Patterson Belknap

Patterson Policy Watch – A Resource for the Nonprofit Sector

Welcome to the *Patterson Policy Watch*, which tracks key legal and policy developments that matter to the nonprofit sector. In response to the rapidly evolving landscape under the new presidential administration, Patterson Belknap's Tax-Exempt Organizations Group is highlighting executive actions, agency directives, legislative updates, and judicial responses that have the potential to impact nonprofit organizations and the communities they serve.

Below is a digest of select developments from the past week through September 9, 2026, which are organized broadly by issue area. We note that this is not a comprehensive list of all updates that may potentially be relevant to tax-exempt organizations. We will continue to provide regular updates to the *Patterson Policy Watch* to help you anticipate and navigate policy and legal developments. You can also view prior editions of the *Patterson Policy Watch* here.

Special Report: Proposed Regulations Under Section 501(c)(3) Regarding Racial Nondiscrimination Would Prohibit Affirmative Action and Similar Race-Conscious Policies and Programs in Private Schools

On September 3, the Internal Revenue Service (IRS) and Treasury Department (Treasury) issued proposed regulations that, if made final, would provide that a private school does not qualify for exemption under Section 501(c)(3) of the Internal Revenue Code if it "discriminates on the basis of race, color, or national or ethnic origin in administration of its educational, admissions, scholarship, athletic, or other policies, based on the fundamental public policy of the United States against such practices." As a result, Section 501(c)(3) private schools could no longer engage in affirmative action or similar race-conscious policies and programs intended to increase diversity without jeopardizing their tax-exempt status.

- **Explanation of Provisions**: The Notice of Proposed Rulemaking (NPRM) explains: "These proposed regulations would provide that ***all forms of racial discrimination in education, regardless of the intent behind or the legality of such discrimination*** (for example, where such discrimination is defended as serving remedial or diversity-related objectives), ***are against a fundamental public policy of the United States*** and thus preclude a school's exemption from Federal income tax under section 501(c)(3)." In so doing, the proposed regulations would make clear that discriminating based on race, color, or national or ethnic origin for any purpose by a private school is contrary to a fundamental public policy of the United States.

- **Evidence of Fundamental Public Policy**: The proposed regulations are based on the doctrine established by the Supreme Court in *Bob Jones University v. United States*, 461 U.S. 574 (1983) that violations of fundamental public policy (such as racial discrimination in education) disqualify an entity for tax-exemption under Section 501(c)(3).The NPRM states that the specific public policy underlying the proposed regulations is evidenced by antidiscrimination law such as the Equal Protection Clause of the Fourteenth Amendment, the Civil Rights Act of 1964, Supreme Court cases including *Brown v. Board of Education*, 347 U.S. 483 (1954), *Runyon v. McCrary*, 427 U.S. 160 (1976), *Bob Jones University v. United States*, and *Students for Fair Admissions, Inc. v. President and Fellows of Harvard College, 600 U.S. 181 (2023)*, as well as historic and more recent Executive Branch actions to ensure racial nondiscrimination is instituted throughout the United States, including Executive Order 10730 (Sep. 24, 1957) (authorizing the use of the National Guard to enforce the desegregation of public schools in Little Rock, Arkansas), Executive Order 14173 (Jan. 21, 2025) (directing agency heads to create plans to deter illegal discrimination, including at institutions of higher education), and Executive Order 14280 (April 23, 2025) (directing the Secretary of Education and Attorney General to take action aimed at preventing racial discrimination in school disciplinary systems).

- **Impact on Existing IRS Guidance**: If finalized, the proposed regulations would modify Revenue Procedure 75-50, which currently sets forth guidelines for determining whether private schools have racially nondiscriminatory policies required under Section 501(c)(3). The modification would make clear that a school's policies or programs favoring racial minority groups are impermissible under Section 501(c)(3), ***even when their purpose and effect is to further a school's racially nondiscriminatory policy or is not otherwise unlawful***. While the Revenue Procedure previously allowed for such affirmative action policies, the proposed regulations would deem them to be impermissible racially discriminatory policies incompatible with Section 501(c)(3) status. Accordingly, under the proposed regulations, a private school will not qualify for Section 501(c)(3) status if it has any educational policy, admissions policy, scholarship or loan program, athletic program, or other school-administered or supported program that discriminates on the basis of race, color, or national or ethnic origin for any purpose.

- **Exception for Religiously Based Selection Criteria**: The NPRM also provides a religious carve out that confirms that Section 501(c)(3) ***private schools can continue to select students on the basis of their religious affiliation*** and to maintain a religious mission, curriculum, or program of observance under the proposed regulations. Such religiously-based selection criteria are *not* deemed to be impermissible discrimination under Section 501(c)(3), even if members of the relevant religious community share ancestry or ethnic characteristics, as long as students are selected based *solely* on their religion and not on their ancestry or ethnicity. The NPRM and proposed regulations do not address programs that use sex or gender as selection criteria.

- **Impact on Charitable Giving and Scholarships**: The NPRM notes that the proposed regulations ***may affect the charitable giving behavior of donors who wish to provide scholarships or loans where race, ethnicity, or national origin are included in the eligibility criteria***. While private schools would no longer be able to provide this type of financial assistance under the proposed regulations, the NPRM notes that donors could use alternative eligibility criteria such as income, geography, or first-generation student status to ultimately benefit a similar population of students. The NPRM also observes that private schools may incur legal and administrative costs to bring any race-based scholarship endowment funds into compliance with the proposed regulations.

- **Application**: The proposed regulations would apply to private primary, secondary, and high schools, as well as colleges and universities, in each case that qualify under Section 501(c)(3). The NPRM estimates that the proposed regulations may affect 18,000 of these schools and 750,000 students attending such schools who may qualify for scholarships on the basis of race, ethnic, or national identity.

- **Effective Date**: The proposed regulations would affect private schools in taxable years beginning after May 31, 2027, which, as the NPRM states, "is after the final regulations are expected to be published." The NPRM makes clear that there is no grandfathering for preexisting policies under the proposed regulations, as the proposed applicability date is intended to "allow any private schools that may need to amend their existing policies, including admissions or scholarship policies, to do so before the beginning of any taxable year to which the final regulations are expected to apply."

- **Full Text of Proposed Regulations**: Proposed Treasury Regulations § 1.501(c)(3)-2 would provide as follows:
  - (a) *In general*. A private school (as defined in paragraph (c) of this section) must be operated exclusively for one or more exempt purposes (as defined in § 1.501(c)(3)-1(d)) to be an organization described in section 501(c)(3) of the Internal Revenue Code (Code). A private school that fails to satisfy the nondiscrimination requirement of paragraph (b) of this section is not an organization described in section 501(c)(3) with respect to any taxable year of the private school described in paragraph (d) of this section.
  - (b) *Nondiscrimination requirement*. A private school is not operated exclusively for exempt purposes if it adopts, maintains, or enforces any policy or practice that discriminates on the basis of race, color, or national or ethnic origin in the administration of any educational policy, admissions policy, scholarship or loan program, athletic program, or other school-administered or school-supported program. For purposes of this section, discrimination on the basis of race, color, or national or ethnic origin includes any discrimination on the basis of race, color, or national or ethnic origin for any purpose.
  - (c) *Private school defined*. For purposes of this section, the term *private school* means an organization described in section 501(c)(3) (determined without regard to the nondiscrimination requirement of paragraph (b) of this section) and classified as an educational organization described in section 170(b)(1)(A)(ii) of the Code. The term private school does not include a governmental unit, an agency or instrumentality of a governmental unit, or an organization that is owned or operated by an agency or instrumentality of a governmental unit. For purposes of this definition, the term *governmental unit* means the United States, a State, an Indian Tribal government (within the meaning of section 7701(a)(40) of the Code), the District of Columbia, a possession of the United States, or a political subdivision of any of the foregoing.
  - (d) *Applicability date*. This section applies with respect to the taxable year of any private school beginning after May 31, 2027.
- **Comments**: Public comments and requests for a public hearing must be submitted by November 3, 2026.

Health

- September 2: Several states sued the Department of Health and Human Services (HHS) and the Centers for Medicare and Medicaid Services over a rule blocking federal reimbursements for gender affirming care. The rule, which was issued by the Centers for Medicare and Medicaid Services on August 11, 2026, would prohibit the use of federal Medicaid and Children's Health Insurance Program dollars to fund certain gender-affirming treatments. The states' lawsuit alleges that HHS and the Centers for Medicare and Medicaid Services violated the Administrative Procedure Act and the Spending Clause of the Constitution. The plaintiffs seek declaratory and injunctive relief; the rule goes into effect on October 13, 2026.

Other

- September 1: Representatives Lloyd Doggett (D-TX) and Terri Sewell (D-AL), both of whom are members of the House Committee on Ways and Means, sent a letter to IRS CEO Frank Bisignano regarding reporting "that Treasury Secretary Scott Bessent and his aides are preparing a campaign of audits, revocations of tax-exempt status, and back-tax and penalty assessments against a slate of charitable organizations … selected not for any identified violation of the tax laws but for their perceived opposition to this Administration." The September 1 letter also renews the requests the representatives set out in their April 14 letter to IRS CEO Bisignano, which was covered in the April 21, 2026 issue of the *Patterson Policy Watch*.
  - September 2: Senators Raphael Warnock (D-GA) and Ron Wyden (D-OR) sent a letter to Treasury Secretary Scott Bessent and IRS CEO Frank Bisignano regarding the same reporting. The senators' letter requests that certain information be provided by September 15, 2026.

Legislative Watch

- On September 3, H.R. 10258, the "Protecting the Rights of Organizations Fairly Act" or the "PROOF Act," was introduced in the House by Representatives Lloyd Doggett (D-TX) and Terri Sewell (D-AL) and referred to the House Committee on Ways and Means. The bill would amend the Internal Revenue Code of 1986 to codify certain due process protections with respect to examinations of tax-exempt organizations, including detailed notice requirements, record-keeping and disclosure obligations, information document request standards, rights to supervisory and closing conferences, and a proposed adverse determination process with appeal rights through the IRS Independent Office of Appeals.

Laura E. Butzel	212.336.2970	lebutzel@pbwt.com
Robin Krause	212.336.2125	rkrause@pbwt.com
John Sare	212.336.2760	jsare@pbwt.com
Susan M. Vignola	212.336.2256	svignola@pbwt.com
Justin S. Zaremby	212.336.2194	jszaremby@pbwt.com
Tiffany N. Tam	212.336.2520	ttam@pbwt.com
Peter B. Franklin	212.336.2978	pfranklin@pbwt.com
Jack McGlone	212.336.2974	jmcglone@pbwt.com
Colleen O'Leary	212.336.2516	coleary@pbwt.com