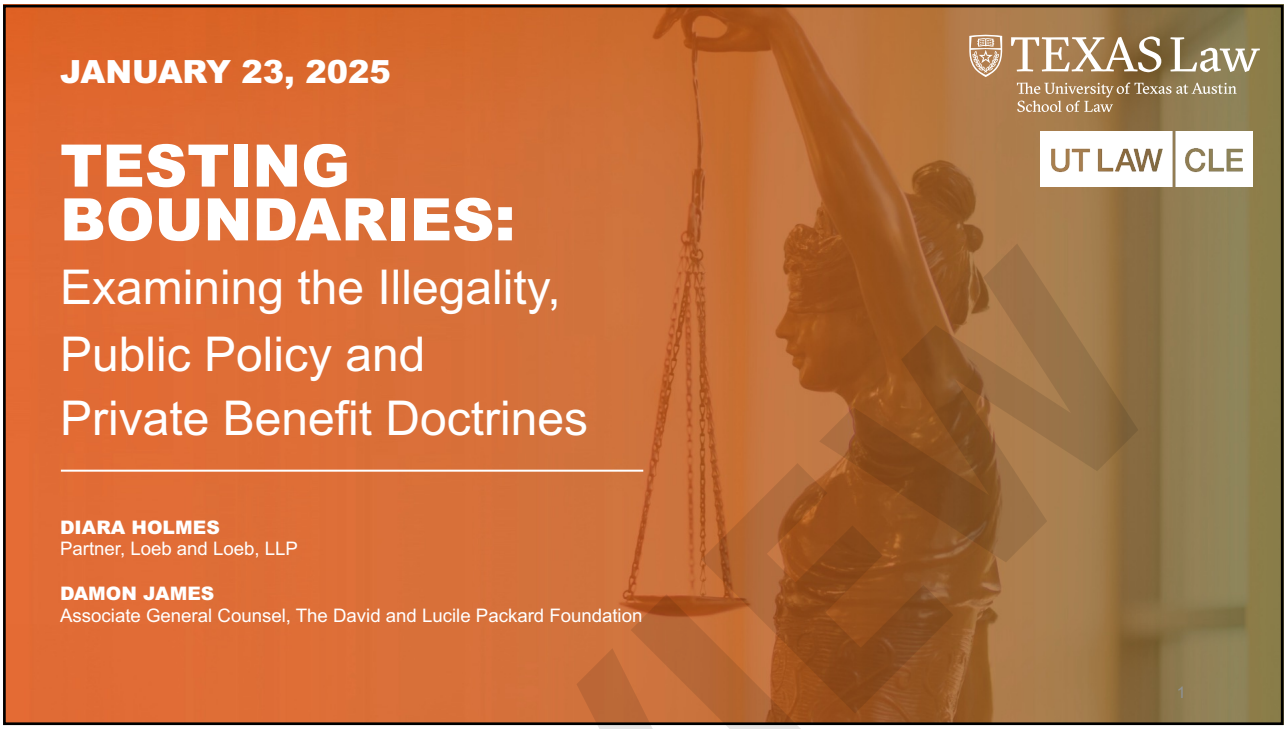
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TEXAS Law
The University of Texas at Austin
School of Law
UT LAW CLE
TESTING BOUNDARIES:
Examining the Illegality, Public Policy and Private Benefit Doctrines
DIARA HOLMES
Partner, Loeb and Loeb, LLP
DAMON JAMES
Associate General Counsel, The David and Lucile Packard Foundation
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Overview
• Illegality Doctrine
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Illegality Doctrine

- The **illegality doctrine** prohibits **both (i) illegal activities,** and **(ii) those that -- while not necessarily illegal -- are contrary to a fundamental public policy.**
  - An organization with an **illegal purpose** cannot qualify for tax exemption.
    - In *Church of Scientology of California v. Commissioner,* the court did not need to evaluate the substantiality of illegal activities because it determined that one of the organization's primary purposes was criminal tax fraud.
  - Even an organization with a legal purpose will not qualify for tax exemption if it engages in **substantial illegal activity**.
    - In *Mysteryboy, Inc. v. Commissioner,* T.C. Memo 2010-13, the Tax Court held that an organization that encouraged sexual activity with minors with the goal to repeal child pornography and rape laws was not exempt. Its proposed activities are prohibited by law, violate public policy as reflected in those laws, and tend to promote illegal activities.

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Illegality Doctrine – Violations of Public Policy

- In *Bob Jones University v. United States*, 461 U.S. 574 (1983), the Court supported the IRS' decision to revoke the 501(c)(3) tax-exemption of a private religious university that discriminated against African Americans in making admissions decisions.
- In determining there was a strong public policy against racial discrimination, the Court in Bob Jones considered the unanimous decisions from all three branches of the federal government, which during that period, had consistently ruled that race-based discrimination against African Americans in public education is both unconstitutional and contrary to public policy.
- The Court said, "it would be anomalous for the Executive, Legislative and Judicial Branches to reach conclusions that add up to a firm public policy … and at the same time have the IRS blissfully ignore what all three branches of the Federal Government had declared."

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Civil Disobedience

Rev. Rul. 75-384 – Encouraging Public Disorder as Illegal Purpose

- Organization's primary activity was sponsoring protest demonstrations at which participants were urged to deliberately block vehicles and pedestrians, disrupt the work of government, and prevent the movement of supplies.
- IRS ruled: not exempt under Section 501(c)(3). Activities violated local ordinances and constituted "breaches of public order."

"The organization induces or encourages the commission of criminal acts by planning and sponsoring such events. The intentional nature of this encouragement precludes the possibility that the organization might unfairly fail to qualify for exemption due to an isolated or inadvertent violation of a regulatory statute."

- They demonstrated an illegal purpose inconsistent with charitable purposes and increased the burdens of local government.

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Civil Disobedience

- In contrast, **Rev. Rul. 80-278** involved an organization which had the purpose of protecting and restoring environmental quality. Its activities included education and primarily initiating litigation under environmental laws—e.g., suing local manufacturers and state agencies to stop air pollution and enforce regulations. The organization hired private attorneys for its cases and ensured its lawsuits did not primarily benefit private interests.

- IRS determined the confrontations were carried out through legal channels in the courts and therefore clearly not illegal. Efforts to protect and preserve the environment are recognized as charitable. Congress endorses private litigation as a valid method for enforcing environmental laws, such as the Clean Air Act and Federal Water Pollution Control Act, to assist government enforcement and ensure proper statutory interpretation. The organization's litigation program as a plaintiff is lawful, aligned with public policy, and supports its exempt charitable purposes.

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Title search: Testing Boundaries: Examining the Illegality, Public Policy and Private Benefit Doctrines

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