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May 22, 1987

Ms. Dorothy A. Johnson
President
Council of Michigan Foundations
Suite 3
One South Harbor Avenue
P.O. Box 599
Grand Haven, MI 49417

Dear Ms. Johnson:

You have asked for our opinion on the federal tax treatment of expenditures by the Council of Michigan Foundations ("CMF") in connection with a proposed effort to persuade the Michigan Legislature to create a state income tax credit for contributions to community foundations. CMF is exempt from federal income tax under section 501(c)(3) and is a public charity described in sections 509(a)(1) and 170(b)(1).¹ CMF has elected to have its legislative activities governed by the provisions of sections 501(h) and 4911. It has a substantial number of community foundations as members, but it is itself not a community foundation.

The effort you have in mind is outlined in your letter to us of April 27, 1987. It would include hiring a professional lobbyist, preparation of materials concerning the proposed credit, contacts with members of the Legislature and with other charities, and communications with CMF's own members.

¹ All statutory references are to the Internal Revenue Code of 1986, unless otherwise stated.

Under section 501(h), CMF is permitted to expend up to 20% of its total budget (up to \$1,000,000) for activities that are treated as "attempts to influence legislation." Expenditures for attempts to influence the opinions of the general public (so-called "grassroots" efforts), as contrasted with contacts with the legislators, relevant executive branch officials, and their staffs, are subject to a sublimit of a quarter of the overall limit.

Special rules apply to membership organizations, like CMF. Communications with members that are strictly informative, and do not encourage members either to contact legislators or the general, non-member public, do not count against the limits at all. Communications that urge members to contact legislators or their staffs count only against the overall total. Only those communications with members that urge the members to seek to persuade others in the general public to support (or oppose) legislation count as "grassroots" lobbying, charged against the lower limit.

In addition, certain activities that are, broadly, legislative in character are permitted, without regard to the limitations. The exemption that is most relevant here is the so-called "self-defense" rule. This rule exempts from the limitations all "direct" lobbying that an organization undertakes "with respect to a possible decision of [a legislature] which might affect the existence of the organization, its powers and duties, tax-exempt status, or the deduction of contributions to the organization". Sec. 4911(d)(2)(C). "Grassroots" activity on such measures still counts against the lower limit. The exemption applies only to "direct" activity, i.e., communications with legislators, executive branch officials, and their staffs. However, because communications with members urging them to engage in "direct" lobbying count as "direct" lobbying by the organization, such membership communications are also exempt from the limits.

In our opinion, the effort proposed by CMF falls within the "self-defense" rule, i.e., the proposed tax credit² measure at issue qualifies as "a possible decision of [the Michigan Legislature] which might affect the ... tax exempt status, or the deduction of contributions" to CMF, and hence, "direct" lobbying

² Clearly, a "credit" for gifts to an organization is an aspect of the tax status of the organization and of the treatment of contributions to it, even though not technically a "deduction." There is no evidence that Congress intended to treat credits and deductions differently for purposes of the "self-defense" exemption.

in connection with that effort is not "an attempt to influence legislation" within the meaning of the statute.

The "self-defense" exception applies to the activity of CMF undertaken to promote a state income tax credit for contributions to certain tax-exempt members of CMF, but not to CMF itself. The initial version of the 1976 legislation said explicitly that the "self-defense" exception covered the tax-exempt status and contribution deductibility, not only of an organization itself, but of its members, if those members were themselves section 501(c)(3) organizations. H.R. 13500, 94th Cong., 2d Sess. § 2. Although this explicit language was omitted from the bill as passed, both Treasury and Joint Committee staff people stated at the time that the "self-defense" exception would still apply to "member-defense." A rule to that effect was included in the proposed regulations published in November 1986. Prop. Regs. § 56.4911-3(d)(3). Although the proposed regulations have no legal force as such, until issued in final form, there has been no controversy about that provision, and there is every reason to expect it to be included in the final regulations, when they are eventually published.

We understand that this interpretation of the scope of the "self-defense" provision is shared by such organizations as the Council on Foundations, Independent Sector, and United Way of America, which routinely lobby on tax matters of concern to their exempt members.

In summary:

1. Direct approaches to legislators, their staffs, and executive branch officials by CMF directors, staff or outside consultants or lobbyists would not be lobbying at all as defined in the statute, and would not count against the CMF ceiling on "direct" lobbying.

2. Contacts with CMF members would count against the "grassroots" ceiling only to the extent that they were urged to communicate about the proposed credit with grantees or others outside their own organizations. (The self-defense exception means that CMF communications with members that urge the members to contact legislators directly do not count as lobbying.)

3. Contacts with non-members would count as grassroots lobbying.

You also asked about the effect of the project on the treatment, under section 4945, of grants to CMF from private foundations. There is a strong argument that grants from private foundations to CMF earmarked for the state tax credit project

would not be taxable expenditures under section 4945 by the grantors since the bulk of the activity is not, for tax purposes, treated as lobbying by CMF, so long as the individual foundation's grant does not exceed the amount of the tax credit project budget allocated for activities other than grassroots lobbying.

A simpler approach, however, would be for foundation grantors to rely on the so-called McIntosh ruling, IRS Priv. Ltr. Rul. 78-10-041 (Dec. 8, 1977), under which general support grants to CMF from private foundations can be used for CMF's lobbying without making the payments taxable expenditures by the grantor private foundations.

As to CMF's limits, we understand that CMF has a total annual budget of about \$400,000, all of it for activities that qualify as "exempt purpose expenditures." That being the case, CMF's overall lobbying limit is \$80,000 and its grassroots limit is \$20,000. (To the extent the tax credit project is financed by specially raised funds, so that it is additive to the projected budget, it increases the base. Sec. 4911(e)(1)(B)(ii). For example, if CMF raises the \$65,000 projected budget for the credit project, that would increase the ceilings by \$13,000 and \$3250, for overall and grassroots, respectively. In that case, the applicable limits would be \$93,000 for overall lobbying and \$23,250 for grassroots.

If you have any questions about this matter, please let me know.

Sincerely yours,



Walter B. Slocombe

WBS/kkg

Council of Michigan Foundations

ONE SOUTH HARBOR AVENUE
P.O. BOX 599
GRAND HAVEN, MI 49417
PHONE 616/842-7080

Date: May 27, 1987

Memo to: BOARD OF TRUSTEES

From: Government Relations Sub-Committee on
Community Foundation State Tax Credit
Judith S. Hooker, Chairman
Willard J. Hertz
John E. Hopkins
Dorothy A. Johnson
Ranny Riecker
Robert D. Sparks

Re: Community Foundation State Tax Credit Proposal

At the request of the Board of Trustees, following the February 26, 1987 board meeting, a sub-committee met to review the issues and strategy surrounding the implementation of the proposed community foundation state tax credit and to formulate a recommendation for the Board on how, if at all, to proceed with the strategy. The Sub-Committee was composed of individuals representing the Government Relations Committee and the community foundation membership.

Historical Background

In the spring of 1986, Jack Hopkins, Associate Director of the Kalamazoo Foundation, proposed that the Council of Michigan Foundations (CMF) investigate the feasibility of a tax credit for individual and corporate contributions to a community foundation in the State, similar to that currently in place for educational institutions, libraries and public broadcasting stations. The 27 CMF community foundation members were surveyed as to their interest and there was unanimous and enthusiastic agreement to proceed with the investigation.

The Government Relations Committee, then chaired by James M. Richmond, Vice President, W.K. Kellogg Foundation and CMF Trustee, prepared five drafts of the case statement. The statement was presented to the Board of Trustees at the June 6, 1986 meeting and adopted. The Board received a progress report at the November 6, 1986 meeting, along with a further draft of the statement. Meetings were held with the Governor's staff who expressed interest in the idea. Public Sector Consultants, Inc. provided counsel on the statement and were instrumental in seeing that the idea was incorporated in the Governor's State of the State Address delivered February 4, 1987.

"The State Treasurer will evaluate the feasibility of a state income tax credit for those who donate to community foundations. If this tax credit is determined to be fiscally prudent, it could encourage individuals who wish, through voluntary efforts, to improve the quality of life in their own communities."

At the February 13, 1987 Board of Trustees meeting, questions were raised as to the strategy to be used to seek passage of the legislation, the opinions of other Michigan public charities and whether or not CMF or its members would be effected by the IRS lobbying regulations.

Information

In preparation of the Sub-Committee's deliberations, Public Sector Consultants, Inc. was engaged to review the case statement (Att. 6a) and to prepare a strategy paper (Att. 6b).

Public Sector Consultants, Inc. was compensated on an hourly basis for their services. Mrs. Johnson informed them that a retainer was not appropriate for CMF, as was discussed at the February board meeting. Any work done by a consultant for the project will be done on a contractual basis.

Recommendations

The Sub-Committee recommends the following Board action:

1. The CMF Board of Trustees reaffirms the board policy to seek a tax credit for contributions to community foundations.
2. CMF seek a legal opinion on the IRS lobbying regulation's effect on CMF, a public charity and its private foundation members who may want to make a grant to assist the effort.

Result: Legal opinion, prepared by Caplin & Drysdale, Walter Slocombe (Att. 6c). In summary, CMF could proceed with the recommended strategy and seek grants from all Members, including private foundations under the described terms without any problem for CMF or Members. The legal opinion would be provided with all proposal requests.

3. Association with Public Sector Consultants, Inc. and whatever other consultants needed to secure passage of the community foundation state tax credit legislation.

To implement the above strategy it is recommended that CMF seek special project funds up to \$65,000. The funds will be raised from members who have an interest in the growth of community foundations. The funds will be used to pay for consulting assistance as recommended by the Government Relations Sub-Committee on the Community Foundation State Tax Credit. Commitments will only be made after special purpose funds have been secured.

The policy to seek a tax credit for contributions to a community foundation is consistent with CMF's purpose to increase private and community foundation and corporate grantmaking resources in the State of Michigan.

**Public Sector Consultants, Inc.**

April 16, 1987

MEMORANDUM

TO: The Council of Michigan Foundations

FROM: Bill Rustem

SUBJECT: TAX CREDIT STRATEGY

Legislative Process

Bills to amend Public Act 228 of 1975 (single business tax) and Public Act 281 of 1967 (income tax) should be introduced in the Senate because the issue of tax credits is more likely to receive favorable consideration from a Republican-controlled body. Passage by the Senate will provide the impetus for favorable action in the House, where Democrats are in control.

The bills will be referred to the Senate Committee on Finance. Three members (a majority) of that committee have strong community foundations in their districts:

| | |
|---------------------------------|---|
| Senator Norm Shinkle (R), Chair | Community Foundation of Monroe County (also La-Z-Boy Chair Foundation and Monroe Foundation Trust) |
| Senator Richard Posthumus (R) | Grand Rapids Foundation |
| Senator Lana Pollack (D) | Ann Arbor Area Foundation |

Senator Posthumus should be asked to be the prime sponsor. He is the first choice because of his Senate leadership position (assistant majority leader) and because the community foundation in his district is the oldest and second-largest in Michigan. He also is very close to Senator John Engler, the majority leader, and is majority vice-chair of the Finance Committee.

Senator Shinkle chairs the Finance Committee and has a reputation for articulating Republican positions on tax matters. He should be asked to be a co-sponsor. Senator Pollack is minority vice-chair of the committee, and her co-sponsorship, as a Democrat, could help attract bi-partisan support.

As soon as the bills are referred to committee, all five members [the other two are freshmen Doug Carl (R-Utica) and Christopher Dingell (D-Trenton)] should be contacted by letters and calls from the CMF urging support. The letters should be accompanied by a brief (one-page) summary of the issue. Longer summaries are less likely to be read.

The governor's legislative liaison (Stan Fedewa) and the state treasurer (Bob Bowman) will be kept advised by Public Sector Consultants (PSC). We will

make sure that our estimate of the financial effect on the state's tax revenue is in line with the state treasurer's.

While Senate action is progressing, it will be advisable to monitor House action, watching for other bills to amend the single business and income tax acts.

As such bills are introduced (several already have been), it will be necessary to develop a legislative strategy for the House, based in part on where the issues are in the Senate. It is possible that the CMF's tax amendments could be added in the Senate to House-passed bills so that the only House action required would be concurrence in Senate amendments.

Representative Lynn Jondahl, who chairs the House Taxation Committee, should be advised early of the CMF's intent and convinced of its merit because his support is critical. An East Lansing Democrat, Jondahl is the leading spokesperson for Democratic--and the governor's--interests on tax matters. He is serving his eighth term and is an ordained minister.

Policy Decision

A key policy decision for the CMF is whether to seek a personal income tax credit or a deduction for contributions.

A deduction involves a subtraction of the contribution from the income tax base. For example, a \$100 contributor could subtract that amount from his/her net taxable income; a \$100 contribution multiplied by the state income tax rate (i.e., 4.6 percent) would result in a tax reduction of \$4.60.

The tax deduction option against personal income tax should be rejected. As described above, under a tax deduction, a contribution of \$100 would result in a net cost to the taxpayer of \$95.40 (\$100 minus \$4.60). An income tax deduction simply does not provide sufficient incentive to encourage significant gifts.

Tax credits are much more important to the taxpayer because they are subtracted from tax owed, rather than from the tax base. Using again the example of a \$100 contribution, the contributor could subtract \$100 from tax owed, rather than the \$4.60 in the example above.

Tax credits come in two forms, refundable and nonrefundable. An example of a refundable tax credit is the homestead property tax credit, in which a taxpayer who does not owe the State any income tax will get a refund check in the amount of the credit from the State. An example of a nonrefundable tax credit is that allowed for a contribution to a public broadcasting station. In this instance, a contributor who does not owe any state income tax cannot get credit for the contribution because there is nothing from which to subtract it.

We recommend that the CMF seek a nonrefundable public contribution credit against the state income tax, as is allowed for contributions to the Michigan Colleges Foundation. (This credit would be separate from the credit currently available for contributions to colleges and universities, libraries, and the Michigan Colleges Foundation.) Under such a credit, the contributor computes the credit three ways and is allowed to take whichever amount is smallest:

- A. 50 percent of the contribution reported on line 18a, or
- B. 20 percent of the tax on line 16 of MI 1040, or
- C. \$100 (\$200 for a married couple filing a joint return).

Option A would permit a gift of \$100 at a cost of only \$50 to the contributor. The nonrefundable provision means that a taxpayer who does not have any state tax liability cannot receive credit. This would reduce the cost to the State. It also is compatible with the governor's State of the State message in which he refers to evaluation of the feasibility "of a state income tax credit for those who donate to community foundations." It has the further advantage of being based on precedent in the existing tax law (for contributions to the Michigan Colleges Foundation and other public purposes). PSC will research tax law in other states for similar precedents. It usually is easier to sell a concept to the legislature if it is based on precedent either in Michigan or other major industrial states.

By current law, only a nonrefundable credit is allowable against the SBT. We recommend that the CMF seek legislation for a similar, but separate, credit to permit contributions to community foundations to the extent allowable for contributions such as those to public broadcasting stations: up to 5 percent of the tax liability or \$5,000, whichever is less.

Other Organizations

We need to prevent a "bandwagon" effect. As the CMF proposals start through the legislative process, if other organizations, such as United Way, appear before legislative committees to ask that they be included, our effort probably will fail. What would happen could be compared to loading a boat with cargo: if the cargo is light, the boat will sail; if too much is loaded on, the boat will sink. There will be much greater chance of success if only one organization leads the way. If the CMF can blaze the trail alone, not only will the CMF benefit, but the process will also be made much easier for other organizations to follow.

We suggest that the CMF host a meeting with other major organizations to seek agreement that other organizations will not try to be included in the bills, but will wait until they are passed. In subsequent years, other organizations can seek inclusion, perhaps with the CMF support. If all organizations seek inclusion the first time, one of two things probably will happen: (1) the cost to the State will be considered to be prohibitive and/or (2) the legislative committees will bog down in hearings on the matter and go on to other issues.

The CMF could pledge its support for others' future legislative efforts in exchange for an agreement that the CMF be permitted to make the legislative journey alone this year. Since only about one bill in six becomes law, the journey will be hazardous enough without further impediments.

We suggest that the CMF consider the services of a lobbyist. While Public Sector Consultants does not engage in legislative lobbying, we do develop public information or advocacy programs for clients. We also will be pleased to recommend a lobbyist whom we feel can best serve the CMF's interest. We have worked with several on a number of projects in the past and can recommend with confidence an individual or firm that will meet the CMF's high standards of integrity and capability. We will be happy to cooperate with a lobbying firm and supervise its work in your behalf.

Prepared by
PUBLIC SECTOR CONSULTANTS, Inc.

for the
The Council of Michigan Foundations

COMMUNITY FOUNDATIONS: THE
CASE FOR TAX CREDIT

DRAFT

April 16, 1987

COMMUNITY FOUNDATIONS: THE CASE FOR TAX CREDIT

PROPOSAL

Amend Chapter 1 of Public Act 228 of 1975 (entitled Single Business Tax Act) and Chapter 5 of Public Act 281 of 1967 (entitled Income Tax Act of 1967) by adding new sections that would permit contributors to community foundations to receive tax credits for their contributions. The new credit would be identical to that allowed for contributions to public broadcast stations, public libraries, college foundations, and institutions of higher learning, but would be claimed separately.

WHAT IS CURRENT LAW?

Under current law, the charitable tax credit allows taxpayers to take a tax credit equal to 50 percent of the aggregate amount of their charitable contributions to (a) public broadcast stations not affiliated with a college or university, (b) public libraries, (c) institutions of higher learning located in Michigan, (d) the Michigan Colleges Foundation, and (e) nonprofit corporations, funds, foundations, trusts, or associations operated exclusively for the benefit of Michigan institutions of higher learning. The credit cannot exceed \$200 for an individual filing a joint return and \$5,000 for a business.

WHAT IS A COMMUNITY FOUNDATION?

A community foundation is a public charity that receives and distributes funds to serve the social, cultural, and education needs of a defined geographic area. Each foundation has two major missions: to establish endowments to serve the local community now and in the future and to address community needs by providing leadership and resources. Community foundations have been instrumental in helping established institutions such as hospitals, museums, schools, institutions of higher education, and social agencies meet their goals and try innovative approaches to solve persistent local problems.

Today, community foundations are future-oriented, umbrella philanthropic organizations. They respond to local needs in a variety of ways that range from providing for neighborhood playground equipment and funding symphonies to supporting economic development projects and establishing endowments for diseases such as Alzheimer's.

Unlike the United Way, which provides annual operating support to specific agencies, community foundations provide both immediate and long-term support to an unlimited number of programs, projects, and agencies. Their governing structure allows them to respond quickly to the changing needs of the communities they serve, yet, at the same time, provide ongoing support to programs warranting continued public attention. For example, the Kalamazoo Foundation recently implemented the Hazelton Cork Substance Abuse Prevention Project in direct response to the nationwide and local concern about drug abuse. This pilot program educates students in five area high schools about the dangers of substance abuse. Another beneficiary of the Kalamazoo Foundation is the Domestic/Sexual Assault Program housed at the Young Women's Christian Association. This program, which has received over \$295,000 since 1976 from the Kalamazoo Foundation, provides temporary shelter, food, and support services to abused women and children.

Ultimately, it is the structure and the earning power of their endowments that make community foundations unique. When donors contribute, they can make unrestricted gifts or earmark their contributions for one or more programs focusing on a particular issue. This gives the donor control over how his/her donation is used. Contributions are then pooled with like donations, thus maximizing the benefit of the donation by increasing its earning power.

At present in Michigan, there are thirty-four community foundations, with assets totaling over \$150 million and annual grantmaking exceeding \$10 million (see Exhibit 1). In the Lower Peninsula, every major metropolitan area except Lansing is served by a community foundation; in the Upper Peninsula there are no community foundations. At present, efforts are under way in the Upper Peninsula and in Lansing to establish such foundations (see Exhibit 2).

EXHIBIT 1

LOCATION, ASSETS, AND ANNUAL GRANTS OF
COMMUNITY FOUNDATIONS IN MICHIGAN

| <u>Name</u> | <u>Location</u> | <u>Total Assets</u> | <u>Annual^a Grants</u> |
|--|---------------------|---------------------|--------------------------------------|
| Albion Civic Foundation | Albion | \$ 670,000 | \$ 44,000 |
| Ann Arbor Area Foundation | Ann Arbor | 2,057,942 | 89,957 |
| Greater Battle Creek Foundation | Battle Creek | 1,943,515 | 72,056 |
| Bay Area Community Foundation | Bay City | 438,940 | 32,995 |
| Berrien Community Foundation, Inc. | St. Joseph | 1,554,572 | 26,091 |
| The Colon Foundation | Colon | 8,904 | 53 |
| Community Foundation of Southeastern Michigan | Detroit | 6,151,976 | 538,230 |
| Fenton Community Foundation | Fenton | 10,510 | 392 |
| Flint Area Health Foundation | Flint | 5,361,901 | 251,930 |
| The Flint Public Trust | Flint | 2,669,990 | 88,348 |
| Greater Frankenmuth Area Community Foundation | Frankenmuth | 199,009 | 15,770 |
| Fremont Area Foundation | Fremont | 23,533,783 | 939,316 |
| Grand Blanc Community Foundation | Grand Blanc | 246,910 | 22,064 |
| Grand Haven Area Community Foundation, Inc. | Grand Haven | 2,130,964 | 36,244 |
| Grand Rapids Foundation | Grand Rapids | 36,778,578 | 2,829,829 |
| Grosse Pointe Farms Foundation | Grosse Pointe Farms | 295,602 | NA |
| Grosse Pointe Park Foundation | Grosse Pointe Park | NA | NA |
| Holland Community Foundation, Inc. | Holland | 467,013 | 113,791 |
| The Jackson Foundation | Jackson | 1,967,066 | 175,125 |
| Kalamazoo Foundation | Kalamazoo | 52,688,097 | 4,272,786 |
| Leelanau Township Community Foundation | Northport | 198,604 | 1,296 |
| Marcellus Community Foundation, Inc. | Marcellus | 3,000 | 1,000 |
| Marshall Civic Foundation | Marshall | 56,929 | 2,200 |
| The Midland Foundation | Midland | 6,794,495 | 729,519 |
| Community Foundation of Monroe County | Monroe | 97,096 | 7,176 |
| Muskegon County Community Foundation | Muskegon | 13,196,894 | 562,863 |
| Northeast Michigan Community Foundation | Alpena | 744,526 | 107,778 |
| Community Foundation of St. Clair County | Port Huron | 166,028 | 17,389 |
| Greater Rochester Area Community Foundation | Rochester | 18,047 | 14,169 |
| Saginaw Community Foundation | Saginaw | 561,180 | 20,300 |
| Shiawassee Foundation | Owosso | 24,103 | 1,388 |
| Three Rivers Community Foundation | Three Rivers | NA | NA |
| Traverse Area Foundation, Inc. | Traverse City | 26,257 | 62,231 |
| Zeeland Community Foundation, Inc. | Zeeland | 181,783 | 3,675 |

SOURCE: Council of Michigan Foundations, Grand Haven, Michigan.

NA=Not available.

^a Reporting years vary.

EXHIBIT 2
COMMUNITY FOUNDATIONS IN MICHIGAN



SOURCE: Council of Michigan Foundations, Grand Haven, Michigan.

WHY SHOULD CONTRIBUTORS TO COMMUNITY FOUNDATIONS BE ELIGIBLE FOR CHARITABLE TAX CREDIT?

Community foundations develop and support many valuable programs that otherwise would have to be provided by state or local government. For example, the Jackson Foundation funds an intensive job retraining program to help displaced homemakers enter the job market. The Community Foundation for Southeastern Michigan helped the Warren/Connor Development Commission initiate three neighborhood crime prevention programs. The Holland Community Foundation purchased two telecommunication devices for use in local agencies and organizations to inform and assist deaf and hearing-impaired persons. And the Midland Foundation provides emergency heating and plumbing repair assistance to families in need. These programs all provide valuable services that benefit communities immensely without any cost to state or local government.

Community foundations also develop and support innovative programs that contribute to the state's future economic stability. Three examples are

- an eleven-part seminar series funded by the Berrien Community Foundation, Inc., to strengthen and make more effective and efficient nonprofit organizations in southwest Michigan, many of which use state funds;
- Battle Creek Unlimited, funded by the Greater Battle Creek Foundation, which has been very successful in persuading Japanese and German industries to build plants in Battle Creek (two from Germany and five from Japan to date); and
- the Muskegon Heights Small Business Development Program, partially funded by the Muskegon County Community Foundation, to identify people in the community who have management potential and educate and assist them in starting and operating small businesses. Within two years, this county-wide program hopes to establish 25-30 new businesses and strengthen or expand 50-75 existing businesses.

Finally, by its very nature and location, a community foundation can accurately assess the needs of its community and determine which programs will be of most benefit. For example, the unemployment rate in Calhoun County is well above average. The Greater Battle Creek Foundation, recognizing this special need in its service area, established a local Economic Development Fund to generate jobs by encouraging development in downtown Battle Creek and helping community members obtain newly generated jobs.

These programs, which are excellent examples of how community foundations help the state without state government dollars, are only a few of the innovative programs being implemented by community foundations around Michigan. By including community foundations among the organizations eligible for charitable tax credits, the benefits gained would increase substantially while state government would experience only a slight annual revenue decrease. Public Sector Consultants estimates that the first-year cost to the state general fund would be \$1.5 million to \$2.5 million. A more precise estimate is difficult because we do not know how this credit will affect contributors' behavior or how federal tax reform will affect charitable giving in general.

Our estimate is that the proposed credit would result in a \$3 million to \$5 million--or a 2 to 3 percent--increase in total contributions to community foundations in the first year of the program. In subsequent years, community foundations could gain a great deal more if sufficient attention is given to the need to market the new tax credit.

The tax credit for public broadcast station donations became effective in 1979. Five years later, the total number of contributors to public broadcast stations had increased 83 percent and donations had increased 105 percent. (See Exhibit 3.) A comparable increase would raise the number of community foundation donors from 10,060 in 1986 to 18,410 in 1991.

EXHIBIT 3

MICHIGAN CHARITABLE CONTRIBUTION TAX CREDIT

| <u>Tax Year</u> | <u>Number of Credits</u> | <u>Total Credits</u> | <u>Average Credit</u> |
|-----------------|--------------------------|----------------------|-----------------------|
| 1979 | 99,200 | \$4,884,500 | \$49.24 |
| 1980 | 134,300 | 6,619,000 | 49.29 |
| 1981 | 154,700 | 7,873,000 | 50.89 |
| 1982 | 182,700 | 9,403,500 | 51.47 |
| 1983 | 193,800 | 10,367,800 | 53.50 |
| 1984 | 181,300 | 10,032,700 | 55.34 |

SOURCE: Michigan Department of Treasury, Taxation and Economic Policy Office.

NOTE: A tax credit for contributions to public libraries, Michigan institutions of higher learning, the Michigan Colleges Foundation, and other nonprofit corporations, funds, foundations, trusts, or associations operated exclusively for the benefit of institutions of higher learning was written into state law in 1968. In 1979, the state law was amended to allow credit for contributions to public broadcast stations.

It must be said that there is no guarantee that the experience with the tax credit for public broadcast stations would be paralleled by the proposed credit community foundations, since the average contribution to a community foundation is presently much larger than the average contribution to a public broadcast station.

Consideration of the proposal to include community foundations in the charitable tax credit is very timely. The role of the community foundation is expanding in response to reductions in federal support to communities and the trend toward returning responsibility and control of local programs to cities and states. Legislation such as the Gramm-Rudman-Hollings act and proposed budgetary policy shifts threaten to further reduce federal and state support for local human, social, cultural, and economic needs. Therefore, social responsibility is returning to the community and thus, in part, to community foundations.

The need for a tax credit also has been increased by federal tax reform, which reduces marginal tax rates and eliminates the charitable contribution deduction for nonitemizers. Lower marginal tax rates for both individuals and corporations will reduce the after-tax benefit of charitable gifts. A state tax credit for community foundation contributions can partially offset the

reduction in the federal tax incentive. It is now appropriate for state and local governments to step in and assume a responsibility previously the province of the federal government.

WILL THE PROPOSED CHANGE IN THE CHARITABLE TAX CREDIT HURT OTHER MICHIGAN NONPROFIT ORGANIZATIONS?

No. Nearly all organizations now eligible are education-oriented. At present, the legislation gives charitable tax credits only to institutions of higher education (public and private), the Michigan Colleges Foundation, public libraries, and public broadcast stations. Donors historically have strongly supported such organizations since their functions are specific and narrowly defined. Donor support of these organizations is likely to continue even with the addition of a tax credit for community foundations.

Furthermore, it should be noted that community foundations themselves are substantial contributors to educational and cultural organizations and institutions. Therefore, a tax credit for contributions to community foundations will benefit educational and cultural entities as well.

WOULD THE TAX CHANGE ENCOURAGE CHARITABLE GIVING IN MICHIGAN?

Yes. Changing the tax code to allow credit for community foundation donations would generate additional support for much-needed community programs. Members of a community become more willing to make donations when they can see directly the results of their charitable contributions. Likewise, the proposed change would encourage giving by corporations and business organizations that have not yet reached their tax credit limit; they would have an incentive to provide additional support to communities in which their employees live and work. With more contributions, community foundations can build the endowments needed to respond to the many immediate and long-term community needs outside the reach of educational institutions, libraries, and public broadcasting.

In addition to encouraging charitable giving, a tax credit for community foundation donations would promote the public/private partnership by increasing volunteerism. This is because financial commitment to a worthy cause usually stimulates personal involvement, particularly at the local level

where there is a direct and noticeable return on one's financial and personal investments. If the experience of public broadcast stations is an indicator, it is likely that adoption of the proposed tax credit would provide an extra incentive for middle-income working families to participate in community activities and contribute to community foundations.

WILL THE PROPOSED TAX CHANGE LEAD TO FUTURE REQUESTS FOR SUCH REVISIONS?

No. The Single Business Tax Act limits the tax credit to donations made to four types of organizations active in educational and cultural enhancement. Some may suggest that other charities in the state would wish to be included in the act if community foundations are included. However, it should be remembered that community foundations are unique. The scope of their activity within their communities potentially includes all charities. For example, the Kalamazoo Foundation--the largest community foundation in Michigan--has contributed nearly \$54 million to a wide variety of charities that conduct projects to benefit the people of Kalamazoo County. Likewise, the Grand Rapids Foundation--the oldest community foundation in Michigan--has contributed over \$20.5 million to charities benefiting the people of Grand Rapids.

In fact, all charities that may wish to be listed in the act would be eligible to receive funds from community foundations. The net effect of the proposed tax credit would be to provide support to Michigan communities at large without making additional state appropriations to local government entities or individual charities. In essence, the legislation would shift funds to communities via community foundations through tax credits and would also help put local control and decision-making back where it is most effectively administered--in the hands of the people.