Tax Reform Act of 1969, the IRS established a program of auditing all private foundations at least once every five years, with the largest and most complex being audited once every two years."[38]

Relatively few changes have been made to the self-dealing rules since then. In 1984, Congress enacted § 4962, which permitted abatement of first-level private foundation excise taxes "if the taxable event was due to reasonable cause and not to willful neglect" and "corrective action is accomplished within the appropriate correction period."[39] As the then-President of the Council on Foundations testified at a congressional hearing, "[b]ecause of the complexity of the private foundation rules and the inability of many foundations—particularly smaller foundations—to obtain sophisticated legal counsel, inadvertent violation of these rules do occasionally occur."[40] What is important for our purposes is that Congress did not extend this relief to acts of self-dealing, where the penalty tax is payable by self-dealers and knowing managers but not by the private foundation itself. According to a 1992 EO CPE text, Congress excluded

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[35] *Id.*

[36] *Id.* at 34.

[37] TREASURY REPORT, *supra* note 22, at 109.

[38] Henry Hansmann, *Reforming Nonprofit Corporation Law*, 129 U. PENN. L. REV. 497, 602 n.335 (1981) (citing *Private Foundations: Hearings on the Role of Private Foundations in Today's Society and a Review of the Impact of Charitable Provisions of the Tax Reform Act of 1969 on the Support and Operation of Private Foundations Before the Subcomm. on Foundations of the Senate Comm. on Finance*, 93d Cong., 1113 (1974) (background paper submitted by Donald C. Alexander, former Commissioner of the IRS).

[39] I.R.C. § 4962(a).

[40] *Hearings before the Subcomm. on Oversight of the Comm. on Ways and Means*, H.R., 98th Cong. 1st Sess., Part I. Serial 98-32, 154 (statement of James A. Joseph, President, Council on Found.).

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§ 4941 "because the underlying reason for abatement is the preservation of assets for charitable purposes. Congress did not believe there was any justification for abatement on the self-dealer, because charity does not suffer if the self-dealer pays, and because current law generally prohibits commercial transactions between disqualified persons and foundations."[41]

Significantly, as part of the Pension Protection Act of 2006, the rate for exempt organization excise taxes, including that for private foundation self-dealing, was doubled. In the case of § 4941, the initial tax went from 5% to 10% for self-dealers and from 2.5% to 5% for managers. The maximum for managers was increased from $10,000 to $20,000.[42] The Senate Finance Committee explained these changes as follows:

> In the years following passage of the 1969 Act, the IRS closely monitored the conduct of private foundations, and in 1990 the Treasury Department concluded that foundations were largely a compliant sector. In subsequent years, however, audits of foundations and other section 501(c)(3) organizations generally has fallen significantly. With a decreased enforcement presence, there is an increased likelihood that private foundations are not as compliant as reported by the Treasury Department in 1990 and that the current excise tax rates, which have not increased in 35 years, are not providing a sufficient deterrent. Thus, the Committee believes that it is appropriate to double the initial taxes and the dollar amount limitations on foundation manager liability.[43]

This explanation to some extent represents revisionist history. While compliance with the tax laws is always important, the legislative history of the 1969 Tax Reform Act had emphasized proportionality and administrability more than deterrence.

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[41] Thomas Miller et al., *Abatement and Waivers*, *in* EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION (CPE) TECHNICAL INSTRUCTION PROGRAM FOR FISCAL YEAR 1992 (1992), https://www.irs.gov/pub/irs-tege/eotopicf92.pdf.

[42] Pension Protection Act of 2006, Pub. L. No. 109–280, § 1212(a)(1)(A)–(B), (a)(2), 120 Stat. 780, 1074.

[43] Senate Finance Committee, Report on Telephone Excise Tax Repeal and Taxpayer Protection and Assistance Act of 2006 (footnotes omitted), 2006 TNT 180-67 (Sept. 18, 2006). The increases in the first level of excise taxes for self-dealing become part of the Pension Protection Act of 2006, P.L. 109-208, § 1212(a)(1)(A)–(B).

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C. Experience under § 4941

Many believe the private foundation excise tax rules, including those on self-dealing, have achieved their purpose. As one scholar of the private foundation excise taxes, Professor Richard Schmalbeck, has written, "In the view of many in the field . . . the 1969 private foundations rules, taken as a whole, should be counted among the more successful tax reform efforts of the latter half of the 20th century . . . The Act seems to have been effective in removing most of those abusive practices from the private foundation landscape."[44] Similarly, in 1989 James Joseph, then of the Council on Foundations, testified before the House Committee on Ways and Means that "the rules are working well, and have proven to be beneficial."[45]

To evaluate a policy, however, we need to go beyond general impressions to data when possible. According to the 1965 *Treasury Report*, 0.9% of foundations reported on their Form 990-A borrowing from what today would be disqualified person, 1.4% receipt of personal services, 0.2% availability of assets or services, and 1.4% the purchasing of securities or other property.[46] Today, these all would be self-dealing transactions, but at the time, many may have been permissible as arm's-length transactions. The *Treasury Report* recognized, however, that other self-dealing transactions may have gone unreported because of fear of IRS enforcement action.

> Private foundation excise taxes are now reported on Form 4720.[47] In addition, Part VII-B of the Return of Private Foundation, Form 990-PF, includes "Statements Regarding Activities for Which Form 4720 May Be Required."[48] The instructions to Part VII-B of the Form 990-PF state that, if the answer to any question in the part is yes, the foundation must

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[44] *See* Schmalbeck, *supra* note 28, at 62.

[45] Tax Analysts, *IRS Executive Task Force Releases Penalty Reform Proposals*, 89 TNT 45-36 (Feb. 27, 1989).

[46] The TREASURY REPORT breaks these numbers down further by size of foundation and percentage of donor influence.

[47] *See I.R.S. Form 4720, Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code* (Dec. 2019), https://www.irs.gov/pub/irs-pdf/f4720.pdf.

[48] *I.R.S. Form 990-PF: Return of Private Foundations* (Dec. 2019), https://www.irs.gov/pub/irs-pdf/f990pf.pdf.

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"complete and file Form 4720 unless an exception applies."[49] Questions 1(a)(1-6), 1(b), and 1(c) of Section A, Part I of Form 4720 relate to § 4941.[50] They ask separately whether the reporting private foundation engaged in each category of self-dealing.

Until recently, the IRS Statistics of Income (SOI) collected data regarding Forms 4720 filed in connection with violations of § 4941. These SOI data permit some comparison of the 1965 numbers to the situation today. In 2015, the most recent year for which information as to both the amount of excise tax and the number of private foundations is available, 239 Forms 4720 were filed reporting tax on self-dealing with taxes of $2,086,082, or a mean of $8,728 per form.[51] For the same year, SOI puts the total number of 990-PFs filed at 99,683.[52] Assuming that there is only one form per foundation,[53] the percentage of foundations engaging in prohibited self-dealing transactions is approximately 0.24%. For the years for which SOI data are available, the largest percent of private foundations involved in self-dealing transactions, again using assumptions that give a higher percentage than is in fact likely, is 0.29% in 2009, where the mean reported per form is $11,866.[54]

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49 *I.R.S. Instructions to I.R.S. Form 990-PF: Return of Private Foundations* (Dec. 2019), https://www.irs.gov/pub/irs-pdf/i990pf.pdf.

50 *See supra* note 47.

51 I.R.S., *SOI Tax Statistics—Domestic Private Foundation and Charitable Trust Statistics: Excise Taxes Reported by Charities, Private Foundations, and Split-Interest Trusts on Form 4720, Calendar Year 2015* (last visited June 26, 2020) [hereinafter *SOI Tax Statistics*], https://www.irs.gov/statistics/soi-tax-stats-domestic-private-foundation-and-charitable-trust-statistics. The most recent data are from 2015. SOI information for 2016 and 2017 do not include this category. The IRS SOI is no longer collecting data from individuals filing Form 4720. June 15, 2019 email from Emily Gross of SOI (on file with author). Unlike the other private foundation excise taxes, § 4941 imposed the tax on the self-dealer, not the private foundation. Thus Forms 4720 related to self-dealing are not filed by the private foundation itself, but by disqualified persons, usually individuals. Table A attached to this article gives SOI data on Forms 4720 filed in connection with violations of § 4941 from 2003–2015.

52 *Id.*

53 This assumption is a simplifying one and is not likely accurate; several disqualified persons and knowing managers may be involved in one transaction. The same transaction may result in liability over several years. The assumption used gives a larger percentage of foundations engaged in prohibited self-dealing transactions than would a perhaps more realistic assumption.

54 I.R.S., *SOI Tax Statistics—Domestic Private Foundation and Charitable Trust Statistics: Excise Taxes Reported by Charities, Private Foundations, and Split-Interest Trusts on Form 4720, Calendar*

At least to some extent, the existence of § 4941 appears to have an *in terrorem* effect and to succeed in preventing self-dealing transactions. These numbers, however, do not ineluctably lead to the conclusion that § 4941 is working well. According to the IRS Data Book for Fiscal Year 2015,[55] a total of 119 returns from Forms 990-PF, 1041-A, 1120-Pol, and 5227 were examined.[56] With SOI reporting the number of private foundations for that year as 99,683, the percentage of private foundations examined would be only .12%. As discussed *infra*, a comparison of data from a survey of public charities and the number of Forms 4720 filed for intermediate sanction violations under § 4958 suggests that many such self-dealing transactions go unreported. I would expect the same for § 4941 violations. In fact, as Professor Mayer has pointed out, a 2012 project focusing on large private foundations resulted in additional taxes or penalties in almost half of the closed examinations."[57]

Indeed, some practitioners have told me that reporting § 4941 transactions on Form 990 and filing Form 4720 are seen as voluntary, often filed only when media report on the self-dealing. Thus, even some large foundations may well fail to report self-dealing transactions on Form 990-PF, and, in turn, their disqualified persons fail to file the Form 4720. Such failures seem all the more likely for small foundations, those with assets under $1 million in assets and which constitute the majority of reporting foundations.[58] As Professor Fishman writes in his contribution to this

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Year 2009 (last visited June 26, 2020), https://www.irs.gov/statistics/soi-tax-stats-domestic-private-foundation-and-charitable-trust-statistics; U.S. DEP'T OF THE TREAS., INTERNAL REV. SERV., *SOI Tax Statistics—Domestic Private Foundation and Charitable Trust Statistics: Domestic Private Foundations: Number and Selected Financial Data, by Type of Foundation and Size of Fair Market Value of Total Assets, Tax Year 2009* (last visited June 26, 2020), https://www.irs.gov/statistics/soi-tax-stats-domestic-private-foundation-and-charitable-trust-statistics.

[55] I.R.S. DATA BOOK FISCAL YEAR 2015, at 34 tbl.13 (2015), https://www.irs.gov/pub/irs-soi/15databk.pdf.

[56] *Id.* Of course, the number of private foundations examined does not correspond precisely to self-dealing transactions, because the self-dealing excise tax falls on individuals and not entities. Moreover, examinations reported may involve several years of the same entity. But these numbers, I believe, give a rough estimate of the level of IRS scrutiny of private foundations.

[57] Lloyd Hitoshi Mayer, *"The Better Part of Valour is Discretion": Should the IRS Change or Surrender Its Oversight of Tax-Exempt Organizations*, 7 COLUM. J. TAX L. 80, 95–96 (2016).

[58] Fishman, *supra* note 16, at 287.

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symposium, "small foundations . . . are essentially unregulated because of the Internal Revenue Service's lack of resources or interest."[59]

Furthermore, available data do not address the harm of forbidding even beneficial transactions in order to apply an objective standard.[60] In addition, as discussed below in Part II, provisions applicable to public charities enacted more recently than § 4941 suggest Congressional uncertainty about the objective approach of § 4941.

III. Comparison to the Excise Tax on Excess Benefit Transactions

A. Summary and History of § 4958

The § 4958 intermediate sanction rules Congress adopted in 1996 for public charities and social welfare organizations offer important comparisons to the self-dealing rules of § 4941. They resemble the private foundation rules in many ways. However, unlike § 4941, they permit self-dealing transactions if certain substantive or procedural requirements are met.[61] Perhaps most strikingly, the § 4958 rules adopt the subjective approach abandoned and criticized when § 4941 was enacted.

Prior to adoption of the intermediate sanction rules, the extreme nature of the sanction for inurement (private benefit by insiders)—revocation of exemption—and the uncertainty as to the term's meaning posed challenges for the IRS. As Margaret Richardson, then Commissioner of the Service, testified in 1993 during consideration of intermediate sanctions,

> the lack of a sanction short of revocation of exemption in cases in which an organization violates the inurement standard or one of the other standards for exemption causes the Service significant enforcement difficulties. Revocation of

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[59] *See id.* at 247.

[60] In 2002, the ABA Section of Taxation suggested as one reform option an arm's-length standard for transaction that could clearly be shown to be beneficial to the private foundation and retention of the bright line prohibition for those that could not. *See* Tax Analysts, *ABA Responds to Request for Comments on Excise Taxes Imposed on Foundation and Organization Managers*, 2002 TNT 200-41, at 260 (Oct. 16, 2002).

[61] Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1311(a), 110 Stat. 1452, 1475 (1996) (codified at I.R.C. § 4958).

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> an exemption is a severe sanction that may be greatly disproportional to the violation in issue.[62]

That is, the desire to craft a proportional penalty in large measure prompted the provisions of § 4958; Congress sought a more modest penalty that could be applied in lieu of revocation.

In drafting § 4958, Congress looked to the private foundation rules and adopted an approach that in many ways resemble them. Like the private foundation taxes, intermediate sanctions involve a two-tier excise tax[63] and define the disqualified persons and knowing managers subject to these taxes. Also, like the private foundation taxes, § 4958 does not impose a direct burden on the organization itself for violation, unless violations become so severe that revocation is appropriate. Both sets of rules permit reasonable compensation for personal services.

But these two sets of rules differ in important ways as well. There is no absolute prohibition on self-dealing for public charities; the intermediate sanction regime imposes an excise tax only if the value of the benefit fails to match the consideration received by the organization.[64] Indeed, when the Senate Finance Committee suggested as one reform option extending to public charities the absolute ban on self-dealing now applicable only to

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[62] SUBCOMM. ON OVERSIGHT, H.R. COMM. ON WAYS AND MEANS, 103RD CONG., REP. ON REFORMS TO IMPROVE THE TAX RULES GOVERNING PUBLIC CHARITIES 6 (Comm. Print 1994) (quoting the prepared statement of Hon. Margaret Milner Richardson, Commissioner of Internal Revenue, delivered to the Committee on June 15, 1993).

[63] Under I.R.C. § 4958, the initial penalty on disqualified persons is 25% of the excess benefit. I.R.C. § 4958(a)(2). If not corrected, the second-tier tax is 200% of the excess benefit. IRC § 4958(b). Knowing and willing managers are subject to a 10% first-tier tax up to a maximum of $20,000. I.R.C. § 4958(a)(2), (d)(2).

[64] Under the intermediate sanction rules, the category of disqualified persons who are subject to tax for engaging in an excess benefit transactions includes "any person who was, at any time during the five-year period [preceding the excess benefit transaction] in a position to exercise substantial influence over the affairs of the organization." I.R.C. § 4958 (f)(1)(A); Treas. Reg. § 53.4958-3(a)(1). The category also includes certain members of the family of a disqualified person and certain controlled entities. I.R.C. § 4958(f); Treas. Reg. § 53.4958-3(b). Officers, directors, trustees are per se disqualified persons. Treas. Reg. § 53.485803(c)(1)–(3). Whether other individuals or entities are disqualified persons because they exercise substantial influence is a matter of facts and circumstances, Treas. Reg. § 53.4958-3(e), with exceptions including whether an individual receives economic benefits less than the amount used to define a highly compensated employee under I.R.C. § 414(q)(1)B)(i). Treas. Reg. § 53.4958-3(d).

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private foundations,[65] nonprofits condemned the idea. For example, the CEO of Independent Sector, an umbrella group of nonprofits, objected, "[p]ublic charities, particularly smaller charities, frequently receive from board members and other disqualified persons goods, services, or the use of property at substantially below market rates."[66] Under intermediate sanctions, only the excess benefit above what is reasonable is subject to tax.

Thus, to a large extent, Congress in the intermediate sanction rules went back to the ambiguity of the pre-1969 standards for self-dealing transactions that the *Treasury Report* so criticized. Establishing what is an excess benefit above the fair market price for § 4958 purposes presents difficulties that § 4941 avoids. Valuation, as tax lawyers know well, is often a difficult and delicate task.[67] By subjecting the entire amount of a self-dealing transaction to the excise tax, the private foundation rule of § 4941 avoids this challenge.

In addition to the difficulty in establishing what is an excess benefit, the rebuttable presumption of reasonableness complicates enforcement.[68] If a public charity: (1) approves the terms of a transaction in advance by a board (or board committee) composed of persons who have no conflict of interest regarding the transaction; (2) prior to making a determination, these disinterested persons obtain and rely upon appropriate comparability data;[69] and (3) the board adequately documents the basis for its determination; the transaction will be presumed not to be an excess benefit transaction and the

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[65] *See* STAFF OF S. FIN. COMM., 108TH CONG., TAX EXEMPT GOVERNANCE PROPOSALS: STAFF DISCUSSION DRAFT 13 (2004) (citing Hansmann, *supra* note 38, at 569–73).

[66] Melanie B. Leslie, *The Wisdom of Crowds? Groupthink and Nonprofit Governance*, 62 FLA. L. REV. 1179, 1217 (2010) (quoting Letter from Diana Aviv, Pres. & CEO, Independent Sector, to Senate Finance Committee, *Comments on Discussion Draft on Reforms to Oversight of Charitable Organizations* 5 (July 16, 2004), https://www.finance.senate.gov/imo/media/doc/Diana%20Aviv.pdf.

[67] *See* Caracci v. CIR, 456 F.3d 444, 447 (5th Cir. 2006) (rejecting in full the IRS valuation that gave rise to self-dealing taxes); *see also* Aprill, *supra* note 1, at 440.

[68] The Treasury regulations established the rebuttable presumption of reasonableness in accordance with the legislative history of I.R.C. § 4958. *See* Failure by Certain Charitable Organizations to Meet Certain Qualification Requirements; Taxes on Excess Benefit Transactions, 63 Fed. Reg. 41486 (proposed Aug. 4, 1998).

[69] Comparable data can include data from for-profit organizations. *See* Treas. Reg. § 53.4958-4(b)(1)(ii).

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IRS will have the burden of proving otherwise.[70] As a result, public charities have a clear process not available to private foundations for essentially negating charges of self-dealing. Professor Jill S. Manny has observed, as a result of the rebuttable presumption, "[u]ltimately the intermediate sanctions provisions are all about process, not substance."[71]

Over the years, some on Capitol Hill have expressed dissatisfaction with § 4958. For example, a discussion draft of proposed reform for tax-exempt organizations prepared by Senate Finance Committee Staff urged application of the private foundation self-dealing rules to public charities.[72] The Joint Committee on Taxation has also recommended abandoning the rebuttable presumption.[73] To date, however, the rules regarding self-dealing by public charities remain unchanged, except for 2006 changes applicable to supporting organizations and DAFs.[74]

B. Experience Under § 4958

Although the intermediate sanction regime has been in place since the end of 1995,[75] its impact remains difficult to gauge. In 2016, on the twentieth anniversary of § 4958, a number of exempt organization experts shared their evaluation of the provision.[76] In general, they agreed that the intermediate sanctions regime "appears to be popular with EO tax practitioners," although

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[70] *See* Treas. Reg. § 53.4958-6. If the burden shifts, the IRS will be required to present "sufficient contrary evidence to rebut the probative value of the evidence put forth by the parties to the transaction." Treas. Reg. § 53.4958-6(b).

[71] Jill S. Manny, *Nonprofit Payments to Insiders and Outsiders: Is the Sky the Limit?*, 76 FORDHAM L. REV. 735, 736 (2007).

[72] *See supra* note 65, at 3–4 (2004). *See also* Marion R. Fremont-Smith, *Is It Time to Treat Private Foundations and Public Charities Alike?*, 52 EXEMPT ORG. TAX REV. 257 (2006).

[73] STAFF OF J. COMM. ON TAXATION, 109TH CONG. OPTIONS TO IMPROVE TAX COMPLIANCE AND REFORM TAX EXPENDITURES 262–64 (Comm. Print 2005).

[74] *See infra* Part II(C).

[75] *See* Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1311(d)(1)–(2), 110 Stat. 1452, 1478 (1996) (stating that the provision, in general, applies to transactions occurring after Sept. 14, 1995).

[76] Fred Stokeld, *Landmark Law on EOs and Excess Benefit Turns 20*, 152 TAX NOTES 915, 915 (Aug. 15, 2016). As noted earlier, the IRS Statistics of Income Division will no longer be reporting aggregate data on Forms 4720 filed in connection with excess benefit transactions. *See* Tax Analysts, *supra* note 45.

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some suggested "expanding the law to cover more categories of EOs" and that "section 4958 had, ironically, led to higher levels of reasonable compensation through the use of compensation comparability data."[77]

SOI data suggest little reporting of § 4958 violations.[78] In 2015, for example, only eleven individuals filed Form 4720 reporting excess benefit transactions with a total tax of $283,739, or a mean reported amount of $2,580.[79] For no year between 2003 and 2015 did the number of applicable tax-exempt organizations likely to be involved in a § 4958 transaction represent even .01% of total applicable exempt organizations.

Enforcement activity is, as we all know, lacking. SOI data reported examination of 2,712 Forms 990 and 990-EZ in Fiscal Year 2018. Even if all examinations related to § 501(c)(3) and § 501(c)(4) organizations, 1.6% of applicable organizations would have been subject to examination.[80]

Other evidence confirms that self-dealing is far more widespread than SOI data indicate. A 2007 study conducted by the Urban Institute's Center on Nonprofit and Philanthropy of more than 5,100 public charities from across the nation found that more than 20% of those surveyed acknowledged engaging in such financial transactions with board members in the preceding two years.[81] In many cases, the organizations that engaged in self-dealing transactions did not benefit by receiving needed property or services at a

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[77] *Id.* Bruce Hopkins bemoaned the lack of guidance other than regulations, such as private letter rulings or public discussion about the extent of taxes imposed under § 4958. *Id.*

[78] *See infra* Table B (showing SOI data on § 4958 from 2003–2015).

[79] *SOI Tax Statistics*, *supra* note 51. Tables at this site collect data on excess benefit transactions reported on Form 4720.

[80] Again, the number of applicable organizations examined does not correspond precisely to reported § 4958 transactions, because the excise tax falls on individuals and not entities. Moreover, examinations reported may involve several years of the same entity. Further, the numbers include all organizations filing Form 990, not just applicable organizations. However, § 501(c)(3) public charities account for two-thirds of exempt organizations registered with the IRS. *See* BRIAN MCKEEVER, THE NONPROFIT SECTOR IN BRIEF, URBAN INST., NAT'L CTR. FOR CHARITABLE STATISTICS (2018). Overall, these numbers, I believe, give a rough estimate of the level of IRS scrutiny of applicable organizations.

[81] FRANCIE OSTROWER, NONPROFIT GOVERNANCE IN THE UNITED STATES: FINDINGS ON PERFORMANCE AND ACCOUNTABILITY FROM THE FIRST NATIONAL REPRESENTATIVE STUDY 1, 8–9 (2007).

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price below market.[82] Moreover, the bigger the charity, the more likely were such self-dealing transactions.[83] Thus, the available data offer little comfort regarding compliance with § 4958.

C. The Special Case of Supporting Organizations and Donor Advised Funds

Under the Pension Protection Act of 2006,[84] some special rules apply to supporting organizations, entities which are treated as public charities because of their relationship to another public charity,[85] and to DAFs, funds within public charities for which donors can give advice as to distribution or investment of assets.[86] As a result of these special rules, supporting organizations and DAFs face a hybrid of the private foundation and public charity rules.[87]

Any grant, loan, compensation, or other similar payment from a supporting organization to a substantial contributor or a person related to the substantial contributor and any grant, loan, compensation, or other similar payment from a DAF to a person who, with respect to such fund, is a donor, donor advisor, or a person related to a donor or donor advisor is treated automatically as an excess benefit under § 4958,[88] and the entire amount paid to any such person is treated as the amount of the excess benefit.[89] By taxing

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[82] *Id.*

[83] *Id.* at 8.

[84] *See* Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780.

[85] I.R.C. § 509(a)(3). Supporting organizations are deemed to be Type I, Type II or Type III. Type III supporting organizations can be functionally integrated or non-functionally integrated. *See generally I.R.S. Supporting Organizations—Requirements and Types*, https://www.irs.gov/charities-non-profits/charitable-organizations/supporting-organizations-requirements-and-types (last visited on June 26, 2020). A number of special rules apply to non-functionally integrated Type III supporting organizations, but these special rules are beyond the scope of this paper.

[86] I.R.C. § 4966(d)(2).

[87] In addition to special rules regarding § 4958, the legislation in § 4966 imposed another set of excise taxes on certain distributions from the sponsoring organization of a DAF and on knowing managers. These new excise taxes are also beyond the scope of this paper.

[88] *See* I.R.C. § 4958(f)(7). I will use "Donor/Advisor" to refer to all these categories.

[89] *Id.* § 4958(c)(2), (3). The IRS issued interim guidance regarding these provisions, including transition rules and an exception for certain employer-sponsored disaster relief funds, in Notice 2006-109,

the entire amount paid as an excess benefit, these rules apply private foundation principles to an excise tax imposed on two types of public charities.

The Pension Protection Act also added § 4967 to the Code. Section 4967 imposes excise taxes on distributions from DAFs if the distribution provides more than "an incidental benefit" to a donor or other parties related to a donor, whether directly or indirectly.[90] In December 2017, the Treasury and the IRS issued Notice 2017-73 describing the approaches they were considering to address certain issues for DAFs and requesting comments on those approaches.[91] It discussed distributions from a DAF that enable a Donor/Advisor to attend or participate in a charity-sponsored event—known colloquially as a rubber chicken dinner—or a distributions from a DAF that are treated as fulfilling a pledge of Donor/Advisors.[92]

The differing approaches taken in the notice demonstrate the uncertain reach of private foundation principles. Notice 2017-73 states that proposed regulations under § 4967 would provide, if finalized, "that a distribution from a DAF pursuant to the advice of a Donor/Advisor that subsidizes the Donor/Advisor's attendance or participation in a charity-sponsored event confers on the Donor/Advisor a more than incidental benefit." Notice 2017-73 rejected bifurcation, that is, permitting an individual to pay the amount representing private benefit and to attribute to the DAF the charitable contribution portion of the payment.[93] Notice 2017-73 here followed the approach of § 4941.[94]

2006-2 C.B. 1121. *See also* DEP'T OF THE TREASURY, REPORT TO CONGRESS ON SUPPORTING ORGANIZATIONS AND DONOR ADVISED FUNDS (2011).

[90] *See* I.R.C. § 4967(a), (c)(2). The excise tax imposed on the donor or related person is 125% of the benefit. A knowing manager is subject to an excise tax of 10% of the amount of such benefit, up to a maximum of $10,000. *Id.*

[91] I.R.S. Notice 2017–73, 2017–51 I.R.B. 562. This notice followed Notice 2007-21, 2007-1 C.B. 611, requesting comments on the operation of DAFs and supporting organizations.

[92] *Id.* at 562–64. The 2017 Notice also discussed the important issue of using DAFs to avoid public support limitations, but that issue is beyond the scope of this paper.

[93] *Cf.* I.R.S. Priv. Ltr. Rul. 90-21-066 (Mar. 1, 1990) (bifurcation in private foundation context constitutes self-dealing).

[94] *See* Treas. Reg. § 53.4941(d)-2(f)(2) (as amended in 1995) (giving examples of incidental or tenuous benefit); Rev. Rul. 77–160, 1977–1 C.B. 351 (self-dealing when private foundation pays church

In the case of a DAF satisfying a pledge, however Notice 2017-73 stated that regulations, if proposed, would not consider such a distribution to confer more than incidental benefit if a series of somewhat complicated requirements are satisfied.[95] That is Notice 2017-73 there it did not adopt the private foundation rule.[96] The reasoning offered was pragmatic—DAFs have difficulty knowing whether a pledge is legally enforceable under state law.

Notice 2017-73, of course, met with both opposition and support. The National Philanthropic Trust, for example, wrote that "the Notice misses the mark by applying private foundation rules to DAFs that we believe are solely applicable to private foundations."[97] The comment letter noted that the Technical Explanation of the Pension Protection Act defined "more than incidental private benefit" in relation to DAFS by reference to standards applicable to the charitable contribution deduction and not those applicable to private foundations.[98] In contrast, the New York State Bar Tax Section supported the position regarding rubber chicken dinners and urged that distributions to fulfill charitable pledges also be treated as conferring more than incidental benefit.[99] Its response was "guided by our view that in many situations DAFs and private foundations present similar policy issues" and that, as a result, DAF rules regarding more than incidental benefit should conform to the private foundation rules.[100]

We can perhaps understand better both the attraction of and the resistance to the private foundation approach—absolute and objective—in

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membership dues); I.R.S. Gen. Cous. Mem. 36, 784 (July 9, 1975) (background to I.R.S. Rev. Rul. 77–160).

[95] I.R.S. Notice 2017–73, 2017–51 I.R.B. 562, 565.

[96] *See* Treas. Reg. § 53.4941(d)-2(f)(1) (as amended in 1995) (stating that a private foundation's grant or other payment in fulfillment of the legal obligation of a disqualified person ordinarily constitutes a prohibited act of self-dealing).

[97] Gill A. Nusbaum, *DAFs Shouldn't be Treated Like Private Foundations, Charity Says*, 81 EXEMPT ORG. TAX REV. 275 (2018).

[98] *Id.*

[99] N.Y. STATE BAR ASS'N TAX SECTION, REPORT ON NOTICE 2017–73, at 5 (2018), https://www.nysba.org/Sections/Tax/Tax_Section_Reports/Tax_Reports_2018/1390_Report.html.

[100] *Id.* at 3. The Report explains that both private foundations and DAFs share the principal charitable activity of disbursing funds and that, for both kinds of charitable giving vehicles, the donor retains the ability to influence the use of donated funds. *Id.*

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recent legislation and proposed guidance by returning to first principles, the characterization of private foundation self-dealing excise as both a matter of constitutional law and tax policy. This article turns to these issues.

IV. Reconsidering the Character of § 4941

A. Constitutionality

National Federation of Independent Businesses v. Sebelius ("*NFIB*") calls upon us to reconsider the constitutionality and character of § 4941 and other private foundation excise taxes. In *NFIB*, Chief Justice Roberts declined to hold the individual mandate or shared responsibility payment of the Affordable Care Act ("ACA") as constitutional under the Commerce Clause.[101] To the surprise of many, his opinion, joined by Justices Ginsburg, Breyer, Sotomayor and Kagan, upheld it as constitutional under Congress's power to tax, despite Congress dubbing it a penalty.[102] In reaching this conclusion, the Chief Justice articulated a set of tests for Congressional exercise of the taxing power under the Constitution. In doing so, he relied on several of the same cases as courts did in the 1980's when reviewing challenges to the private foundation excise taxes.

Chief Justice Roberts, citing *United States v. Kahriger*,[103] described the essential feature of any tax as producing "at least some revenue for the government."[104] He noted Congressional Budget Office data that the ACA individual mandate was expected to raise $4 billion per year by 2017.[105] The

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[101] *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 546–58.

[102] *Id.* at 561–75. For three of the many analyses of the case, *see, e.g.*, Peter D. Cooter & Neil S. Siegel, *Not the Power to Destroy: An Effects Theory of the Tax Power*, 98 VA. L. REV. 1195 (2012); Barry Cushman, NFIB v. Sibelius *and the Transformation of the Taxing Power*, 80 N.D. L. REV. 133 (2013); Gillian E. Metzger, Comment*: To Tax, To Spend, To Regulate*, 126 HARV. L. REV. 83 (2012). *See also* JOAN BISKUPIC, THE CHIEF: THE LIFE AND TURBULENT TIMES OF CHIEF JUSTICE JOHN ROBERTS (2019) (discussing how the Chief Justice had a 360-degree change of heart regarding the constitutionality of the ACA in an effort to ensure the Court's institutional role in Chapter IX).

[103] United States v. Kahriger, 345 U.S. 22, 28 n.4. (1953). *Kahriger* involved a tax on wagering, which the Court upheld as such.

[104] *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 564.

[105] *Id.* The Tax Cuts and Jobs Act set the rate for the individual mandate at zero, effective January 1, 2019. An Act to provide for reconciliation pursuant to Titles II and V of the concurrent resolution on the budget for fiscal year 2018. Tax Cuts and Jobs Act Pub. L. No. 115-97, §§ 1102(d)(1)(GG), 11081(a),

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Chief Justice continued by contrasting the individual mandate to a so-called tax on child laborers:

> Our cases confirm this functional approach. For example, in *Drexel Furniture*, we focused on three practical characteristics of the so-called tax on employing child laborers that convinced us the "tax" was actually a penalty. First, the tax imposed an exceedingly heavy burden—10 percent of a company's net income—on those who employed children, no matter how small their infraction. Second, it imposed that exaction only on those who knowingly employed underage laborers. Such scienter requirements are typical of punitive statutes, because Congress often wishes to punish only those who intentionally break the law. Third, this "tax" was enforced in part by the Department of Labor, an agency responsible for punishing violations of labor laws, not collecting revenue.[106]

Importantly, the opinion acknowledges that taxes can have a regulatory effect and purpose because they can affect behavior:

> But taxes that seek to influence conduct are nothing new. Some of our earliest federal taxes sought to deter the purchase of imported manufactured goods in order to foster the growth of domestic industry . . . . And we have upheld such obviously regulatory measures as taxes on selling marijuana and sawed-off shotguns. Indeed "[e]very tax is in some measure regulatory. To some extent it interposes an economic impediment to the activity taxed as compared with others not taxed."[107]

Chief Justice Roberts also wrote, "imposition of a tax nonetheless leaves an individual with a lawful choice to do or not do a certain act, so long as he is willing to pay a tax levied on that choice."[108]

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131 Stat. 2054 (2017). The mandate thus no longer raises any revenue. As a result of this change to the law, the Fifth Circuit on December 18, 2019 held the individual mandate unconstitutional and remanded the case for consideration of the provision's severability. *See* Texas v. United States, 945 F.3d 355 (5th Cir. 2019), *cert. granted*, 140 S. Ct. 1262 (2020).

[106] *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 565–66 (citing Bailey v. Drexel Furniture (Child Labor Tax Case), 259 U.S. 20 (1922)).

[107] *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 567 (citations omitted) (quoting Sonzinsky v. United States, 300 U.S. 506, 513 (1937)). To support this statement, the opinion cites *United States v. Sanchez*, 340 U.S. 42, 44–45 (1950) (tax on marijuana) and *Sonzinsky v. United States*, 300 U.S. 506, 513 (1937) (tax on sawed-off shotguns). Both of these cases observe that a tax can be a tax even if obtains "negligible revenue." *Id.* Note that the opinion included citations to the IRS Cumulative Bulletin.

[108] *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 574.

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However, the opinion warns that "Congress's ability to use its taxing power to influence conduct is not without limits."[109] It explained that "there comes a time in the extension of the penalizing features of the so-called tax when it loses its character as such and becomes a mere penalty with the characteristics of regulation and punishment."[110] Further, "[i]n distinguishing penalties from taxes, this Court has explained that 'if the concept of penalty means anything, it means punishment for an unlawful act or omission.'"[111] *NFIB* concludes that "we need not here decide the precise point at which an exaction becomes so punitive that the taxing power does not authorize it."[112]

The occasion of its fiftieth anniversary offers an ideal opportunity to subject § 4941 to the full gauntlet of the *NFIB* tests. That is, we should at least try to answer the question that *NFIB* avoided—whether this excise tax is so punitive as to be beyond the reach of the taxing powers. To a large extent, cases from decades ago have addressed this very question with analysis very much like *NFIB* in some ways and in other ways very different. The differences necessitate re-examining the constitutional status of these excise taxes.

Importantly, in the case of the private foundation excise taxes, unlike the ACA individual mandate, Congress has characterized § 4941 as a tax. As Professor Erik Jensen has observed, "[i]f Congress is willing to characterize as a tax what we might otherwise think of a penalty, courts are unlikely to reject that characterization."[113] Jensen acknowledges that such is not always the case. *NFIB* relies on *Drexel Furniture*, and there the Supreme Court

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109 *Id.* at 572.

110 *Id.* at 573 (citing Dep't of Revenue of Mont. v. Kurth Ranch, 511 U.S. 767, 779 (1994)) (quoting *Drexel Furniture*, 259 U.S. at 38). *Kurth Ranch* upheld a state tax on illegal possession and storage of dangerous drugs. There, the Court wrote, that "at some point, an exaction labeled as a tax approaches punishment" but "neither a high rate of taxation nor an obvious deterrent purpose automatically marks this tax as a form of punishment." *Id.* at 780–81.

111 *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 567 (quoting United States v. Reorganized CF&I Fabricators of Utah, Inc., 518 U.S. 213, 224 (1996)).

112 *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 573.

113 Erik M. Jensen, *The Individual Mandate, Taxation, and the Constitution*, J. OF TAX. OF INVESTMENTS 31, 40 (2012). In contrast to the child labor tax, which the Court struck down, § 4941 is administered by the IRS.

rejected Congress's characterization of charges on those who employ child laborers as a tax.

The cases upholding private foundation excise taxes do not rely on *Drexel Furniture*, but they do rely on other cases that have a prominent place in *NFIB*. The Tax Court's 1987 decision in *Miller Charitable Fund v. CIR*,[114] held the § 4942 excise tax on certain undistributed income to be constitutional.[115] The case acknowledged this excise tax was designed to address perceived abuses of the exempt status of private foundations. Relying on *Sonzinky v. United States*[116] and *United States v. Sanchez*,[117] as did the Supreme Court in *NFIB*, the Tax Court upheld the tax to be a constitutional tax "despite its collateral regulatory purpose and effect."[118]

Other cases specifically address § 4941. These cases include discussion of distinctions between a tax and a penalty as both constitutional and statutory matters, the very issues considered but not resolved in *NFIB*. Section 4941 is a particularly good touchstone for applying the tests of *NFIB v. Sebelius*. It taxes not the private foundation itself, which is a creature of the Code, but individuals with a relationship to the foundation. Moreover, unlike the other private foundation excise taxes, the IRS has no authority under § 4962 to abate the first-level tax for reasonable cause.

In 1982, an Arkansas federal district court in *Rockefeller v. United States*[119] upheld the constitutionality of § 4941. The transaction at issue involved indirect self-dealing between a private foundation established in the will of Winthrop Rockefeller and his son for sales of stock at less than fair market value during administration of the estate.[120] The court found such indirect self-dealing. As in *Miller*, the court upheld the private foundation

[114] *See* Miller Charitable Fund v. Comm'r, 89 T.C. 1112 (1987).

[115] *Id.* at 1119.

[116] *Sonzinsky*, 300 U.S. at 506 (tax on sawed-off shotguns).

[117] *Sanchez*, 340 U.S. at 42 (tax on marijuana).

[118] *Miller Charitable Fund*, 89 T.C. at 1119.

[119] Rockefeller v. United States, 572 F. Supp. 9 (E.D. Ark. 1982), *aff'd* 718 F.2d 290 (8th Cir. 1983).

[120] *Id.* at 11.

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excise tax as constitutional.[121] *Rockefeller*, too, relied on many of the same cases as did the Supreme Court decades later in *NFIB—Sanchez*, *Sonzinsky*, and *Kahriger*. The amount of the § 4941 tax in *Rockefeller* was enormous—$2,067,558.95, which included $341,865 in § 4941 taxes imposed for each of the calendar years of 1975 through 1980, plus $358,233.95 of interest.[122] Language from the case, however, would uphold the § 4941 excise tax even when it produces little revenue, as currently is the case. The court wrote, "[a]lthough § 4941 has a regulatory effect on the activities of charitable organizations and might not raise *any* revenue, it ensures that revenue will be collected under income, estate, and gift tax laws which otherwise might have gone uncollected."[123]

In accordance with a 1980 District Court case, *Farrell v. United States*,[124] *Rockefeller* nonetheless found § 4941(a)(1), the first-tier tax, to be a penalty for purposes of § 6601(3).[125] Section 6601(e)(3) imposes no interest on an assessable penalty if paid within ten days of notice and demand.[126] Such was the case in *Farrell*, and thus, the executor was entitled to a refund of interest paid.

Farrell relied on two earlier cases, both bankruptcy cases,[127] to decide that § 4941 imposes a penalty. The bankruptcy cases turned on the definition of a penalty under the 1898 Bankruptcy Act as an enactment. They found the bankruptcy to have as its purpose "the punishment of conduct perceived as

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121 *Id.* at 13.

122 *Id.* at 12. Inflation adjusted, using the CPI Inflation Calculator, the total amount comes to more than $5,500,000 in today's dollars. As discussed in text at *supra* note 38, the IRS had promised a vigorous enforcement effort in connection with the new private foundation excise taxes. *Rockefeller* involved tax years not long after adoption of the 1969 Tax Reform Act.

123 *Id.* at 13 (emphasis added).

124 Farrell v. United States, 484 F. Supp. 1097 (E.D. Ark. 1980).

125 *Rockefeller*, 571 F. Supp. at 16.

126 I.R.C. § 6601(e)(3); Deluxe Check Printers, Inc. v. United States, 14 Cl. Ct. 782 (1988) (supplemental opinion at 15 Cl. Ct. 175 (1988) relying on *Rockefeller* to conclude that § 4941 was a penalty for purposes of assessing interest). The Court of Appeals reversed the decision regarding liability for the tax and thus did not reach the penalty issue. Deluxe Corp. v. United States, 885 F.2d 848 (Fed. Cir. 1989).

127 *In re* Kline, 403 F. Sup. 974 (D. Md. 1975), *aff'd per curiam*, 547 F.2d. 824 (4th Cir. 1977); *In re* Unified Control Systems, Inc., 586 F.2d 1036 (5th Cir. 1978).

wrongful,"[128] language reminiscent of *NFIB*. *Farrell* rejected the government's argument that the definition of penalty under the bankruptcy code did not control its definition under the Code.

In a 1988 case, *Latterman v. United States*,[129] a Pennsylvania District Court addressed an excise tax, one similar to that in § 4941, under § 4975 for a "prohibited transaction" between a pension plan and a disqualified person. *Latterman* rejected reliance on these bankruptcy cases to interpret § 6601. Instead, it looked to Congress's choice of the word "tax" and observed, "[W]e find nothing in Section 6601 that suggests that Congress intended courts to engage in the rather slippery business of weighing the relative importance of a penal purpose compared with a revenue-raising purpose underlying an assessment in order to determine when interest begins to accrue."[130]

As in these excise tax cases from the 1980's, the character of § 4941 and similar provisions as a tax or a penalty seems uncertain under *NFIB*. *NFIB* acknowledges that a tax can have a regulatory intent and effect. At the same time, *NFIB*'s discussion of penalty turns, at least in part, not on the purpose of or motive for an assessment, but on its level—whether it imposes a heavy burden. Under a strong reading of *NFIB*, the first-tier tax might fail the case's tests for a constitutional tax by taxing the entire amount of a self-dealing transaction rather than just the amount by which the private foundation, and thus the public, is harmed. Even if the first-tier tax passes muster, the second-tier tax of 200% for failure to correct may exceed Congress's taxing power. It gives a disqualified person little if any meaningful choice of whether or not to pay the tax.[131] Moreover, the excise taxes on knowing managers implicate

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[128] *In re* Kline, 403 F. Supp. at 978.

[129] Latterman v. United States, 872 F.2d 564 (3d Cir. 1989). The first-tier tax under § 4975 is 15%, the second-tier 100%. Section 4941 served as the model for § 4975. Aprill, *supra* note 1, at 452–57 (comparing § 4941 and § 4975).

[130] *Latterman*, 872 F.2d at 569–70.

[131] The IRS does impose the second-tier excise taxes involving § 501(c)(3) organizations, in the context of I.R.C. § 4941 and other provisions. *See, e.g.*, United States v. Ziegenhais, 2014 U.S. Dist. LEXIS 37253 (D. Ct. Texas 2014) (upholding second-tier I.R.C. § 4941 taxes); Caracci v. CIR, 456 F.3d 444, 447 (5th Cir. 2006) (overturning first- and second-tier I.R.C. § 4958 taxes imposed by IRS); Moody v. CIR, 1995 T.C. Memo LEXIS 195 (1995) (upholding second-tier I.R.C. § 4941 taxes on self-dealer); Thorne v. CIR, 99 T.C. 67 (1992) (overruling IRS imposition of second tier taxes under I.R.C. § 4944 and I.R.C. § 4945 for procedural reasons); Howell v. CIR, 77 T.C. 916 (1981) (determining that under the Second Tier Correction Tax Act of 1980, Tax Court had jurisdiction to review a docketed but untried case

the scienter requirement *NFIB* identified as another indication of a penalty. Further, the cases addressing § 4941 view its regulatory purpose as rendering self-dealing unlawful, another key characteristic of a penalty, according to *NFIB*.

Again, quoting Professor Jensen, "At the margin, distinguishing between a tax and a penalty can be difficult . . . . In addition, there can be doubts as to whether Congress really intended to make particular behavior unlawful."[132] Professor Jensen adds that "we need to remember that in most cases the tax-versus-penalty characterization will not matter. Unless the Commerce Clause is substantially reined in in subsequent cases, by far most governmental charges will continue to be valid whether characterized as penalties or taxes."[133] Thus, even if these excise taxes fail the *NFIB* tests for congressional exercise of the taxing power, they are unlikely to risk being held unconstitutional. Still, it is possible that § 4941 is not a tax but a penalty as a constitutional matter.

In light of *NFIB*, private foundation excise taxes do not fit easily into either the category of constitutional taxes or constitutional penalties. The difficulty in characterizing § 4941, of course, may lie with *NFIB* itself. That is, applying *NFIB* to § 4941, rather than illuminating the excise tax provision, exposes the weakness of the Supreme Court's distinction between a tax and a penalty. It offers further confirmation to those who read the opinion as a less than coherent compromise that was "plainly an effort to protect the Court."[134]

Reviewing the cases involving the constitutionality of the private foundation excise taxes, moreover, underscores another aspect of *NFIB*, that the constitutional meaning of tax is not identical to the term's statutory meaning. Although *NFIB* upheld the individual mandate as a tax for

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involving second-tier I.R.C. § 4941 taxes). I note that I.R.C. § 4961, added in 1980 by Pub. L. 96-596, requires abatement of second-tier taxes if correction is made before the end of the correction period.

[132] Jensen, *supra* note 113, at 35.

[133] *Id.* at 40.

[134] Metzger, *supra* note 102, at 86.

constitutional purposes, it did not so characterize it for purposes of § 7421, the Anti-Injunction Act.[135] The opinion explains:

> Congress cannot change whether an exaction is a tax or a penalty for *constitutional* purposes simply by describing it as one or the other. Congress may not, for example, expand its power under the Taxing Clause, or escape the Double Jeopardy Clause's constraint on criminal sanctions, by labeling a severe financial punishment a "tax". . . . The Anti-Injunction Act and the Affordable Care Act, however, are creatures of Congress's own creation. How they relate to each other is up to Congress, and the best evidence of Congress's intent is the statutory text. . . .[136]

Because the statute did not characterize the individual mandate as a tax, the Court decided it was not a tax for purposes of the Anti-Injunction Act, and the Court could reach the merits of the case even though the provision had not yet been enforced. Thus, because of the Court's distinction between constitutional and statutory meanings of "tax" and "penalty," *NFIB* does not undermine the line of cases from the 1980's treating § 4941 as a tax for constitutional purposes but as a penalty for certain statutory purposes, such as imposition of interest.

Whether to conceptualize § 4941 and the other private foundation excise taxes as a penalty has long been a matter of dispute. When the IRS Commissioner conducted an elaborate study of penalties in 1989, the study treated the private foundation taxes as penalties. It found the two-tier excise taxes, with the second-tier tax at very high levels, to be effective.[137] Yet, when the Joint Committee on Taxation studied penalties in 1999, it declined to study these excise taxes as penalties, in part because doing so "could make it more difficult to draw a distinction between normal operation of the substantive rules of the Code and 'penalty' provisions."[138] Moreover, treating these excise taxes as penalties would call for difficult decisions regarding the

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[135] The Anti-Injunction Act bars suits "for the purpose of restraining the assessment or collection of any tax." I.R.C. § 7421(a).

[136] *Nat'l Fed'n of Indep. Bus.*, 567 U.S. at 544.

[137] *See supra* note 45.

[138] JOINT COMM. ON TAXATION, 106TH CONG., JCS-3-99, STUDY OF PRESENT-LAW PENALTY AND INTEREST PROVISIONS AS REQUIRED BY SECTION 3801 OF THE INTERNAL REVENUE SERVICE RESTRUCTURING AND REFORM ACT OF 1988 (INCLUDING PROVISIONS RELATING TO CORPORATE TAX SHELTERS) VOL. I, 15 (Comm. Print 1999).

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level of tax required to effect deterrence in a world, unlike that at the time of the provisions' adoption, where enforcement levels are low.[139]

The status of § 4941 is uncertain under *NFIB*, under the private foundation cases from the 1980's, and the positions of key governmental bodies. Yet, how we characterize § 4941 matters. It affects how we evaluate its success and what changes would improve its effectiveness. Uncertainty under current approaches suggests attempting another way to understanding it. I make that attempt next by evaluating § 4941 as a Pigouvian tax, a tax that would meet the tests of *NFIB*, but which has a particular regulatory purpose.

B. Section 4941 as a Pigouvian Tax

Pigouvian taxes, named for the economist Arthur Pigou, aim to regulate behavior by placing a small tax, usually in the form of a uniform excise tax, on the activity to be regulated because of the harm it produces for members of the public. This harm, a cost its producer does not take into account, is known as an externality. As Professor Vic Fleischer has explained, "The idea is that by placing a small tax, equal to marginal social cost, on each unit of an activity to be discouraged—environmental pollution is the most common example—prices will rise, forcing polluters to internalize the social cost of the harmful activity."[140] In the words of two economists, a Pigouvian tax forces those undertaking harmful activities "[t]o consider the extra social cost" they impose.[141]

These taxes are the economists' darling. Gregory Mankiw has written, "To many economists, the basic argument for increased use of Pigouvian

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[139] *See* Aprill, *supra* note 1, at 445–51 (discussing in more detail the application of economic deterrence theory to § 4941).

[140] Victor Fleischer, *Curb Your Enthusiasm for Pigouvian Taxes*, 68 VAND. L. REV. 1673, 1675 (2015). As will be obvious, I am much indebted to this piece for its description of economic theory in ways lawyers can understand. *See also* Jonathan S. Masur & Eric A. Posner, *Toward a Pigouvian State*, 164 U. PA. L. REV. 934 (2015), Brian D. Galle, *Carrots, Sticks, and Salience*, 67 TAX L. REV. 53 (2013); Brian D. Galle, *The Tragedy of the Carrots: Economics and Politics in the Choice of Price Instruments*, 64 STAN. L. REV. 797 (2012).

[141] LEONARD E. BURMAN & JOEL SLEMROD, TAXES IN AMERICA: WHAT EVERYONE NEEDS TO KNOW 98 (2013).

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taxes is so straightforward as to be obvious."[142] Academics are particularly enamored of them and have suggested such a tax on "carbon, gasoline, fat, high fructose corn syrup, guns, financial transactions, executive pay, excessive zoning, and sport utility vehicles."[143]

A carbon tax is the best known Pigouvian tax. The Tax Policy Center, for example, describes the reasons for a carbon tax as follows:

> Energy prices do not currently reflect these costs of greenhouse gas emissions. Those who benefit from burning fossil fuels generally do not pay for the environmental damage the emissions cause. Instead, this cost is borne by people around the world, including future generations. Imposing a carbon tax can help to correct this externality by raising the price of energy consumption to reflect its social cost.[144]

Because of the widespread attention to a possible carbon tax, many have been exposed to the idea of a Pigouvian tax without knowing the term.

Although many Pigouvian taxes involve adjusting prices of commodities,[145] proposals for Pigouvian taxes go further. In particular, several economists have considered Pigouvian taxes on CEO and other high levels of compensation. In 2012, well before the current debate on wealth inequality, Liam C. Malloy argued for such a Pigouvian tax, writing that "the worsening distribution of income in the United States, and in particular the amounts going to those at the top" create "an externality with broader negative side effects akin to pollution and hence as something that should be heavily taxed."[146] Lockwood, Nathanson and Weyl, in order to account for externalities, include a Pigouvian tax as part of their proposal for an optimal

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[142] Fleischer, *supra* note 140, at 1676 n.10 (quoting N. Gregory Mankiw, *Smart Taxes: An Open Invitation to Join the Pigou Club*, 35 EAST. ECON. J. 14, 15 (2009)).

[143] Fleischer, *supra* note 140, at 1675.

[144] *See Key Elements of the U.S. Tax System, What Is A Carbon Tax*, TAX POL'Y CTR: BRIEFING BOOK (2020), https://www.taxpolicycenter.org/briefing-book/what-carbon-tax; *see also* NOAH KAUFMAN & KATE GORDON, THE ENERGY, ECONOMIC AND EMISSIONS IMPACTS OF A FEDERAL US CARBON TAX, COLUM. CTR. ON GLOBAL ENERGY POL'Y (2018); Don Marron et al., *Taxing Carbon: How, What and Why*, TAX POL'Y CTR. (2015), https://www.taxpolicycenter.org/publications/taxing-carbon-what-why-and-how/full. Fleischer endorses Pigouvian taxes on pollution. *See* Fleischer, *supra* note 140, at 1691–92.

[145] *See* Katherine Pratt, *A Constructive Critique of Public Health Arguments for Antiobesity Soda Taxes and Food Taxes*, 87 TUL. L. REV 73 (2012) (comparing cigarette and food taxes).

[146] *See* Liam C. Malloy, *Want Less Inequality? Tax It*, AM. PROSPECT (Nov. 14, 2012), https://prospect.org/culture/books/want-less-inequality-tax/.

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tax on the allocation of talent.[147] Others describe the inclusion of a Pigouvian term for high labor income as a correction for "rent-seeking activity."[148]

We can easily extend such analysis to view § 4941 in Pigouvian terms. The Code has established the category of private foundations and the specific requirements for them in order that they serve public purposes. It broadly prohibits self-dealing between disqualified persons—insiders—and private foundations out of concern that these insiders will receive too much from or pay too little to the private foundations. That is, to the extent that those involved with private foundations engage in self-dealing, they serve personal purposes and impose social costs by undermining the public purpose. The Code thus imposes an excise tax on self-dealing.

So far, so good. But, as Professor Fleischer has cautioned, a Pigouvian tax "assumes uniform marginal social costs across all individuals and firms."[149] That is, Pigouvian taxes work:

> when policymakers can readily observe the relationship between the activity causing the harm and the amount of harm caused, and where there is little variation among taxpayers. In such cases a uniform excise tax may be set to make the externality-producer bear an additional tax burden so that the private cost of the activity equals the social cost. Unless the variation is closely related to income, the tailoring necessary to address the variation is likely beyond the institutional capacity of the Treasury Department and the Internal Revenue Service.[150]

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[147] Benjamin B. Lockwood et al., *Taxation and the Allocation of Talent*, 125 J. POL. ECON. 1635, 1635–82 (2017).

[148] *See, e.g.*, Thomas Piketty et al., *Optimal Taxation of Top Labor Incomes: A Tale of Three Elasticities*, 6 AM. ECON. J. 230 (2014); Casey Rothschild & Florian Scheuer, *Optimal Taxation with Rent-Seeking*, 83 REV. ECON. STUD. 1225 (2016). Rent-seeking occurs "when an entity seeks to gain added wealth without any reciprocal contribution of productivity." Christina Majaska, *What is Rent Seeking*, INVESTOPEDIA, https://www.investopedia.com/terms/r/rentseeking.asp (last visited June 26, 2020). Journalist Ben Casselman has explained the term as "gaming the system to make more money than you have earned." Ben Casselman, *The Rent-Seeking Is Too Damn High*, ABC (Nov. 5, 2016, 7:00 AM), https://fivethirtyeight.com/features/the-rent-seeking-is-too-damn-high/.

[149] Fleischer, *supra* note 140, at 1676 ("[A] Pigouvian tax is likely to work well when marginal social cost is roughly equal to average social cost. More precisely, a Pigouvian tax is likely to be optimal when there is a normal and narrow distribution of marginal social costs across the different firms and individuals that engage in that activity.").

[150] *Id.* 140, at 1689–91.

If we apply these observations to the private foundation excise taxes, we may wonder whether differences between large and small foundations, between corporate and family foundations, local and national foundations, old and new foundations, etc. should shape the applicable excise tax rules. Moreover, the fact that § 4941 subjects the entire amount of a self-dealing transaction to tax, even if the transaction benefits the foundation, demonstrates that it does not operate as a Pigouvian tax (not to mention the 200% tax on failure to correct!). A self-dealing transaction that benefits the exempt organization does not impose social costs.

Professors Masur and Posner acknowledge Fleischer's point that Pigouvian taxes can be difficult to calculate. But, they continue, "this argument would apply equally to any type of regulations where the regulator must calculate social costs, not only Pigouvian taxes."[151] They also observe that Pigouvian taxes offer an advantage over other forms of regulation: a "regulator only needs to know the cost of the activity to determine the correct Pigouvian tax. It is not necessary to know the benefit."[152] By this reasoning, a flawed excise tax may be preferable to other regulatory options.

With the contrast between Fleischer's position and that of Masur and Posner, why do I even bring up Pigouvian taxes? Just to seem trendy? I hope not. I do so because this approach focuses us on the purpose and structure of excise taxes on self-dealing by § 501(c)(3) organizations. For these kinds of transactions, we have been unable to settle on the measurement of harm. To quote Professor Fleischer again, "[t]ax instruments are easiest to use to achieve social policy goals when policymakers can readily observe the relationship between the activity causing the harm and the amount of harm caused, and where there is little variation among taxpayers."[153]

Fleischer explains that, if such is not the case, and especially if the tax agency does not have specialized knowledge regarding the variation among externality producers, regulation by a specialized agency may be preferable to taxation.[154] The checkered history of choosing subjective or objective

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[151] Masur & Posner, *supra* note 140, at 138.

[152] *Id.* at 95.

[153] Fleischer, *supra* note 140, at 1691.

[154] *Id.* at 1694–97. *See also* JEREMY BEARER-FRIEND, THE GREAT DEMOCRACY INITIATIVE, RESTORING DEMOCRACY THROUGH TAX POLICY 15 (2018), https://greatdemocracyinitiative.org/wp-

standards to tax self-dealing by § 501(c)(3) organizations—whether private foundations, public charities generally, or DAFs and supporting organizations in particular—demonstrates the difficulties of matching the excise tax to the extent of social harm to the § 501(c)(3) entity and to the public. That is, these taxes have the Pigouvian impulse to protect the public from harm by imposing an excise tax but fail to achieve this goal.

Congress enacted § 4941 because a subjective standard did not work; § 4958 returned to a subjective standard because of the difficulty in demonstrating the amount of social harm—the excess benefit. Legislation regarding DAFs and supporting organizations reverted to the objective standard. In short, tax policy regarding self-dealing by § 501(c)(3) organizations has alternated between invoking subjective and objective standards. As the SOI data demonstrate, neither option seems to have succeeded, especially in light of the low level of enforcement.

V. CONCLUSION

Self-dealing can harm § 501(c)(3) organizations by failing to provide such organizations with adequate economic benefit for transactions with insiders. Self-dealing diminishes the ability of such entities to pursue their charitable—and therefore public—purposes. Insiders, which the Code calls disqualified persons, have a particular ability to engage in rent-seeking—that is, to extract resources—from tax-exempt organizations. Thus, the Code includes regulatory excise taxes on self-dealing. Because private foundations can give insiders greater control than do public charities, the risk of inurement in the form of self-dealing is high, perhaps inherent, to this category of § 501(c)(3) organizations, and the Internal Revenue Code has stricter rules for private foundations than for public charities.

Many believe that § 4941 has succeeded in its intended *in terrorem* effect.[155] Its bright line rules enable advisors to give private foundations clear

content/uploads/2018/12/Tax-and-Democracy-121118.pdf (recommending OMB conduct review of agency authority to impose Pigouvian taxes and that EPA, SEC, and DOL conducting trial rounds of Pigouvian taxes).

[155] *See, e.g.*, U.S. GOV. PRINTING OFF., TAX RULES GOVERNING PRIVATE FOUNDATIONS: HEARINGS BEFORE THE SUBCOMMITTEE ON OVERSIGHT OF THE COMMITTEE ON WAYS AND MEANS OF

and unequivocal advice, usually a resounding, "Don't." Nonetheless, dissatisfaction remains. On one hand, violations undoubtedly go unreported and undetected, given the low levels of enforcement.[156] On the other hand, the prohibition of self-dealing transactions benefitting the private foundation produces frustration.[157]

Somewhat ironically, less stringent rules could increase compliance by removing some of the rule's paralyzing terror. To that end, in my 2014 piece, I suggested both procedural protections and a system of pre-approval.[158] Another possible relaxation would involve amending § 4962.[159] This provision permits the IRS to abate first-tier private foundation excise taxes if the violation was due to reasonable cause, was not due to willful neglect, and has been corrected within the appropriate correction period.[160] Section 4962, however, explicitly excludes § 4941 from this possible administrative grace.[161]

When the IRS Commissioner established a task force to study tax penalties in the late 1980s,[162] the Tax Force found that the private foundation two-tier excise taxes encouraged remedial action. It acknowledged that two-tier excise taxes could pose issues as to comprehensibility but assumed that private foundations generally would have tax advisors. As for administrability, the report stated, "In administering the excise tax provision, the Service can exercise a certain amount of discretion in imposing the tax. Section 4962 provides that, if the Service determines the event was due to reasonable cause and not willful neglect and such event was corrected within the applicable correction period, no first-tier tax will be imposed."[163] This

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THE HOUSE OF REPRESENTATIVES, 98TH CONG., SERIAL 98-32, PART I 57–65 (1984) (providing the statement of James I. Owens, IRS Acting Commissioner at the hearings).

[156] *See supra* Part I(C).

[157] *See* Tax Analysts, *supra* note 60.

[158] *See* Aprill, *supra* note 1, at 451–58.

[159] I thank Douglas Mancino for this suggestion.

[160] I.R.C. § 4962(a).

[161] *Id.* § 4962(b).

[162] See Tax Analysts, *supra* note 45.

[163] *Id.*

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statement, however, failed to note that § 4962 does not apply to self-dealing transactions under § 4941. Section 4941 by its terms does not meet the Task Force's criteria for administrability, which relies on administrative discretion rather than strict liability.[164]

The IRS's own analysis calls for extending abatement of first-tier taxes to § 4941 violations. If such is the path chosen, violations of § 4941 would have to satisfy the § 4962 criteria—a showing of reasonable cause, absence of willful neglect, and successful correction. No definition of "reasonable cause" or of "willful neglect" for purposes of § 4962 appears in the Code or applicable regulations. An EO CPE chapter from 1992 looks to similar language in § 6651, which addresses abatement of penalties for failure to file a tax return or pay tax, to interpret these requirements.

On the basis of that comparison, the 1992 EO CPE chapter suggests that reasonable cause for abating first-tier of eligible private foundation excise taxes would require a taxpayer to demonstrate exercise of "ordinary business care and prudence in providing for the payment of the tax liability" and that the taxpayer was "either unable to pay or would have suffered an undue hardship if the liability had been paid on the due date."[165] According to this EO CPE text, willful neglect "implies failure to exercise the care that a reasonable person would observe under the circumstances to see that the standards were observed, despite knowledge of the standards or rules in question."[166] It emphasizes that the absence of willful neglect does not suffice; reasonable cause must also exist.[167] That is, according to this IRS interpretation, satisfying the requirement of reasonable cause under § 4962 sets a higher hurdle than absence of willful neglect, which requires knowledge of applicable law.[168]

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[164] In fact, the IRS has been known to abate penalties without explicit statutory authoring. *See I.R.S. Penalty Relief Due to First Time Penalty Abatement or Other Administrative Waiver*, https://www.irs.gov/businesses/small-businesses-self-employed/penalty-relief-due-to-first-time-penalty-abatement-or-other-administrative-waiver (last visited June 26, 2020).

[165] Thomas Miller et al., *supra* note 41. *See also* Treas. Reg. § 301.6651-1(c).

[166] *Id.*

[167] *Id.*

[168] Guidance under statutory provisions regarding requirements for the charitable contribution deduction would also seem to offer a useful model for interpreting § 4962, a provision applicable to

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The *2017 Penalty Handbook* in the *Internal Revenue Manual* (*IRM*) goes into more detail than the 1992 EO CPE chapter regarding reasonable cause.[169] The *Penalty Handbook* lists a number of examples of reasonable cause. They include death or serious illness or unavoidable absence of the taxpayer and fire, casualty or natural disaster.[170] In very specific circumstances, according to the *Penalty Handbook*, ignorance of the law may serve as reasonable cause. Factors for relying on ignorance include consideration of a taxpayer's education as well as a reasonable and good faith effort to comply with the law.[171] One commentator has asserted that a taxpayer can satisfy the reasonable cause requirement when "erroneous good faith belief is coupled with objective ambiguity in the applicable statute."[172]

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organizations eligible to receive tax-deductible charitable contributions. Section 170(f)(11)(A)(ii)(II), in particular, has parallel language. It permits a deduction even for contributions that lack a qualified appraisal if the failure is due to reasonable cause and not willful neglect. Proposed § 170 regulations from 2008 had provided that, to meet the "reasonable cause" exception, the donor would have to submit a detailed explanation with his or her return of why the failure was due to reasonable cause and not willful neglect. The Service warned in the preamble to the proposed regulations that it anticipated strictly construing the reasonable cause exception. *Substantiation and Reporting Requirements for Cash and Noncash Charitable Contribution Deductions*, 73 Fed. Reg. 45908, 45911–12 (Aug. 7, 2008), https://www.govinfo.gov/content/pkg/FR-2008-08-07/pdf/E8-17953.pdf. The 2018 preamble to the final regulations, however, explains that because of Crimi v. Comm'r, T.C.M. 2013-51, 105 T.C.M. (CCH) 1330 (2013), proposed regulation § 170A-16(f)(6) regarding reasonable cause had been deleted. That is, the final regulations contain no standard for the reasonable cause exception under § 170(f)(11)(A)(ii)(II). *See* T.D. 9636, 83 Fed. Reg. 36417, 36419. *See infra* note 184 for further discussion of *Crimi*.

[169] *See* I.R.M. 20.1.1. (outlining the *Penalty Handbook*) As Saltzman and Book explain, the IRS may use the Reasonable Cause Assistant, a decision-support interactive software tool, in making a reasonable cause determination. MICHAEL SALTZMAN & LESLIE BOOK, IRS PRACTICE AND PROCEDURE, ¶ 7B.07[2][6]. *See Penalty Handbook* at IRM 20.2.2.3.6.

[170] I.R.M. 20.2.1.3.2.2.1, 20.1.1.3.2.2.2.

[171] I.R.M. 20.2.1.3.2.2.6.

[172] John Anthony Castro, *Reasonable Cause to Avoid Tax Penalties*, CASTRO & CO. INT'L (Jan. 31, 2019), https://www.castroandco.com/blog/2019/january/reasonable-cause-to-avoid-tax-penalties/ (citing United States v. Northumberland Ins. Co., Ltd., 521 F. Supp. 70 (D.N.J. 1981). *See, e.g.*, Williams v. Comm'r, 123 T.C. 144 (2004) (holding taxpayer was able to show his positions taken on net operating loss carryforward were "reasonable and taken in good faith" where issue was "unclear and complex" even though Service was ultimately successful on underlying issue); Patients Mutual Assistance Collective Corp. v. Comm'r, 151 T.C. 176 (2018) (reversing penalties where taxpayer's position when little authority and credible verbal testimony that taxpayer attempted to comply with law in good faith); Peterson v. Comm'r, 148 T.C. 463 (2017) (reversing penalties because matter was case of first impression, and taxpayers made good-faith effort to assess liability). *But see* Baxter v. Comm'r, 910 F.3d 150 (4th Cir. 2018) (holding noncredible testimony of taxpayer called into question whether there was an honest misunderstanding of the law, even where issue was complicated).

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For private foundations without counsel, some cases of indirect self-dealing may meet an "objective ambiguity" test.[173] A direct self-dealing transaction that benefits the foundations seems less likely to do so, even though those without professional advisors may not realize such a transaction is subject to the self-dealing excise tax.

Particular code provisions are more generous than the *Penalty Handbook* general discussion regarding ignorance of the law. Section 6664 excuses underpayment penalties for accuracy under § 6662 if there is reasonable cause and the taxpayer acted in good faith.[174] The regulations under this provision state, "Circumstances that may indicate reasonable cause and good faith include an honest misunderstanding of fact or law that is reasonable in light of all of the facts and circumstances, including the experience, knowledge, and education of the taxpayer."[175] Under such a test, disqualified persons without knowledge of private foundation law and without professional advice, as seems to be the case with many small family foundations,[176] could assert reasonable cause under such a standard if § 4962 were extended to § 4941.

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[173] One example of indirect self-dealing is a transaction between a disqualified person and a corporation controlled by the private foundation. *See* I.R.S. Rev. Rul. 76-158; Treas. Reg. § 53.4941(d)-1(b)(8). Example 6, gives another. There a private foundation and two of its disqualified persons, a substantial contributor and the son of the substantial contributor, control Corporation W by virtue of stock ownership that, as a bloc, could elect the majority of W's board. The two disqualified persons also own 50% of the stock of corporation Y, making Y a disqualified person. The making of a loan of $100,000 by W to Y constitutes an indirect act of self-dealing between Y and the private foundation.

[174] *See* I.R.C. § 6664(c). Section 6662 applies penalties for underpayments resulting from negligence. Section 6662(c) defines "negligence" as "any failure to make a reasonable attempt to comply with provisions of this title. As Saltzman and Book observe, "Courts have said, with respect to the negligence penalty, that 'negligence is lack of due care or failure to do what a reasonable and ordinarily prudent person would do under the circumstances.'" SALTZMAN & BOOK, *supra* note 169, at ¶ 7B.03[2][a][i] (quoting Marcello v. Comm'r, 380 F.2d 499 (5th Cir. 1967) and citing other cases).

[175] Treas. Reg. § 1.6664-4(b). SALTZMAN & BOOK, *supra* note 169, at ¶ 7B.03[3][a][i], n.232, caution that "[t]he Service disagrees that complexity of the law alone absent taxpayer effort to ascertain the law can constitute reasonable cause."

[176] Fishman, *supra* note 16, at 289. However, those wealthy enough to establish a private foundation as well as others who have oversight of the foundation may have difficulty proving themselves to be sufficiently unsophisticated for this defense. *Cf.* United States v. Agrawal, 2019 U.S. Dist. LEXIS 212438 (Dec. 9, 2019) (rejecting argument of lack of sophistication by taxpayer who worked as math teacher and geophysicist for non-willful failure to timely make Report of Foreign Bank and Financial Account).

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Other foundations may have advisors, but the advisors may lack "competent professional investment advice, legal counsel knowledgeable in the complexities of the private foundation regulatory regime, or accounting services familiar with the private foundation legal regime."[177] If § 4962 were extended to § 4941 violations, issues regarding reliance on inaccurate advice would surely arise.

The *Penalty Handbook* devotes an entire section to "Erroneous Advice or Reliance."[178] The *Penalty Handbook* instructs agents to ask whether the taxpayer is relying on specific advice received from someone else, whether orally or in writing."[179] Again, the regulations regarding reasonable cause under § 6664 for failure to satisfy § 6662 give somewhat more specific guidance. These regulations include "whether a taxpayer has reasonably relied in good faith on advice (including the opinion of a professional tax advisor) as to the treatment of the taxpayer" as a factor in determining reasonable cause.[180] The regulations caution that "reliance may not be reasonable or in good faith if the taxpayer knew, or reasonably should have known, that the advisor lacked knowledge in the relevant aspects of Federal tax law.[181]

Given the specialized nature of the private foundation taxes, determining whether a tax advisor has the requisite expertise could be difficult. As a leading treatise explains, reasonable cause in the context of reliance on a professional tax advisor requires a taxpayer to have "retained a competent tax advisor, supplied the advisor with relevant information, and relied on the advisor's advice in good faith."[182] Regarding competence. the

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[177] Fishman, *supra* note 16, at 289.

[178] I.R.M. 20.2.1.3.2.2.1, 20.1.1.3.2.2.5.

[179] *Id.*

[180] Treas. Reg. § 1.6664-4(c).

[181] *Id. See* Hristov v. Comm'r, T.C.M. 2012-147 (reliance by taxpayer on tax professional not reasonable if taxpayer knows professional lacks expertise in specific area of tax law).

[182] SALTZMAN & BOOK, *supra* note 169, at ¶ 7B.03[3][a]. The treatise further explains that the interpretation of reasonable cause in the current accuracy provision, adopted at the end of 1989, has been carried over from the interpretation of the reasonable cause exception in the former stand-alone, substantial understatement penalty under the 1986 Code. There, the reasonable exception had been interpreted to require the exercise of ordinary business care and prudence. Ordinary business care and prudence, in turn, required demonstration of the three factors quoted in the text. *Id. See* Neonatology v. Comm'r. 115 T.C. 43 (2000), *aff'd* 299 F.3d 221 (3d Cir. 2002). Note that reliance on professionals may

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Supreme Court has observed, "Most taxpayers are not competent to discern error in the substantive advice of an accountant or attorney. To require the taxpayer to challenge the attorney, to seek a 'second opinion' . . . would nullify the very purpose of seeking the advice of a presumed expert in the first place."[183] Many cases have excused the § 6662 penalty based on reliance of an experienced lawyer or accountant, even when the tax professional gave erroneous advice.[184] Such might be the case for small foundations relying on tax professionals with experience in areas of tax other than private foundations if rules like those under § 6662 were adopted as part of an amended 4962.[185]

In sum, careful amendment of § 4962 could offer relief in some cases of § 4941 self-dealing. Simply amending the first-tier abatement permitted under § 4962 to include self-dealing under § 4941, however, will not make a meaningful difference to disqualified persons. Effective and useful guidance under an amended § 4962, whether in the statute itself or regulations, requires an interpretation of reasonable cause like that found under § 6664, rather than the § 6651 interpretation endorsed in the 1992 EO CPE chapter.

This consideration of § 4941, however, also offers support for a far more sweeping change than simply amending § 4962. Excise taxes on § 501(c)(3) organizations, including § 4941, aim at regulation. Evidence of their success under current conditions is thin at best. Other observers of the exempt

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be deemed unreasonable when a conflict of interest exists. *See* I.R.M. 29.1.5.7.4; SALTZMAN & BOOK, *supra* note 169, at ¶ 7B.03[3][a][ii]; Castro, *supra* note 172. *See also* text at footnote 10 and cases listed in footnotes 14–30.

183 United States v. Boyle, 469 U.S. 241, 251 (1985). The case held that reliance on an agent did not excuse failure to file a timely tax return. The Court distinguished reliance on an advisor to make a timely filing from relying on an advisor regarding a matter of tax law.

184 *See, e.g.*, Romanowski v. Comm'r, T.C.M. 2013-55 (2013); Blackwood v. Comm'r, T.C.M. 2012-190 (2012); Litman v. United States, 78 Fed. Cl. 90 (Ct. Fed. Cl. 2007). *See generally* SALTZMAN & BOOK, *supra* note 169; Castro, *supra* note 172. For a case in which a court holds that taxpayers met the requirements of reasonable cause and no willful neglect in connection with substantiation of a charitable contribution under § 170(f)(11)(A)(ii)(II) when the taxpayers relied on their long-time certified accountant erroneously advising them that an appraisal was qualified, see *Crimi v. Comm'r*, T.C.M. 2013-51, 105 T.C.M. (CCH) 1330 (2013).

185 Fishman, *supra* note 16, longs for foundation counsel and accounting firms to be authorized to practice before the IRS. As a variation of this suggestion, regulations could perhaps specify requirements for "qualified foundation advisors," somewhat like those for qualified appraisers, see Treas. Reg. § 1.170A-17, and deem reliance on qualified foundation advisors to be per se reasonable.

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organization sector have detailed many other difficulties the IRS faces in its duties vis-à-vis exempt organizations, an area of the tax law that aims at regulation rather than revenue-raising.[186]

All of these considerations lead me to join those urging that we consider removing oversight of § 501(c) organization, at least in part, from the IRS. One option would be to establish, a new federal regulatory agency completely separate from the IRS in order to increase accountability, develop new forms of regulation, and focus the need for funding.[187] Such a radical change, I believe, is unrealistic. But, as others have explained in more detail than I will repeat here,[188] a new self-regulatory organization (SRO) seems possible. Such an SRO, of course, could take different forms. Marc Owens models his proposed SRO on the Financial Industry Regulatory Authority (FINRA) and its relationship with the SEC.[189] He envisions a body with mandatory membership, with implementation and enforcement authority and the ability to impose direct sanctions.[190] Professor Helge would go further, proposing a new entity that "would be a self-funded, independent and proactive regulator" designed to serve the dual purposes of curbing abuses and educating charitable managers."[191]

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[186] *See* Marcus S. Owens, *Charity Oversight: An Alternative Approach*, COLUM. ACAD. COMMONS (2013), https://academiccommons.columbia.edu/doi/10.7916/D8154F1D; Terri Lynn Helge, *Policing the Good Guys: Regulation of the Charitable Sector through a Federal Charity Oversight Board*, 19 CORNELL J. LAW & PUB. POL'Y 1 (2009); *see also* Mayer, *supra* note 57.

[187] *See* Mayer, *supra* note 57, at 115–16.

[188] *See* sources cited *supra* note 186.

[189] *See* Owens *supra* note 186. FINRA is nonprofit organized by Congress to regulate the brokers and brokerage firms who are its members. Its Board of Governors consists of twenty-four industry and public members, of which seven are chosen by members and thirteen designated as public members. The SEC approves standards and rules promulgated by FINRA. FINRA can issue sanctions and levy fines. Members can appeal its enforcement actions to the SEC and then to federal courts. *See* FINRA, About FINRA, http://www.finra.org/about. For an endorsement of Owens's approach see JOEL L. FLEISHMAN, THE FOUNDATION: A GREAT AMERICAN SECRET 186, 257–58.

[190] *Id.*

[191] Helge, *supra* note 186, at 70. She models her proposed agency on the Public Company Accounting Oversight Board (PCAOB). *Id.* "The PCAOB is a nonprofit corporation established by Congress to oversee the audits of public companies in order to protect investors and the public interest." *See About PCAOB*, PUB. CO. ACCOUNTING OVERSIGHT BD., https://pcaobus.org/About (last visited June 26, 2020). It has authority to investigate and discipline public accounting firms for violations of the Sarbanes-Oxley Act of 2002. The five members of its board are appointed to staggered five-year terms by the SEC, after consultation with the chair of the Board of Governors of the Federal Reserve and the

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Whether "a new self-regulatory body that operates under the close supervision of the IRS"[192] would in fact improve oversight of the sector, including enforcement of private foundation self-dealing, is uncertain at best. Nonetheless, this study of § 4941 leads me to endorse Professor Roger Colinvaux's suggestion that Congress convene a panel to study how best to structure federal oversight of exempt organizations.[193] The current state of enforcement of § 4941 offers but one example of the a need not only for greater enforcement, but also for consideration of more fundamental change.

Secretary of the Treasury. It is subject to SEC oversight, including approval of PCAOB's rules, standards, and budget. *Id.* Thus, I see her proposal as an SRO and not a new agency.

[192] Mayer, *supra* note 57, at 122.

[193] Roger Colinvaux, *Fixing Philanthropy: A Vision for Charitable Giving and Reform*, 162 TAX NOTES 1007, 1013 (2019).

APPENDIX A

Table A
Data from Forms 4720 Reporting Section 4941 Excise Tax

Year	# of returns	Dollars Reported	Mean Amount Reported	# PFs	% of PFs Involved in Reported 4941 Tax
2015	239	208,6082	8,728	99,683	0.24
2014	193	1,679,288	8,701	97,484	0.2
2013	113	1,135,401	10,048	95,121	0.12
2012	206	2,997,191	14,549	93,542	0.22
2011	189	2,875,959	15,217	92,900	0.2
2010	201	1,005,447	5,027	93,436	0.22
2009	261	3,097,030	11,866	91,535	0.29
2008	178	1,146,999	6,444	90,850	0.2
2007	203	1,721,285	8,480	84,613	0.24
2006	186	2,248,367	12,088	81,850	0.23
2005	185	3,342,174	18,066	79,535	0.23
2004	162	658,254	4,063	76,897	0.21
2003	157	566,881	3,611	76,348	0.2

Data from IRS, Statistics of Income, Charitable and Exempt Organizations Statistics,
https://www.irs.gov/statistics/soi-tax-stats-charitable-and-exempt-organizations-statistics
Only data from 2003-2015 available.

The percentage of PFs involved in transactions subject to the 4941 tax assumes one Form 4720 per private foundation. This assumption is unlikely to be accurate. It is likely that more than one individual, such as several disqualified persons as well as knowing managers, file for the same self-dealing transaction. Given the definition of taxable period, an individual may well file Form 4720 for several years for the same transaction. If these conditions hold, the percentage of PFs involved in such transactions would be even smaller.

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APPENDIX B

Table B
Data from Forms 4720 Reporting Section 4958 Excise Tax

Year	# of Returns	Dollars Reported	Mean Amount Reported	# of Applicable EOs	% of Applicable EOs Involved in Reported 4958 Tax
2015	11	28,3739	25,794	1,169,019	*
2014	16	171,788	10,737	1,169,042	*
2013	-	-	-	-	
2012	25	1,156,893	46,276	1,081,491	*
2011	11	72,240	6,527	1,084,612	*
2010	26	831,052	4,155	1,326,432	*
2009	13	275,835	21,218	1,283,942	*
2008	26	158,004	6,077	1,231,559	*
2007	10	42,372	4,237	1,178,597	*
2006	8	186,215	23,277	1,117,496	*
2005	5	123,856	24,771	1,102,504	*
2004	8	1,467	183	1,071,661	*
2003	5	123,856	24,771	1,025,091	*

Most data from IRS, Statistics of Income, Charitable and Exempt Organizations Statistics, https://www.irs.gov/statistics/soi-tax-stats-charitable-and-exempt-organizations-statistics
Only data from 2003-2015 available.

# of Applicable EOs calculated by adding # of 501(c)(3)s (including PFs) and 501(c)(4)s from Table 25 of IRS annual Data Books, https://www.irs.gov/statistics/soi-tax-stats-all-years-irs-data-books, and subtracting the number of PFs based on SOI data.

SOI has no entries for this category for 2013.

SOI gives the same numbers for 2003 and 2005.

The percentage of applicable EOs involved in transactions subject to 4958 tax assumes one Form 4720 per applicable EO. As explained in the note under Table A, that assumption is likely not accurate and the number involved is likely smaller. But even with the assumption of one form per entity assumption, the percentage involved is negligible, rounding to .00%.

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