» The Watcher » February 9, 2004 Vol.5, No.3

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The Misleading 2005 Budget

It's hard to know how much emphasis should be put on the president's 2005 Budget. On one hand, it lays out the president's main policy objectives – mainly tax cuts for upper income individuals, increases in defense spending, and real cuts for many domestic services. On the other hand, the cost estimates, deficit forecasts, and other analyses are fundamentally misleading.

There is no example more revealing of the president's use of spin tactics to cover up his shortfalls than his 2005 budget proposal. Overall, the budget attempts to minimize the size of the deficit without appearing to cut popular and important services.

As budget analysts, we are deeply disappointed and concerned with the frequency and magnitude of these tactics. Honest budgeting and accounting is a fundamental prerequisite for sound decision making in a

democracy.

Here are just some of the most blatant examples:

- The budget only provides revenue and spending numbers for 2005-2009, even while – according to the Budget's own numbers – 87 percent of the 10-year revenue costs of the proposals occur *after 2009*. Congress must look at the 10-year costs when passing legislation, so only presenting 5 years worth of budget numbers is inadequate.
- Programmatic detail normally published in the budget was omitted, leaving Congress, journalists, and independent analysts leafing through a 999 page computer printout by the OMB.
- The costs of rebuilding Iraq and Afghanistan after Sept. 30 of this year are not included, nor are there any ongoing funds included "for the Defense Department's participation on the global war on terrorism."
- Another huge cost is that the president dodges a long-term problem with the Alternative Minimum Tax (AMT) by proposing a fix for 2004 and 2005 only. The budget states, "long-term change is needed" (page 263, 2005 Budget, Analytical Perspectives.) A real fix to the problem would require adding billions to the deficit, which, presumably, is why a real fix is not included in the final totals.
- There is a table on the cost of the president's proposals, which only looks at the revenue costs, even though footnotes cite tens of billions in outlay costs as well (Table, S-9) Why not include all costs of proposed programs?
- There are proposed changes to the budget "baseline" and Pay-As-You-Go (Pay-Go) rules that would enable tax cuts to be made permanent without properly accounting for their costs, and would allow additional corporate tax cuts to be passed at a lower threshold than spending for education, national parks, child nutrition, scientific research, Medicare benefits, or any other services. See [article on budget rules] for more details.

2005 Federal Budget Continues Fiscal Decline

OMB Watch has released a new report providing an analysis of the president's budget that describes the fiscal chaos created by the president's proposals. The report is entitled "2005 Federal Budget Continues Fiscal Decline."

The report finds that even if we take the numbers in the budget at face value, there is considerable fiscal decline in the federal budget, including:

- A deficit of $521 billion for 2004;
- Revenue at 15.7 percent of GDP - the lowest in over 50 years;
- Massive structural deficits totaling $1.3 trillion over the years 2005-2009;
- Long-term deficits over the next 50 years, tripling current deficits as a percentage of GDP; and
- Over the next 10 years, the president is proposing a net $1.1 trillion in revenue reductions - most of which (87 percent) will occur after the 2005-2009 window included in the budget.

The final section offers some of the implications of this recent fiscal decline.

See OMB Watch - 2005 Federal Budget Continues Fiscal Decline for full details.

Budget Process in the Service of Tax Cuts

It is important to remember the magnitude of the federal budget process on the outcome of community results. While budget process issues are often arcane and sometimes difficult to determine the affects on results, in the case of several of the president's proposals, the purpose is very clear—to make tax cuts easier to pass and expansion of government services more difficult.

One mechanism that has been used in the past to reduce budget deficits and move towards budget surpluses is called "pay-as-you-go" or "pay-go." This is a requirement that legislation that will increase entitlement (non-discretionary) spending or reduce revenues must be offset by cuts in other entitlement spending or by tax increases, to insure that the deficit does not rise. The statutory pay-go rules expired after 2002, although modified pay-go rules in the Senate were created through the FY 2004 budget resolution.

The president proposes to reinstate the "pay-go" rules, with some very big differences. Rather than "pay-go" rules that apply to entitlement spending **and** revenue reductions (tax cuts), the President wants to apply the "pay-go" rules only to increases in entitlement spending or refundable tax credits. Any legislation that reduces revenue through tax cuts (other than refundable tax credits) does not have to be offset. Additionally, under the usual "pay-go" rules, the offset for increases in spending or reductions in revenue can come either from reducing other program spending or by increasing revenue through tax changes. Under the President's proposal, increases in entitlement spending could only be offset by program cuts, not through savings on the tax side.

Under the President's proposal, legislators could not expand a program like prescription drug benefits under Medicare, for instance, and pay for it by eliminating a corporate tax loophole—rather, it would have to be paid for by cutting something from the entitlement side.

Entitlement programs, like Social Security, Medicare, and Medicaid, and refundable tax credits, like the Earned Income Tax Credit (EITC) or the child care tax credit, are most important to low- and middle-income families. On the other hand, high-income people receive most of their government benefits from tax cuts (or tax "entitlements.") Once again the bias of this administration is made clear. Tax cuts are "free," even though they increase deficits just as much as spending, and in fact, are more dangerous, since once taxes are cut, it is politically difficult to raise taxes.

The President has yet another way to make tax cuts look free of cost. Another of his budget process "reform" proposals is to have the Congressional Budget Office essentially "pretend" that all of the 2001 and some of the 2003 tax cuts (all of which are scheduled to expire by 2010) are already permanent. The official budget "baseline" is supposed to reflect current law and be a reference point from which to measure the impact of new legislation or tax cuts. If the huge cost of making expiring tax cut provisions permanent is already incorporated into the baseline, proposals to make the tax cuts permanent will have zero cost when compared to the baseline.

The administration justifies these skewed and gimmicky proposals because they will put pressure on keeping spending down so deficits can be cut. As OMB Budget Director Josh Bolton stated, "We want to keep the focus on spending and that's where we think the [deficit] problem is." Actually, the deficit problem is really on the side of revenue. Federal revenue for FY 2004 – at just 15.7 percent of gross domestic product – is projected to be at its lowest level since 1950; and federal income tax receipts for FY 2004, at 8.0 percent, will be at their lowest level since 1942. The President's proposals are designed to continue the nosedive of federal revenue and the defunding of government.

Besides these budget process changes, the President has proposed to:

- Extend the discretionary budget "caps" for 2005 through 2009. The caps set annual limits on the overall amount of discretionary spending. The President proposes that the amounts be based on his 2005 budget (which limits the increase in discretionary spending outside of defense and homeland security to less than .5 percent increase for 2005) with only small increases. This is another way to keep spending down.
- Make the requirements for "emergency" spending (which is not counted under the budget caps) stricter. "Emergency" spending must be necessary, sudden, urgent, unforeseen and not permanent.
- Change from a concurrent budget resolution (passed by House and Senate, but not signed by the President) to a joint budget resolution (agreed upon jointly by the House and Senate, signed by the President, and having the force of law).
- Change from an annual appropriations process to a biennial appropriations process (taking place every two years).
- Allow a Presidential line-item veto, giving the President the authority to veto new appropriations,

mandatory spending, or "limited grants of tax assistance" whenever he determines that the spending is not an "essential government priority." The savings would go to deficit reduction.
- Make a "continuing resolution" automatic when appropriations are not enacted by the start of a new fiscal year, by funding at the level of the President's budget or the prior fiscal year – whichever is lower.

Some of these changes, like the "emergency" spending provision, may be worthwhile. Even budget "caps," if they are set at adequate levels, have been useful in the past. However, under this Administration, the caps are far too low to fund the programs and services that most Americans want. Most of the budget "reform" provisions that the President has proposed either give him more power over the spending process – the line-item veto, the joint budget resolution – or, like the budget "caps" or automatic continuing resolution are ways to reduce government while preserving tax cuts for the wealthy.

State-by-State Effects of the Bush Budget

The National Priorities Project has released a state-by-state analysis of the effect of the President's budget.

A Government Rollback

It is no secret that, after contributing to the deficit by huge tax cuts, a primary focus of this Administration now is decreasing the deficit by cutting spending, while continuing to reduce revenue by way of tax cuts. This will require massive cuts and eliminations of programs and services. It augurs a historically significant rollback in federal spending that if unchecked will fulfill conservative promises to reduce government to the barest of minimums.

Sixty-five programs have been slated for elimination in fiscal year 2005 at a "savings" of $4.9 billion according to Office of Management and Budget Director Bolton. Major cuts are proposed for another 63 programs. A list published by the *Washington Post* of "major reductions and terminations in the 2005 budget" is just the tip of the iceberg. The *Post* also reported the existence of a 999-page OMB computer printout that "suggests" even more cuts and freezes through 2009. (The Center on Budget and Policy Priorities obtained the OMB document and OMB Watch has put it on out web site.) You can find a wealth of information about the budget, and even a link to a *Washington Post* article, on the OMB site. For more about cuts in domestic discretionary programs, see the Center on Budget and Policy Priorities analysis.

Some of the program eliminations are being justified by the "grade" they received under the "Program Assessment Rating Tool" (PART) being used by the administration to evaluate the effectiveness of programs. The PART was implemented during the FY 2004 budget cycle, and used to evaluate 20 percent, or 234 government programs. During FY 2005, 40 percent, or about 400 programs, were evaluated under the PART. Another 20 percent will be added in FY 2006, bringing the total up to 60 percent.

Of the 65 programs slated for elimination, 13 were zeroed out based on the PART evaluation. Of those 13, eight received a grade of "failed to demonstrate results," as did a total of 40 percent of programs this year (and over 50 percent last year). Those programs are:

- Small Business Innovation Research Program, Commerce
- Tech-Prep Education State Grants, Education
- Nuclear Energy Research Initiative, Energy
- Metropolitan Medical Response System, Homeland Security
- State Criminal Alien Assistance Program, Justice
- Environmental Education, Environmental Protection Agency
- Business Information Centers, Small Business Administration

Five of the 13 programs slated for elimination were deemed "ineffective:"

- Even Start, Education
- Federal Perkins Loans, Education
- HOPE VI, Housing and Urban Development
- Juvenile Accountability Block Grants, Justice
- Migrant and Seasonal Farm workers, Justice

Two programs that were eliminated were rated as "adequate:"

- Advanced Technology Program, Commerce
- Comprehensive School Reform, Education

About 25 percent of all programs evaluated under the PART received an "adequate" or "ineffective" grade. Another 40 percent of the programs rated under PART for the 2005 budget cycle received "effective" or "moderately effective" grades. An OMB summary of the PART evaluations for FY 2005 can be found on its website or in the CD Rom included with the Analytical Perspectives volume of the Budget.

It is clear that the PART evaluations are being used as a way of justifying program cuts and elimination. We have previously reported on problems with the PART assessment, as evidenced by our comments on the process. Information about the PART, including the programs evaluated, and being proposed for evaluation (forthcoming), and the ratings, can be found on OMB's website.

Economy and Jobs Watch: GDP, Employment, and the Federal Reserve

Release of two new pieces of economic data showed that the economy, while growing, is still below expectations.

Gross Domestic Product

Gross domestic product (GDP) grew at an annual rate of 4 percent in the final quarter of 2003. This was less than half the 8.2 percent growth rate in the third quarter, and below economists' expectations (CNN reported an expected rate of 5 percent). For 2003 as a whole, the economy grew at a 3.1 percent rate, which is less than the 3.3 percent average growth rate over the past 10 years. In the recovery from a recession and during a period of extraordinarily stimulative monetary policy, we would normally expect much stronger economic performance.

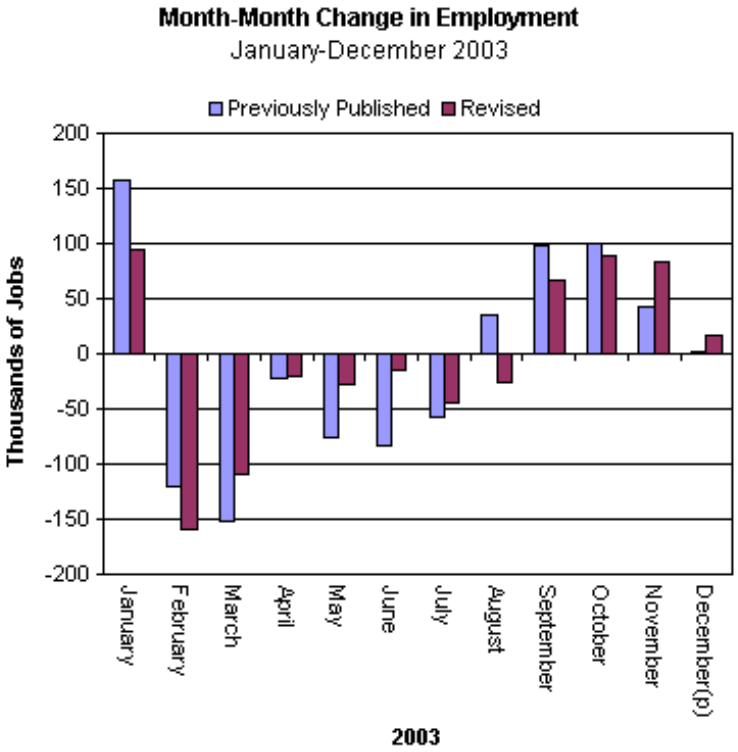
Employment

Employment data for January showed an increase of 112,000 jobs, and a small dip in the unemployment rate to 5.6 percent. While positive, size of the job growth is below the level needed to keep up with population growth, below the level needed to create a healthy labor market, and below the predictions put forth by the administration.

JobWatch.org shows that job growth from June to January was 1.8 million jobs short of the administration's predicted effect of the tax cut.

The weaker than expected job numbers, together with the mild GDP report paints a picture of an economy that continues to muddle along without a clear direction.

In addition to their regular release, the Bureau of Labor Statistics also published a revision to their jobs numbers for the past year. The revisions incorporated new data as well as updated methods for estimating the "births" and "deaths" of firms. The following figure shows the employment picture remains essentially unchanged in 2003, with a revised total 147,000 jobs lost from January to December 2003.



The Fed

The economy has greatly benefited over the last year from an accommodative Federal Reserve (Fed), which has generated a strong housing market and pumped large amounts of money into the economy through loan refinancing.

However, the Fed cannot hold interest rates down forever, especially given pressures from the exploding budget deficit and the falling value of the dollar, and will likely begin to slowly raise rates by the end of the year.

After a two-day meeting of the Fed's decision-making group, the Federal Open Market Committee (FOMC) released their usual policy statement. While they chose to again keep rates unchanged, they removed a line from previous statements that said "policy accommodation can be maintained for a considerable period." This omission signaled to observers that the monetary policymakers are closer to taking their foot off the gas.

With the Federal Reserve backing away from the stimulus table, the current direction of fiscal policy – which is providing little effective stimulus in the short-run – continues to put at risk the health of the economy. This is especially true in the long run as surpluses have given way to massive structural deficits.

OMB's Revised Cost of Medicare Prescription Drug Benefits Raises Questions

During last year's debate on the Prescription Drug and Medicare Improvement Act of 2003, Congress used an outlay cost estimate of $395 billion for the new program. However, in the president's 2005 budget, the 10-year outlay cost was estimated to be $534 billion – 35 percent greater than the initial estimate. See Table S-13, Page 387, 2005 budget..

The final bill was passed on Nov. 25, 2003 and the president signed the bill into law on the Dec. 8 – the $139

billion revision was thus published less than 2 months after the bill was signed. According to the administration's budget, "The largest portion of the difference in these cost estimates is attributable to assumptions regarding beneficiary participation, market behavior, and cost growth rates." (Note to Table S-13, Page 387).

It is not unusual for cost estimates to change over time, however a revision this large coming so soon after the initial estimate raises important questions about what and when the administration and the Office of Management and Budget (OMB) knew about the revised estimates. Did the OMB withhold new cost estimates during the congressional debate? Did the president know about the new cost estimates when he signed the bill in December? Are the costs inflated to make it easier to "cut the deficit in half" by 2009?

Manipulation or selective withholding of budget estimates for political reasons is not a good way to start a budget process. The administration and OMB need to make it clear when these new estimates were made, and exactly how and why they differ from the previous estimates.

Tax Freedom or Telecommunications Windfall?

There is considerable confusion about the debate on Internet taxes. One issue is whether items sold over the Internet should be taxed. Another issue is whether there should be a tax on access to the Internet; similar to the tax we pay for use of telephones. This second issue – charges a user pays to an Internet Service Provider to connect to the Internet, as well as taxes that would discriminatorily apply only to Internet technology and use – is now being debated in Congress.

The "Internet Tax Freedom Act" was a temporary "moratorium" banning state and local taxation of Internet access and prohibiting "discriminatory" taxes that single out the Internet for special taxation. It was enacted in 1998 and subsequently renewed through November 1, 2003. The purpose of this temporary moratorium was to encourage the growth of the Internet.

Given the expiration of the moratorium, Congress is moving to **permanently** ban taxation of Internet access. During the last congressional session, the House passed "The Internet Tax Non-discrimination Act" (H.R. 49). A vote on a companion bill in the Senate (S.150) was postponed. It is likely to be brought to the floor this session.

Besides making the moratorium permanent, the bills include two other provisions that significantly expand the scope of the original moratorium:

- One would eliminate a "grandfather" clause included in the original legislation that allowed state and local taxes on Internet access if the taxes had been in effect prior to October 1, 1998. (State and local governments in 11 states would be affected.) The House bill would immediately eliminate the grandfather clause. The Senate bill would eliminate it after three years.
- Another would expand the definition of "Internet access" to prevent states and localities from any taxing of telecommunications services "used to provide Internet access." This provision could (depending on interpretation) prohibit states and localities from taxing: 1. telecommunications services purchased by Internet access providers; 2. DSL telephone service (27 states and D.C. currently get sales or excise taxes on DSL); and, 3. telephone service itself as it shifts to the Internet (e.g., VOIP), a process that has already begun.

Rather than a simple continuation of the original moratorium on the taxation of Internet access, the proposed legislation would provide a huge tax break to the telecommunications industry, while dramatically reducing sources of state and local revenue, at a time when many states are experiencing severe fiscal imbalances.

The full impact on state and local government revenue is not even known because the interpretation of "telecommunications services used to provide Internet access" is so broad and ill defined. The telecommunications industry will certainly argue for the widest possible interpretation. The elimination of the grandfather clause would cost the 11 states and local governments from between $80 million and $120 million annually. The loss of the ability to tax DSL would cost those states and localities about $70 million annually. Even more technical issues could arise due to the broad definitions in the legislation that could unintentionally cost state and local government much more. For a more complete examination of this issue from which the cost

estimates were drawn, see the Center on Budget and Policy Priorities analysis.

Supporters of the legislation argue that taxes on Internet access exacerbate the so-called "digital divide." Cloaking the financial self-interest of the telecommunications industry in concern for low-income people's ability to access the Internet is a disingenuous argument. It is far more likely that cuts in the services that state and local government provide due to inadequate state and local revenue, like Internet access or training at libraries and schools, would make it more difficult for people to access the Internet.

The underlying question is "Why should telephone service be taxed, and Internet service not?" In contrast to the prohibition of taxes on Internet service, the charges a user pays to a company for telephone service are taxed, and have been since the federal tax was first imposed as an "excise" or "luxury" tax during the Spanish-American War. That tax on telecommunications services has also become an important source of revenue for state and local governments, amounting to more than $20 billion a year in revenues. While a moratorium on Internet taxation might have been a good idea to allow its growth, it is probably time to reexamine its purpose now.

Even without addressing that question, since Internet access has become more complicated than the original "dial-up" connection, and the technology for Internet and telephone access is rapidly changing, a permanent ban on taxation of Internet access, without more careful study and consideration, is a bad idea. The possibility of depriving states and localities of long-standing telecommunications revenue by broadening the definition of Internet access, especially given the fiscal crises in most states, is difficult to justify. In the absence of a compromise to proceed with taxation of Internet access, Congress should not permanently prohibit such taxes. One solution is to provide an extension of the original moratorium on taxation in order to allow more time to develop a well-considered policy.

Sens. Lamar Alexander (R-TN) and Thomas Carper (D-DE) are working with a number of groups who are concerned about this issue, and intend to introduce a compromise bill sometime this week. The bill would extend the moratorium for two years and also exempt DSL Internet access from taxation.

Tax and Budget Survey News

The OMB Watch Tax and Budget Survey is now closed. We had a tremendous response of over 700 completions. We extend our sincere thanks to all of you who completed the survey. We will be reporting the results soon!

Budget Increases Funds for OSHA Whistleblowers

The myriad of numbers in the recent proposed federal budget included a surprising change in the Occupational Safety and Health Administration (OSHA)—an increase of funds to investigate whistleblower claims.

President Bush's 2005 budget request for OSHA includes a $5 million increase in enforcement funding, with $2 million specifically earmarked to strengthen the agency's whistleblower protection efforts. The increase in whistleblower funds is significant considering that while OSHA's overall proposed budget approached half a billion dollars, the agency only received a total increase of $4.1 million.

OSHA Administrator John Henshaw cited an increase of responsibilities and workload under whistleblower protections legislation. Henshaw specifically noted the Corporate and Criminal Fraud Act (Sarbanes-Oxley), which increased whistleblower provisions in an effort to avoid future Enron and Anderson Consulting scandals. Sarbanes-Oxley established an administrative remedy for corporate whistleblowers within the U.S. Department of Labor (DOL). The law also permits corporate whistleblowers to seek federal court relief if the DOL does not resolve their case within 180 days.

The Sabanes-Oxley legislation modeled its protections after other legislation noted by the OSHA Administrator, the Wendell H. Ford Aviation Investment and Reform Act for the 21 Century. The law, signed by President Clinton in 2000, protects the rights of airline employees to report safety violations and other wrongdoing.

This increase in whistleblower funding runs contrary to numerous previous actions under the Bush administration to reduce protections for whistleblowers and discourage federal employees from speaking out. The Homeland Security Act of 2002 made whistle blowing illegal for critical infrastructure information submitted by corporations. Any violation would be punishable by up to a year in jail and a huge fine. Recent legislative efforts to reinforce whistleblower protections have not received the support of the Bush administration. Additionally, Congress recently discovered that an Environmental Protection Agency headquarters' official instructed regional staff not to cooperate with congressional staff investigating the status of contaminated sites around the country (see this week's Watcher article.)

Court Rules Portion of Patriot Act Illegal

A federal judge has ruled that at least one provision of the USA Patriot Act is unconstitutional.

A U.S. District Judge in California ruled that the U.S. Patriot Act's ban on providing "expert advice or assistance" to foreign terrorist groups is unconstitutionally vague, in violation of the First and Fifth Amendments. This is the first federal court decision finding any portion of the Patriot Act illegal. The judge's decision did not include a nationwide injunction on the provision as sought by the plaintiffs.

The California case involves five groups and two U.S. citizens who are trying to provide support for lawful, nonviolent activities on behalf of Kurdish refugees in Turkey. These groups aim to help find a peaceful resolution of the Kurds' campaign for self-determination in Turkey, but under the anti–terrorism law have been threatened with 15 years imprisonment.

Numerous groups have criticized the law as overreaching legislation that infringes on the rights and civil liberties of citizens. The court decision lends credence to the numerous cities and towns that have passed laws opposing the U.S. Patriot Act. New York City is the most recent city to pass such a resolution. On Feb. 4 the New York City Council approved a resolution condemning the law as unpatriotic for infringing on privacy rights.

Another case challenging the Patriot Act is currently pending in Detroit. The plaintiff, the American Civil Liberties Union, argues that the Patriot Act grants the federal government unconstitutional authority to secretly seize library reading lists and other personal records.

The California ruling could be the first of many in which the judicial branch of government acts as a check and balance against the excessive law passed by an overly zealous legislature.

Draft FEC Advisory Opinion Generates Comments from Nonprofits

The Federal Election Commission (FEC) staff has drafted an Advisory Opinion (AO) that could have far reaching impact on nonprofit advocacy. Draft AO 2003-37 was written in response to a request from Americans for a Better Country, a political organization under Section 527 of the tax code, but it could impact all issue advocacy, not just partisan campaign activity.

The draft AO broadens the definition of expenditures that "promote, support, attacks or oppose" a candidate for federal office that are regulated by the FEC to include any criticism or support of a public official who happens to be running for federal office, even if the election is not mentioned or the official is not identified as a candidate.

This approach would sharply restrict the ability of many 527 groups to speak out on public policy matters, even if the election or a federal candidate is not mentioned. The Commissioners will consider the draft opinion by Feb. 19. If approved, it will apply immediately to 527 groups. However, many are concerned about a slippery slope where the FEC language may eventually reach to 501(c)(3) and 501(c)(4) organizations and force them to comply with FEC regulations. If that were to happen, it would greatly undermine free speech rights of charities and other 501(c) groups, such as social welfare organizations and labor unions.

The draft AO generated broad response from the nonprofit community between its release on Jan. 19 and the

Feb. 5 meeting of the FEC. Most of the written comments on the draft indicated concern about potential over-reaching effect the draft AO could have. For example, one letter was signed by 324 organizations, including OMB Watch, stating, “Making it unlawful to criticize the policies and action of a sitting President or Members of Congress except under the auspices of a registered political committee is one of the most fundamental attacks on the freedom of speech and freedom of association of American citizens ever contemplated by a governmental agency.”

Other comments were submitted by the AFL-CIO, the American Lung Association, Independent Sector, the Michigan Nonprofit Association, the National Council of Nonprofit Associations and the Service Employees International Union. The Republican National Committee submitted comments in support of the draft AO, as did campaign finance reform groups Democracy 21, the Campaign Legal Center and the Center for Responsive Politics. However, another strong reform supporter, Public Citizen, filed comments opposing the draft.

At the Feb. 5 FEC meeting the Commission decided to delay their decision until Feb. 19 (the legal deadline), to allow time for the Commissioners to review public comments. The FEC is made up of six commissioners, three Republicans and three Democrats. Four votes are required to approve action, including this draft AO. Democratic FEC Commissioner Scott Thomas told reporters that he is “leaning toward the line of analysis” in the draft AO, but said the final AO should clearly states it only addresses regulated political committees.

Republicans founded Americans for a Better Country, but their request for an Advisory Opinion listed many of the activities being undertaken by Americans Coming Together, a Democratic leaning 527 political committee. The AO request has been viewed as a partisan attempt to limit voter mobilization efforts that would favor Democrats.

IRS Attorney Says Nonprofits Can Lobby During Election Seasons

The District of Columbia Bar Association Exempt Organizations Committee held a meeting recently that focused on legal issues in an election year. IRS attorney Judith Kindell explained to those attending the meeting that, “Organizations don’t have to stop lobbying campaigns simply because of an election.”

Referring to groups exempt under Section 501(c) or the tax code, including charities, social welfare organizations, unions and trade associations, Kindell cited recent IRS Revenue Ruling 2004-6, which explains factors the IRS uses to distinguish between genuine issue advocacy and advocacy meant to influence elections. Nonprofits that lobbying public officials on specific issues do not have to stop their efforts when those officials are up for re-election, as long as their efforts do not imply support for or opposition to the official as a candidate.

James Joseph, an attorney with Arnold and Porter who spoke about the rules regarding sponsorship of nonpartisan candidate debates and forums, said the ruling is “one of the best rules written for Section 527 organizations,” whose primary exempt purpose is to influence elections. The examples detailed when the IRS will consider public communications to be “exempt” for 527 purposes, which means they are intended to influence elections and, therefore, are not condoned activities for 501(c)(3) organizations.

In the ruling, guidance is given to define electioneering communications as those that are:

- made during a time that coincides with an election
- identify a candidate
- target voters in a particular election
- identify a candidate’s position on an issue
- distinguish the candidate’s position from others (in the communication or in the overall campaign)
- not part of an ongoing series of substantially similar advocacy on the same issue.

The guidance given also identifies communications that are genuine issue advocacy as ones that:

- identify specific legislation or a specific event outside the control of the organization
- are timed to coincide with the specific event
- identify the candidate solely as a government official in a position to act on the policy or specific event
- mention the candidate solely as the a key sponsor of legislation.

Joseph also told the audience that candidate briefings held by 501(c) organizations, including charities, should be impartial. This means all legally qualified candidates should be invited to participate, the moderator should be impartial and present questions relating to a wide variety of issues. Each candidate must have an equal opportunity to respond.

“Voter registration drives,” said Joseph, “should not refer to specific candidates or parties, unless all are mentioned. They should also address a wide variety of issues.”

Attorney Beth Kingsley of Harmon, Curran, Speilberg and Eisenberg said additional rules apply to federal elections under the Federal Election Campaign Act. This includes restrictions on paid broadcast advertising 60 days before a general election or 30 days before a primary election or nominating conventions.

Groups Ask Congress to Initiate Ethics Investigation of Delay Charity

Common Cause and the National Committee for Responsive Philanthropy have called on members of the House to “urge the Ethics Committee to formally rule on the legality of a plan closely associated with Rep. Tom DeLay (R-TX) to establish a children’s charity as a fundraising vehicle to subsidize donor events at the Republican National Convention.”

In a Feb. 5 letter to House members the two groups noted that the charity, Celebrations for Children, is linking donations to access to Rep. DeLay and others at the Republican National Convention in New York this summer. The letter also notes that only members of the House can ask the Ethics Committee to initiate an investigation, and urges each member to contact Chairman Joel Hefley (R-CO) and ranking member Alan Mollohan (D-WV) to urge them to take action.

In Dec. the *Washington Post* reported that a brochure published by the group offers donors of $500,000 or more benefits including sponsorship of a dinner with DeLay, and tickets to “the Members reception before/during/after Presidential acceptance speech,” and a private yacht cruise with DeLay. Smaller donors are offered similar, but less substantial, benefits. If the IRS approves Celebrations for Children’s application for recognition of exempt status as a charity these donations will be deductible.

Common Cause, Democracy 21, the Campaign Legal Center and the National Committee on Responsive Philanthropy have filed complaints against Celebrations for Children with the IRS, asking that it be denied exempt status as a charity under Section 501(c)(3). The Common Cause/NCRP letter says, “We believe the overt partisanship of these activities is inappropriate for a charitable non-profit 501(c)(3) organization.”

The House Supports Religious Discrimination Bill

On Wednesday, Feb. 4, Rep. Lynn Woolsey (D-CA) offered a substitute amendment during House to strip out language that gave faith-based organizations permission to infuse their federally funded programs with religion and to discriminate on the basis of religion when hiring. Woolsey’s substitute amendment failed to be adopted by a 50-vote margin (183-232).

The Woolsey amendment contained two important legal points: (1) that all federal programs must be carried out in a lawful secular manner, and (2) that no federal grantee carrying out a federal program can use the funds to “discriminate on the basis of religion.” The Supreme Court in Bowen v. Kendrick, 487 U.S. 589 (1988) raised both points. Writing for the majority, Chief Justice Rehnquist wrote the Bowen decision to be consistent with at least 104 years of constitutional prohibitions on using government funds to support inherently religious activity. The Woolsey amendment was aimed at adding the language from Chief Rehnquist’s decision, and removing existing bill language that was snuck into the last reauthorization very late at night.

Before the vote in the full House, the Committee on Education and the Workforce considered H.R. 3030 in legislative session on Oct. 1, 2003 during which two amendments were considered and adopted by voice vote. In the committee the bill was amended to strip out other bad language that was adopted during the last re-authorization process. Chairman Boehner (R-OH) offered an amendment to codify previous regulatory practice ensuring that program beneficiaries and potential program beneficiaries are not discriminated against on the basis of religion.

The CSBG is a multi-million dollar fund used to address the causes and conditions of poverty and to assist people in achieving economic self-sufficiency. Because CSBG passed without the Woolsey language, the bill allows faith-based federal grantees to use tax dollars to fund inherently religious programs that enroll some of America's most vulnerable citizens. From homeless shelters, to substance abuse counseling, your tax dollars could be working to convert vulnerable citizens at a time of crisis.

Because there are no laws clearly regulating what faith-based organizations can do with their government funds, many problems have been recently reported in the news.

In Michigan, the state had to pull a contract with a faith-based organization based in Marlette for allegedly forcing teen program beneficiaries to attend church services. Teen Ranch Inc, doesn't deny using religion in its programs, but does deny forcing anyone to attend religious services. Teen Ranch is sent teens by court order and gets paid $130 per day by the state for each teen. Click here to read more.

The Salvation Army has begun an effort to reassert its evangelical roots. The Salvation Army of Greater New York has stressed the importance of spreading the Gospel in their work. In fact, the division has ordered that job descriptions now clearly state the organization's religious mission. The Salvation Army is also asking employees to fill out forms that state their religious affiliation and to sign a contract that they will follow the organization's religious mission when carrying out their job function. The division has $70 million in state and city funding for its programs. Click here to read more.

And finally, the House Committee on Government Reform's subcommittee on Criminal Justice, Drug Policy and Human Resources held a hearing on "Faith-based Perspectives on the Provision of Community Services" in Colorado Springs on Friday, Jan. 23. Five out the ten witnesses who testified at the hearing were representatives from Focus on the Family. Focus on the Family states on their website that there mission is, "To cooperate with the Holy Spirit in disseminating the Gospel of Jesus Christ to as many people as possible, and, specifically, to accomplish that objective by helping to preserve traditional values and the institution of the family." One group has claimed that Focus on the Family promotes "reparative" therapy for gay men and lesbians. Meaning, the organization uses intense therapy and religious piety as a means of "changing" homosexuals into heterosexuals. One witness at the Jan. 23 hearing is a gender specialist who may have spoke about the program.

Charitable Giving in Bush's 2005 Budget Proposal

President Bush's FY 2005 budget proposal includes several tax incentives to encourage charitable giving accompanied by several requirements that will limit taxpayer deductions.

While the CARE Act is still waiting action in a legislative conference committee, the president recently proposed many of its major tax incentives for charitable giving in his FY 2005 budget. If the CARE Act does finally make it to the president, it is clear that he will sign the piece of legislation into law because much of it will duplicate his intentions as expressed in his FY 2005 budget. Some of these incentives include:

- Non-itemizer Deduction: To allow nonitemizers to deduct contributions of $250 for single filers and $500 for joint filers, with a ceiling of $250 on the amount deducted ($500 for married couples filing jointly. The White House has estimated the cost spread out over ten years at $12 billion. The same provision is found in the House's version of CARE (H.R.7), but has been argued as an expensive provision that yields little in the way of giving.
- IRA Rollover: Donors age 65 and over could donate directly from their individual retirement accounts (IRA) without paying income taxes on the donated amounts. This provision is estimated by the White House to cost $3.5 billion over ten years. The IRA rollover idea can be found in both the House and Senate version of CARE. The House version sets the donor age at 70 1/2, while the Senate version (S.476) sets the age at 59 1/2.

- Excise Tax: Foundations would see a flat rate excise tax on their business investment income of one percent. Today, foundations pay up to two percent excise tax on their investment income. Foundations claim that this reduction to a flat one percent rate would enable them to give more to charities. The White House has estimated the cost to be $1 billion over ten years.
- Food Contributions: All taxpayers engaged in trade or business will be included in the extension of the tax deduction for food inventory donations. Currently, only certain companies can deduct food inventory contributions and the deduction had to be assumed as less than fair market value. Bush's proposal would allow for more players to contribute food inventory and the deduction would be increased to fair market value or two times the typical costs in the inventory (which ever is less.) However, S corporations and non-corporate taxpayers would be limited to 10 percent of income from trade or business. Estimated cost submitted by the White House is $1.2 billion over ten years.
- Remainder Trusts: Instead of losing their federal income tax-exemption for the year they invested in unrelated business activity, charitable remainder trusts will have to pay 100 percent excise tax on their unrelated business earnings. The administration estimates that the change would cost $68 million over ten years.
- Appreciated Property: Shareholders of S corporations will be given a better rate on their deduction for contributions of appreciated property (stock shares). The deduction ultimately lowers their income tax liability. The White House has estimated the cost at $239 million over ten years.
- $150 Million Limitation: The $150 million limitation on 501(c)(3) bonds is proposed to be repealed entirely. The cost of the repeal has been estimated at $94 million over a ten-year period.
- Restrictions on Bonds: 501(c)(3) organizations use of tax-exempt financing to acquire existing residential rental property for charitable purpose would be condoned. Currently, an 501(c)(3) can use tax-exempt financing to acquire residential rental property for charitable purpose only if the property is rented to low-income tenants or is substantially rehabilitated. Bush's proposal lifts those limitations. The White House says the cost spread out over ten years is $299 million.

Conversely, Bush's budget proposal included some provisions that would burden non-cash donors with new requirements for proof of value and set limits on deductions. The IRS has already put out announcements stating that they are getting prepared to crackdown on some of these non-cash contributions to charities. Specifically, on Dec. 22, 2003 the IRS issued an Information Release announcing the tightening of rules regarding donations of intellectual property. The Information Release was coupled with a Revenue Notice in which the IRS spelled out in detail the abuses for which it is now watching. Adopting some of these concerns over tax deduction abuse, President Bush proposed the following provisions:

- Intellectual Property: Sets limit on deductions for gifts of patents and other intellectual property (other than certain copy-rights) to charity to the lesser of the property's fair market value or the amount it cost the donor to produce the property. Currently the gift values of intellectual property are estimated by the fair market value of the property at the time of donation, and are increased by the perceived revenue if property was marketed commercially. Under Bush's proposal, donors could only deduct income that was actually earned by the charity that receives it (including future deductions for up to ten years or the life of the patent in royalties.) The Treasury claims that this proposal could add $3.2 billion in tax payments over ten years.
- Car Donations: Requires donors to seek independent appraisals of any automobile donated. Currently, donors may deduct fair-market value as established by established used car pricing guides, as long as the car's value did not exceed $5,000. Bush proposal would only allow car donations to be deducted if the taxpayer obtains a qualified appraisal of the vehicle. If this change is adopted, the White House says it would bring the government $1.2 billion over ten years. Read IRS' News Release, "IRS Officials Urge Caution and Care for Those Making a Car Donation."
- Property Donations: Any items, other than stock or inventory, donated to charities by companies must be independently appraised if the deduction claimed exceeds $5,000. Donations claimed to be over $500,000 must have the appraisal attached to the return. This proposal would bring all companies in line with policy regulations already set for individuals. The White House expects this proposal to bring in $367 million over ten years.

The House and Senate will be debating the president's budget proposal and will be drafting their own version of the 2005-spending plan. The president's proposed budget is important because it sets the stage for the overall federal fiscal policy in three main categories – how much money the government should spend overall, how much should be taken in tax revenues, and how much deficit or surplus government should run. For more

background information on the federal government's budget process see the Center for Budget Policy Priorities' .

Paul O'Neill's Papers to be Posted Online

Documents forming the basis of Paul O'Neill's headline-grabbing charges that the Bush administration planned as early as Jan. 2001 for the fall of Saddam Hussein will be posted on the Internet as an "experiment in transparency."

Here's the story: Former Treasury Secretary Paul O'Neill made news recently when he charged in the release of his book *The Price of Loyalty* that President George W. Bush planned to invade Iraq in the first few weeks of his administration. The Bush administration initially charged O'Neill's evidence should not have been publicly disclosed. Days ago, current Treasury Secretary John Snow noted that the Treasury Department should never have released at least some of the documents, and vowed to review the department's procedures to ensure that such releases never happen again. Last week, the author of O'Neill's book, Ron Suskind, began posting the 19,000 documents cited in the book on the Internet.

But the real story is not whether O'Neill or the Treasury Department should have released the documents, is the fact that these documents, once poured over, may yield interesting insights into policy decision-making, and these insights may pressure this administration -- and future administrations -- to reveal more information in a more timely manner about their policy deliberations.

If nothing else, the posting of these documents on the Internet shows that government has the technical capability to make more documents available to the public than it does now. The Treasury Department electronically scanned every document that O'Neill saw into an image file and stored them. So duplicating these documents and posting them online is relatively easy.

So why are background administration documents such as these hidden from public view? Those who use the federal open-records law, the Freedom of Information Act (FOIA), often complain that "pre-decisional" agency records are exempt from disclosure under FOIA. In other words, agencies do not have to disclose memos and other documents that government employees write while working through policy alternatives. The logic is that government employees should be able to enjoy a free exchange of ideas while forming policies, and the threat of these early memos' disclosure to the public would constrain early policy deliberations. Proponents of this exemption argue the public interest in government creating good policy decisions after complete and candid deliberations outweigh the public interest in disclosure of these documents. But many who attempt to obtain information from government through FOIA charge the "deliberative process" exemption has been used excessively to withhold information unnecessarily.

If these documents yield new insight into the policy decisions this President has made, more Americans may find new benefits to disclosure and embrace such disclosure as necessary to understand their president's actions and hold their elected leaders to account.

Paul O'Neill's papers may be accessed online at http://thepriceofloyalty.ronsuskind.com/thebushfiles/

EPA Gags Regional Staff on Perchlorate

EPA has prevented regional offices from speaking to congressional staff about perchlorate contamination. Perchlorate is found in rocket fuel and has contaminated drinking water near Department of Defense (DoD) sites in at least 22 states.

Reps. John Dingell (D-MI) and Hilda Solis (D-CA) released a report Jan. 15 that found DoD has made little progress in cleaning up contaminated sites. In their investigations, staff contacted regional EPA offices to gather information about the sites. When calls were placed, EPA officials stated that they "had been instructed by an EPA headquarters official not to speak with committee staff."

Dingell and Solis sent a letter to EPA administrator Mike Leavitt Feb. 5 urging him to stop stonewalling Congress from its routine communications with EPA. The letter noted "[t]here is no need to interject another level of Headquarters bureaucracy into the process unless there is a decision on your part to delay and hamper EPA employees from providing information about the contamination of actual and potential drinking water supplies and the health impacts for the public." Additionally, the letter admonished EPA for its reluctance to use its statutory powers to investigate the scope of perchlorate contamination.

Regrettably, this is not EPA's first effort to block perchlorate information. In 2002, EPA previously prevented agency scientists from discussing two studies that show lettuce absorbs large amounts of perchlorate – high levels of the chemical have been found in water and lettuce supplies. The escalation of EPA's stonewalling activities for all matters dealing with perchlorate is troubling. Moreover, hiding information from Congress inhibits its ability to perform its duties of representing and protecting the public.

Nuclear Insecurity Under DOE

A new Department of Energy (DOE) regulation could threaten safety standards at nuclear weapons facilities nationwide. At the same time, findings by DOE's watchdog office reveal that nuclear facilities cheated during mock attacks.

New Safety Standards

Congress passed legislation in 2002 requiring fines for contractors that violate occupational, safety and health criterion at nuclear weapons facilities. The legislation's goal was to spur improved worker protection policies and greater consistency of protection. However, DOE proposed a rule in Dec. 2003 allowing contractors to ignore the established federal safety standards and instead develop site-specific safety plans. One of the legislation's authors, Sen. Jim Bunning (R-KY), accused DOE of altering Congress' intentions with a rule that will hurt worker protections.

Critics point out that under the DOE rule contactors would be inclined to relax worker protections. Often, the government provides incentives for early completion of projects and the new rule would allow contractors to lower safety standards, which often slow down work. Additionally, the site-specific safety plans would most likely use low standards to avoid fines from violations. Violations and fines also provide valuable information for evaluating the quality of worker protections at a facility. By allowing facilities to rig the system and avoid violations, DOE is hiding problems rather than solving them.

John Conway, chairman of the Defense Nuclear Facilities Safety Board at the Energy Department, stated 100,000 workers at these facilities would see risks from weakened standards. DOE defended the rule saying it will give contractors flexibility to create safety plans that address specific site hazards. Certain dangers covered under federal rules do not exist at every facility. DOE contends the rule will fully protect workers.

See the related New York Times article for more information.

Cheating Before Mock Attacks

A report issued by DOE's inspector general on Jan. 23 revealed a Tennessee nuclear weapons facility cheated in a test of its preparation and security system. The facility was tipped off about surprise-simulated attacks. The

mock attacks were intended to help facilities develop a safety plan. The plant was expected to pass only two of the four tests; when all were passed, DOE launched an investigation.

The investigation determined that guards were allowed to view computer simulations before the tests. Additionally, other incidents of cheating were found at nuclear facilities across the U.S. The allegations were based on interviews with former and current facility guards.

The National Nuclear Security Administration authored a letter in which the agency stated that if the attacks were compromised and information collected was subsequently skewed, then “the results could have extremely significant effects in a way that is entirely unacceptable.”

Information on simulations results is usually classified as national security materials.

Safety standards and security practices at nuclear facilities are alarming and seem contradictory to the administration’s guise of strengthening homeland security. Improvements in safety and security must begin with honest and open assessments of the problems rather than manipulative techniques to hide the problems. It is the administration’s responsibility to ensure the safety of those that work at or live near nuclear facilities.

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