



# Tax-Exempt Organizations: Political Activity Restrictions and Disclosure Requirements

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## Summary

As the 2010 election cycle heats up, attention is focused on the political activities of tax-exempt § 501(c) organizations. This is due in large part to a recent Supreme Court case, *Citizens United v. FEC*, which invalidated long-standing prohibitions in federal campaign finance law on corporate and labor union campaign treasury spending. These prohibitions had affected § 501(c) organizations because many are incorporated and because all organizations (regardless of corporate status) could not serve as conduits for corporate or labor union treasury funds. Thus, post-*Citizens United*, § 501(c) organizations are among the entities operating with less restriction under federal campaign finance law. As a result, it is expected there will be increased political activity by the tax-exempt sector in 2010 in comparison with past election cycles.

Due to this expectation, significant attention is being paid to the regulation of § 501(c) groups under the Internal Revenue Code (IRC). Under the IRC, the ability of § 501(c) organizations to engage in political activity, such as electioneering and lobbying, depends on the type of organization. For example, the charitable organizations described in § 501(c)(3) may not engage in any campaign activity and may only conduct a limited amount of lobbying. Meanwhile, § 501(c)(4) social welfare organizations, § 501(c)(5) labor unions, and § 501(c)(6) trade associations may engage in campaign activity (so long as such activity and any other non-exempt purpose activity is not their primary activity) and an unlimited amount of lobbying. Other types of § 501(c) organizations appear to either be subject to restrictions like those imposed on § 501(c)(3) organizations or treated similarly to § 501(c)(4), (c)(5), and (c)(6) organizations.

While some types of organizations are permitted to engage in election-related activities under the IRC, § 501(c) organizations are subject to tax for making certain political expenditures. The tax is imposed on the lesser of the taxable expenditures or the organization's net investment income. Thus, for organizations with little or no net investment income or those making low-cost expenditures, the tax is of minimal import. For other groups, however, it might serve as a disincentive to directly engage in the activities giving rise to the taxable expenditures.

Finally, § 501(c) organizations must report information regarding their political activities to the IRS on Schedule C of the Form 990. This information must be made publicly available by the organization and the IRS. While information on certain donors also must be reported to the IRS on the Form's Schedule B, any identifying information about those donors is generally not subject to public disclosure.

While this report discusses the political activity limitations in the IRC, it is important to realize that organizations must also comply with applicable election and lobbying laws. For analysis of the intersection between tax and campaign finance laws, see CRS Report R40141, *501(c)(3) Organizations and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by (name redacted) and (name redacted); CRS Report RL34447, *Churches and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by (name redacted) and (name redacted); CRS Report R40183, *501(c)(4) Organizations and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by (name redacted) and (name redacted); and CRS Report RS22895, *527 Groups and Campaign Activity: Analysis Under Campaign Finance and Tax Laws*, by (name redacted) and (name redacted). For discussion of the applicability of federal lobbying law to tax-exempt organizations, see CRS Report 96-809, *Lobbying Regulations on Non-Profit Organizations*, by (name redacted).

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There are approximately 30 types of entities that qualify for federal tax-exempt status as organizations described in section 501(c) of the Internal Revenue Code (IRC). The most common types are

- § 501(c)(3) charitable organizations,
- § 501(c)(4) social welfare organizations,
- § 501(c)(5) labor unions, and
- § 501(c)(6) trade associations.

Whether a § 501(c) organization may engage in political activity, such as lobbying or campaign activity, under the IRC depends on the subparagraph in which it is described. This report analyzes the IRC limitations on political activity by tax-exempt organizations, focusing on these four types of organizations. It ends with a discussion of the IRC reporting and disclosure requirements.

While this report discusses the political activity limitations in the IRC, it is important to realize that organizations must also comply with applicable election and lobbying laws. For analysis of the intersection between tax and campaign finance laws, see CRS Report R40141, *501(c)(3) Organizations and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by (name redacted) and (name redacted); CRS Report RL34447, *Churches and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by (name redacted) and (name redacted); CRS Report R40183, *501(c)(4) Organizations and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by (name redacted) and (name redacted); and CRS Report RS22895, *527 Groups and Campaign Activity: Analysis Under Campaign Finance and Tax Laws*, by (name redacted) and (name redacted). For discussion of the applicability of federal lobbying law to tax-exempt organizations, see CRS Report 96-809, *Lobbying Regulations on Non-Profit Organizations*, by (name redacted).

## Political Activity by IRC § 501(c)(3) Organizations

### Organizational Definition

The organizations described in IRC § 501(c)(3) are commonly referred to as charitable organizations. The section describes these organizations as

organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.<sup>1</sup>

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<sup>1</sup> IRC § 501(h) provides a test for measuring the amount of lobbying done by an organization. It is discussed below.

There are two types of § 501(c)(3) organizations: public charities and private foundations. Public charities receive contributions from a variety of sources whereas private foundations receive contributions from limited sources. Due to fear of abuse, private foundations are subject to stricter regulation than public charities. This includes additional restrictions on their political activities, as discussed below.

## **Summary of the Definition’s Restrictions on Political Activity**

The organizational definition in § 501(c)(3) restricts the ability of these organizations to participate in political activity in two ways: (1) they may only conduct an insubstantial amount of lobbying and (2) they may not intervene in political campaigns. Organizations that violate either restriction may lose their tax-exempt status and the eligibility to receive deductible contributions, among other consequences. The lobbying restriction and political campaign prohibition are discussed in detail below.

## **Legislative History of the Political Activity Restrictions**

The lobbying limitation was enacted in 1934 and the political campaign prohibition was enacted in 1954. The legislative history of both provisions is sparse.

In 1919, the Treasury Department took the position that organizations “formed to disseminate controversial or partisan propaganda” were not “educational” for purposes of qualifying for tax-exempt status under the precursors to § 501(c)(3).<sup>2</sup> One consequence of this rule was that contributions to these organizations were not deductible. Several lawsuits were brought that challenged this treatment, but no clear standard emerged from the court decisions—some courts denied the deduction if the organization advocated for any type of change, whereas others looked at factors such as how controversial the advocacy was or if the organization’s actions were intended to influence legislation.<sup>3</sup> In what is generally recognized as the seminal case, *Slee v. Commissioner*,<sup>4</sup> the U.S. Court of Appeals for the Second Circuit used another rationale. In that decision, the court held that contributions to an organization were not deductible because it did not appear that the lobbying was limited to causes that furthered the organization’s charitable purpose.<sup>5</sup>

With this background, Congress enacted the lobbying limitation as part of the Revenue Act of 1934. There is very little legislative history for the provision, but it appears that Congress was concerned with organizations that lobby also being able to receive tax-deductible contributions.<sup>6</sup> While discussing the provision on the Senate floor, one Member complained about the

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<sup>2</sup> Treas. Reg. 45, Art. 517 (1919).

<sup>3</sup> For a discussion of the Treasury position and these cases, see William J. Lehrfeld, *The Taxation of Ideology*, 19 CATH. U. L. REV. 50 (1969); Tommy F. Thompson, *The Availability of the Federal Educational Tax Exemption for Propaganda Organizations*, 18 U.C. DAVIS L. REV. 487 (1985); Laura B. Chisholm, *Exempt Organizations Advocacy: Matching the Rules to the Rationales*, 63 IND. L.J. 201 (1988); Miriam Galston, *Lobbying and the Public Interest: Rethinking the Internal Revenue Code’s Treatment of Legislative Activities*, 71 TEX. L. REV. 1269 (1993); Oliver A. Houck, *On The Limits of Charity: Lobbying, Litigation, and Electoral Politics by Charitable Organizations under the Internal Revenue Code and Related Laws*, 69 BROOK. L. REV. 1 (2003).

<sup>4</sup> 42 F.2d 184 (2<sup>nd</sup> Cir. 1930).

<sup>5</sup> See *id.* at 185.

<sup>6</sup> See 78 CONG. REC. 5,959 (1934) (statement by Sen. Harrison).

deductibility of donations that were made for “selfish” reasons and specifically mentioned an organization with which he was apparently having problems.<sup>7</sup> Although this Member apparently believed the provision was too broad in that it applied to organizations without “selfish motives,”<sup>8</sup> other Members argued that all contributions to organizations that lobby should be nondeductible because of the difficulty in trying to distinguish between organizations that deserve the benefit and those that do not.<sup>9</sup> It has also been suggested that Congress enacted the provision in order to codify the *Slee* decision.<sup>10</sup> Although this may be true, it should be noted that the *Slee* test and the lobbying provision are not identical. This is because the focus of the test under *Slee* is whether the lobbying furthers the organization’s tax-exempt purpose, whereas the focus of the lobbying provision is whether the lobbying is a substantial part of the organization’s activities.

The 1934 Act had also included a provision that would have restricted the ability of charities to participate in partisan politics. However, that limitation was removed in conference, apparently because of concerns it was too broad.<sup>11</sup>

The political campaign prohibition was enacted as part of the Internal Revenue Code of 1954. The provision was added by Senator Lyndon Johnson as a floor amendment. Upon introducing the amendment, Senator Johnson analogized it to the lobbying limitation; however, he mischaracterized the lobbying limitation by saying that organizations that lobbied were denied tax-exempt status, as opposed to only those organizations that substantially lobbied.<sup>12</sup> The legislative history contains no further discussion of the prohibition, including whether Senator Johnson’s overly-broad description of the lobbying provision and inaccurate analogy were noticed. Although Senator Johnson’s motives behind the provision are not clear from the legislative history, it has been suggested that he proposed it either as a way to get back at an organization that had supported an opponent or because he wished to offer an alternative to another Senator’s proposal that would have denied tax-exempt status to organizations making grants to organizations or individuals that were deemed to be subversive.<sup>13</sup>

## **Lobbying by § 501(c)(3) Organizations**

The organizational definition in IRC § 501(c)(3) states that “no substantial part” of an organization’s activities may be “carrying on propaganda, or otherwise attempting, to influence legislation” (i.e., lobbying).

### **What Is Lobbying?**

Lobbying includes activities that attempt to influence legislation by (1) contacting, or urging the public to contact, legislators about proposing, supporting, or opposing legislation and (2)

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<sup>7</sup> 78 CONG. REC. 5,861 (1934) (statement by Sen. Reed).

<sup>8</sup> *Id.*

<sup>9</sup> See 78 CONG. REC. 5,861 and 5,959 (1934) (statements by Sens. Harrison and La Follette).

<sup>10</sup> See e.g., Gen. Couns. Mem. 34289 (May 3, 1970). General Counsel Memoranda contain legal interpretations of the IRC by the IRS. They have no precedential value. They are available through such services as Lexis and Westlaw.

<sup>11</sup> See 78 CONG. REC. 7,831 (1934) (statement by Rep. Hill).

<sup>12</sup> See 100 CONG. REC. 9,604 (1954).

<sup>13</sup> See Judith E. Kindell and John Francis Reilly, *Election Year Issues*, IRS 2002 EO CPE TEXT, 448-51 (2002).



advocating for or against legislation.<sup>14</sup> Thus, it includes direct lobbying (contacting governmental officials) and grassroots lobbying (appeals to the electorate or general public). “Legislation” includes action by any legislative body and by the public through such things as referenda and initiatives.<sup>15</sup> “Action” includes the introduction, amendment, enactment, defeat, or repeal of such things as acts, bills, and resolutions.<sup>16</sup> It also appears to include Senate confirmation of judicial and executive branch nominations.<sup>17</sup> An organization’s advocacy activities may be lobbying even if legislation is not actually pending.<sup>18</sup> Furthermore, an organization may be treated as lobbying if it does such things as make a contribution or lend money on favorable terms to an entity that lobbies.

Lobbying generally does not include providing testimony in response to an official request by a legislative body.<sup>19</sup> It also does not include contacting executive, judicial, and administrative bodies on matters other than legislation.<sup>20</sup> Additional examples of activities that may not be lobbying include conducting and publishing nonpartisan analysis, study, or research; discussing broad social issues, so long as specific legislation is not discussed; and contacting legislative bodies about legislation that relates to the organization’s existence or status.<sup>21</sup>

### **What Is “No Substantial Part”?**

In order to determine whether lobbying is a substantial part of an organization’s activities, the organization may elect under IRC § 501(h) to measure its lobbying expenditures against objective, numerical standards.<sup>22</sup> If the election is not made, the organization is subject to the “no substantial part” test, which has no bright-line standards. Most organizations do not make the election, and some, including churches and private foundations, are not allowed to make it.<sup>23</sup>

### ***IRC § 501(h) election***

Organizations that make the § 501(h) election measure their lobbying activities against the limits in IRC § 4911. Organizations whose lobbying expenditures exceed the limits in § 4911 for total lobbying expenditures and grass roots expenditures are subject to an excise tax equal to 25% of the excess. In order to not be taxed for excessive lobbying, an organization may not spend more than 20% of its first \$500,000 of expenditures on lobbying, nor more than 15% of its second

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<sup>14</sup> See Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii).

<sup>15</sup> See *id.*

<sup>16</sup> See Gen. Couns. Mem. 39694 (January 22, 1988); IRC § 4911(e)(3).

<sup>17</sup> See IRS Notice 88-76, 1988-2 C.B. 392; Gen. Couns. Mem. 39694 (January 22, 1988).

<sup>18</sup> See *e.g.*, *Christian Echoes Nat’l Ministry Inc. v. United States*, 470 F.2d 849, 855 (10<sup>th</sup> Cir. 1972).

<sup>19</sup> See Rev. Rul. 70-449, 1970-2 C.B. 111.

<sup>20</sup> See Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii).

<sup>21</sup> See Rev. Rul. 64-195, 1964-2 C.B. 138; Gen. Couns. Mem. 36127 (January 2, 1975); IRC § 4945(e); Treas. Reg. § 53.4945-2(d).

<sup>22</sup> IRC § 501(h) was enacted as part of the Tax Reform Act of 1976, P.L. 94-455.

<sup>23</sup> Some churches lobbied not to be eligible for the election because they were concerned that their inclusion would be interpreted as congressional approval of *Christian Echoes Nat’l Ministry, Inc. v. United States*, 470 F.2d 849 (10<sup>th</sup> Cir. 1972), in which the U.S. Court of Appeals for the Tenth Circuit held that the lobbying limitation did not violate a church’s rights under the First Amendment. The legislative history of the election provision explicitly states that its enactment does not indicate congressional approval or disapproval of the *Christian Echoes* decision. See Joint Committee on Taxation, *General Explanation of the Tax Reform Act of 1976*, JCS-33-76, at 416 (1976).

\$500,000 of expenditures, nor more than 10% of its third \$500,000 of expenditures, nor more than 5% of its remaining expenditures, and no more than \$1 million on lobbying in the year. In order not to be taxed for excessive grass roots lobbying, the organization may not spend more than 5% of its first \$500,000 of expenditures on grass roots lobbying, nor more than 3.75% of its second \$500,000 of expenditures, nor more than 2.5% of its third \$500,000 of expenditures, nor more than 1.25% of its remaining expenditures, and no more than \$250,000 on grass roots lobbying in the year.

The election also provides a safe harbor so organizations that do not exceed a certain limit will not lose their § 501(c)(3) status due to substantial lobbying. Specifically, an organization will not lose its exempt status so long as its lobbying expenditures do not exceed 150% of the § 4911 limitations over a four year period. Thus, depending on its activities in prior years, an organization could conduct lobbying in the current year that is significant enough to be subject to tax, but not lose its tax-exempt status.

### *Non-Electing Organizations*

For organizations that do not make the election and those that cannot (e.g., private foundations and churches), the determination as to whether they have conducted more than an insubstantial amount of lobbying is dependent on the facts and circumstances of each case. Case law suggests that “no substantial part” is between 5% and 20% of the organization’s expenditures.<sup>24</sup> However, there is no bright-line test and the percentage of expenditures spent on lobbying is not necessarily determinative.<sup>25</sup> Rather, courts have examined the lobbying in the broad context of the organization’s purpose and activities by looking at such things as how important lobbying is to the organization’s purpose, the amount of time devoted to lobbying as compared with other activities, and the extent to which the organization is continuously involved in lobbying.<sup>26</sup>

Unlike electing organizations, non-electing public charities are only subject to an excise tax on their lobbying expenditures if they lose their exempt status because of substantial lobbying.<sup>27</sup> The tax equals 5% of the organization’s lobbying expenditures, and the same tax may also be imposed on the organization’s manager. Some organizations, including churches, are not subject to the tax.

Private foundations, on the other hand, must generally pay an excise tax on any lobbying expenditures they make.<sup>28</sup> The tax equals 10% of the expenditures. Additionally, a foundation manager who agrees to the expenditure may individually be subject to a tax equal to 2.5% of the expenditure, limited to \$5,000. If the foundation fails to timely correct the expenditure, it is subject to an additional tax equal to 100% of the expenditure and the manager may be subject to an additional tax equal to 50% of the expenditure, limited to \$10,000.

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<sup>24</sup> See *Seasongood v. Comm’r*, 227 F.2d 907, 912 (6<sup>th</sup> Cir. 1955); *Haswell v. United States*, 500 F.2d 1133, 1146-47 (Ct. Cl. 1974).

<sup>25</sup> See *Christian Echoes Nat’l Ministry, Inc. v. United States*, 470 F.2d 849, 855 (10<sup>th</sup> Cir. 1972); *Haswell*, 205 Ct. Cl. at 1142; *Krohn v. United States*, 246 F. Supp. 341, 347-48 (D. Colo. 1965); see also, Gen. Couns. Mem. 36148 (January 28, 1975).

<sup>26</sup> See *Christian Echoes*, 470 F.2d at 855-86; *Haswell*, 205 Ct. Cl. at 1145; *Krohn*, 246 F. Supp. at 348-49.

<sup>27</sup> IRC § 4912.

<sup>28</sup> IRC § 4945. This section was enacted as part of the Tax Reform Act of 1969 (P.L. 91-172).



## **Regan v. Taxation With Representation of Washington**

In 1983, the Supreme Court ruled in *Regan v. Taxation With Representation of Washington* that the lobbying limitation is constitutional.<sup>29</sup> In that case, the IRS denied the application of Taxation With Representation of Washington (TWR) for § 501(c)(3) status because a substantial amount of the group's activities would be lobbying. TWR argued that the lobbying limitation violated its right to freedom of speech under the First Amendment. The group also argued that it was being denied equal protection under the Fifth Amendment because § 501(c)(19) veterans' organizations were allowed to lobby substantially and still qualify for tax-exempt status and to receive tax-deductible contributions.

The Supreme Court rejected both claims. With respect to the First Amendment, the Court found that Congress had not prevented TWR from speaking, but had simply chosen not to subsidize it by means of the tax exemption and tax-deductible contributions.<sup>30</sup> The court also noted that TWR could qualify for exemption under § 501(c)(4) and receive deductible contributions for its non-lobbying activities by setting up a separate § 501(c)(3) organization.<sup>31</sup> With respect to the Fifth Amendment, the Court stated that the test to determine whether the classification was constitutionally permissible was whether it bore a rational relationship to a legitimate governmental purpose.<sup>32</sup> Noting that legislatures have broad discretion when it comes to making classifications for tax purposes, the Court found that it was not irrational for Congress to decide not to extend the taxpayer-funded benefit of unlimited lobbying to charities because of concerns they may lobby for their members' benefit.<sup>33</sup> The Court also stated that distinguishing charities from veterans organizations was permissible because the United States "has a longstanding policy of compensating veterans for their past contributions by providing them with numerous advantages."<sup>34</sup>

## **Political Campaign Activity by § 501(c)(3) Organizations**

The organizational definition in IRC § 501(c)(3) prohibits these organizations from "participating in, or intervening in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office," but does not further elaborate on the prohibition. Treasury regulations define candidate as "an individual who offers himself, or is proposed by others, as a contestant for an elective public office, whether such office be national, State, or local."<sup>35</sup> As to what types of activities are prohibited, the regulations add little besides specifying that they include "the publication or distribution of written or printed statements or the making of oral statements on behalf of or in opposition to such a candidate."<sup>36</sup>

Thus, the statute and regulations do not offer much insight as to what activities are prohibited. Clearly, § 501(c)(3) organizations may not do such things as make statements that endorse or

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<sup>29</sup> 461 U.S. 540 (1983).

<sup>30</sup> *See id.* at 545-46.

<sup>31</sup> *See id.* at 544.

<sup>32</sup> *See id.* at 547.

<sup>33</sup> *See id.* at 547 and 550.

<sup>34</sup> *Id.* at 550-51.

<sup>35</sup> Treas. Reg. § 1.501(c)(3)-1(c)(3)(iii).

<sup>36</sup> *Id.*

oppose a candidate, publish or distribute campaign literature, or make any type of contribution, monetary or otherwise, to a political campaign.

On the other hand, § 501(c)(3) organizations are allowed to conduct activities that are political in nature but are not related to elections, such as lobbying for or against legislation<sup>37</sup> and supporting or opposing the appointment of individuals to nonelective offices. Additionally, § 501(c)(3) organizations may engage in certain election-related activities so long as the activities do not indicate a preference for or against any candidate. Whether such an activity is campaign intervention depends on the facts and circumstances of each case. The following examples show some of the ways in which the IRS has indicated that an activity might be biased. As will be seen, some biases can be subtle and it is not necessary for the organization to expressly mention a candidate by name.

## **Examples of Activities**

### *Voter Guides*

Section 501(c)(3) organizations may create and/or distribute voter guides and similar materials that do not indicate a preference towards any candidate. The guide must be unbiased in form, content, and distribution. According to the IRS, there are numerous ways in which a guide may be biased, and the determination will depend on the facts and circumstances of each case. For example, a guide could display a bias by not including all candidates on an equal basis. Another way a guide could be biased is by rating candidates, such as evaluating candidates and supporting a slate of the best-qualified candidates, even if the criteria are nonpartisan (e.g., based on professional qualifications).<sup>38</sup> A voter guide could also indicate a bias by comparing the organization's position on issues with those of the candidates.<sup>39</sup> A more subtle way in which a guide may show bias is by only covering issues that are important to the organization, as opposed to covering a range of issues of interest to the general public.<sup>40</sup>

Some guides consist of candidate responses to questions provided by the organization. According to the IRS, factors that tend to show these guides are candidate-neutral include the following:

- the questions and descriptions of the issues are clear and unbiased;
- the questions provided to the candidates are identical to those included in the guide;
- the candidates' answers have not been edited;
- the guide puts the questions and appropriate answers in close proximity to each other;

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<sup>37</sup> However, "no substantial part" of a § 501(c)(3) organization's activities may be lobbying. For more information, see CRS Report RL33377, *Tax-Exempt Organizations: Political Activity Restrictions and Disclosure Requirements*, by (name redacted).

<sup>38</sup> See *Ass'n of the Bar of the City of New York v. Comm'r*, 858 F.2d 876 (2d Cir. 1988); Rev. Rul. 67-71, 1967-1 C.B. 125.

<sup>39</sup> See IRS FS-2006-17 (Feb. 2006).

<sup>40</sup> See Rev. Rul. 78-248, 1978-1 C.B. 154.

- the candidates are given a reasonable amount of time to respond to the questions; and
- if the candidates are given limited choices for an answer to a question (e.g., yes/no, support/oppose), they are given a reasonable opportunity to explain their positions.<sup>41</sup>

Other factors that may be important include the timing of the guide's distribution and to whom it is distributed. For example, the IRS ruled that a § 501(c)(3) organization could include a compilation of Members' voting records on issues important to it and its position on those issues in the edition of its monthly newsletter published after the close of each Congress.<sup>42</sup> The newsletter was sent to the usual small number of subscribers and not targeted to areas where elections were occurring. In this specific situation, the IRS stated that the publication was permissible because it was not timed to an election or broadly distributed.

### *Conducting Public Forums*

Section 501(c)(3) organizations may conduct unbiased and nonpartisan public forums where candidates speak or debate. According to the IRS, factors that tend to show a public forum is unbiased and nonpartisan include the following:

- all legally qualified candidates are invited;
- the questions are prepared and presented by a nonpartisan independent panel;
- the topics and questions cover a broad range of issues of interest to the public;
- all candidates receive an equal opportunity to present their views; and
- the moderator does not comment on the questions or imply approval or disapproval of the candidates.<sup>43</sup>

### *Inviting Candidates to Speak*

A § 501(c)(3) organization may invite a candidate to speak at its functions without it being prohibited campaign activity. According to the IRS, factors that tend to indicate the event was permissible include the organization provided an equal opportunity to speak at similar events to the other candidates; the organization did not indicate a preference for or against any candidate; and no fund-raising occurred at the event.<sup>44</sup> Section 501(c)(3) organizations may also invite candidates to speak in their non-candidate capacity.<sup>45</sup> Factors indicating that no campaign intervention occurred include (1) the individual was chosen to speak solely for non-candidacy reasons; (2) the individual spoke only in his or her non-candidate capacity; (3) no reference to the upcoming election was made; (4) no campaign activity occurred in connection with the individual's attendance; (5) the organization maintained a nonpartisan atmosphere at the event; and (6) the organization's communications announcing the event clearly indicated the non-

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<sup>41</sup> See IRS FS-2006-17 (Feb. 2006); Rev. Rul. 78-248, 1978-1 C.B. 154.

<sup>42</sup> See Rev. Rul. 80-282, 1980-2 C.B. 178.

<sup>43</sup> See Rev. Rul. 86-95, 1986-2 C.B. 73; Rev. Rul. 2007-41, 2007-1 C.B. 1421.

<sup>44</sup> See Rev. Rul. 2007-41, 2007-1 C.B. 1421.

<sup>45</sup> See *id.*

candidate capacity in which the individual was appearing and did not mention the individual's candidacy or the election.<sup>46</sup>

### *Voter Registration*

Section 501(c)(3) organizations may conduct nonpartisan voter registration and get-out-the-vote drives.<sup>47</sup> Again, the activities may not indicate a preference for any candidate or party. According to the IRS, factors indicating that these activities are neutral include the following:

- candidates are named or depicted on an equal basis;
- no political party is named except for purposes of identifying the party affiliation of each candidate;
- the activity is limited to urging individuals to register and vote and to describing the time and place for these activities; and
- all services are made available without regard to the voter's political preference.<sup>48</sup>

### *Issue Advocacy*

Section 501(c)(3) organizations may take positions on policy issues. Because there is no rule that campaign activity occurs only when an organization expressly advocates for or against a candidate,<sup>49</sup> the line between issue advocacy and campaign activity can be difficult to discern. According to the IRS, key factors that indicate an issue advocacy communication does not cross the line into campaign intervention include the following:

- the communication does not identify any candidates for a given public office, whether by name or other means, such as party affiliation or distinctive features of a candidate's platform;
- the communication does not express approval or disapproval for any candidate's positions and/or actions;
- the communication is not delivered close in time to an election;
- the communication does not refer to voting or an election;
- the issue addressed in the communication has not been raised as an issue distinguishing the candidates;
- the communication is part of an ongoing series by the organization on the same issue and the series is not timed to an election; and
- the identification of the candidate and the communication's timing are related to a non-electoral event (e.g., a scheduled vote on legislation by an officeholder who is also a candidate).<sup>50</sup>

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<sup>46</sup> *See id.*

<sup>47</sup> *See id.* Private foundations making expenditures for these activities may be subject to tax. *See* I.R.C. § 4945.

<sup>48</sup> *See* 2002 EO CPE Text, *supra* note 13, at 379.

<sup>49</sup> *See* Rev. Rul. 2007-41, 2007-1 C.B. 1421.

<sup>50</sup> *See id.*; *see also* 2002 EO CPE Text, *supra* note 13, at 376-77.

### ***Selling Mailing Lists and Other Business Activities***

Under certain circumstances, § 501(c)(3) organizations may sell or rent goods, services, and facilities to political campaigns. This includes selling and renting mailing lists and accepting paid political advertising. According to the IRS, factors that tend to indicate the activity is not biased towards any candidate or party include the following:

- the selling or renting activity is an ongoing business activity of the organization;
- the goods, services, and facilities are available to the general public;
- the fees charged are the organization's customary and usual rates; and
- the goods, services, or facilities are available to all candidates on an equal basis.<sup>51</sup>

### ***Website Links***

A § 501(c)(3) organization could engage in campaign activity by linking its website to another website that has content showing a preference for or against a candidate.<sup>52</sup> Whether the linking is campaign intervention depends on the facts and circumstances of each case. Factors the IRS will look at include the context of the link on the organization's website, whether all candidates are represented, whether the linking serves the organization's exempt purpose, and the directness between the organization's website and the page at the other site with the biased material.<sup>53</sup>

### ***Activities of the Organization's Leaders and Members***

Members, managers, leaders, and directors of § 501(c)(3) organizations may participate in campaign activity in their private capacity. The organization can not support the activity in any way.<sup>54</sup> For example, these individuals may not express political views in the organization's publications or at its functions (this is true even if the individual pays the costs associated with the statement),<sup>55</sup> and the organization may not pay expenses incurred by the individual in making the political statement. Individuals may be identified as being associated with an organization, but there should be no intimation that their views represent those of the organization.<sup>56</sup>

### **Consequences for Engaging in Political Campaign Activity**

An organization that engages in any amount of campaign activity may lose its § 501(c)(3) status and eligibility to receive tax-deductible contributions. It may also be taxed on its political

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<sup>51</sup> See Rev. Rul. 2007-41, 2007-1 C.B. 1421; see also, 2002 EO CPE Text, *supra* note 13, at 383-84.

<sup>52</sup> See Rev. Rul. 2007-41, 2007-1 C.B. 1421. Due to possible constitutional concerns stemming from the Supreme Court's decision in *Regan v. Taxation With Representation of Washington*, 461 U.S. 540 (1983), the IRS indicated that it would not pursue cases involving a link between the website of a § 501(c)(3) organization and the home page of a related § 501(c)(4) organization. See *Memorandum For All Revenue Agents*, from Marsha A. Ramirez, Director, Exempt Organizations, Examinations, dated July 28, 2008, available at <http://www.irs.gov/pub/irs-tege/internetfielddirective072808.pdf>.

<sup>53</sup> See Rev. Rul. 2007-41, 2007-1 C.B. 1421.

<sup>54</sup> See *id.*; see also 2002 EO CPE Text, *supra* note 13, at 363-65.

<sup>55</sup> See Rev. Rul. 2007-41, 2007-1 C.B. 1421.

<sup>56</sup> See *id.*

expenditures,<sup>57</sup> either in addition to or in lieu of revocation of § 501(c)(3) status.<sup>58</sup> The tax equals 10% of the expenditures, with an additional tax equal to 100% of the expenditures imposed if the expenditures are not corrected (i.e., recovered and safeguards established to prevent future ones) in a timely manner. The organization's managers may also be subject to tax.<sup>59</sup> Other consequences for the flagrant violation of the prohibition include the IRS immediately determining and assessing all taxes due and/or seeking injunctive and other relief to enjoin the organization from making additional political expenditures and to preserve its assets.<sup>60</sup>

## **IRS Political Activity Compliance Initiative**

There has been ongoing congressional, IRS, and public concern about violations of the campaign intervention prohibition by § 501(c)(3) organizations. These concerns led the IRS to develop the Political Activity Compliance Initiative.<sup>61</sup> It has two parts: the IRS performed educational outreach to § 501(c)(3) organizations about the prohibition and used a fast-track process for reviewing possible violations. The initiative was used during the 2004, 2006, and 2008 election cycles, although the 2008 data have not yet been released. It does not appear the IRS has publicly indicated whether it will use the initiative during the 2010 election cycle.

The 2004 initiative involved the expedited review of 110 cases in which § 501(c)(3) organizations were alleged to have violated the campaign intervention prohibition. The IRS issued a written advisory in 69 of these cases, which meant that the agency determined the organization engaged in campaign activity but mitigating factors led to the organization not being penalized. Mitigating factors included that the activity was of a one-time nature or shown to be an anomaly, the activity was done in good faith reliance on advice of counsel, or the organization corrected the conduct (e.g., recovered any funds that were spent) and established safeguards to prevent future violations. The IRS revoked the tax-exempt status of five organizations (one for issues not related to campaign activity) and proposed two more revocations. The IRS did not find substantiated campaign activity in 23 of the cases, and found non-political violations of the tax laws in six other cases. The remaining five cases were still open as of the last IRS update in 2007.

While the 2004 initiative was proceeding, there were reports in various media outlets that raised the question of whether the IRS had been politically motivated in investigating the § 501(c)(3) organizations so close to the 2004 election.<sup>62</sup> In response, the IRS Commissioner asked the Treasury Inspector General for Tax Administration (TIGTA) to investigate whether the IRS had engaged in any improper activities while conducting the project. In 2005, TIGTA released its

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<sup>57</sup> See I.R.C. § 4955. A similar tax is imposed on the political expenditures of private foundations under § 4945, but it is not assessed if the § 4955 tax is assessed. Private foundations are § 501(c)(3) organizations that receive contributions from limited sources. See I.R.C. § 509.

<sup>58</sup> See H.R. Rep. 100-391(II), at 1623-24 (1987).

<sup>59</sup> A tax equal to 2.5% of the expenditures (limited to \$5,000 with respect to any one expenditure) is imposed on the organization's managers who agreed to the expenditures knowing they were political expenditures, unless the agreement is not willful and is due to reasonable cause. Any managers who refuse to correct the expenditures are subject to an additional tax equal to 50% of the expenditures (limited to \$10,000 with respect to any one expenditure).

<sup>60</sup> See I.R.C. §§ 6852, 7409.

<sup>61</sup> The 2004 report is available at [http://www.irs.gov/pub/irs-tege/final\\_paci\\_report.pdf](http://www.irs.gov/pub/irs-tege/final_paci_report.pdf). The 2006 report, which includes updated 2004 statistics, is available at [http://www.irs.gov/pub/irs-tege/2006paci\\_report\\_5-30-07.pdf](http://www.irs.gov/pub/irs-tege/2006paci_report_5-30-07.pdf).

<sup>62</sup> See, e.g., Mike Allen, *NAACP Faces IRS Investigation*, WASH. POST (Oct. 29, 2004); Vincent J. Schodolski, *Political sermons stir up the IRS: Effort to enforce tax-exempt rules or bid to bully pulpits?* CHI. TRIB. (Nov. 20, 2005).



report, which concluded that the IRS had used appropriate, consistent procedures during the initiative.<sup>63</sup>

The 2006 initiative involved 100 cases selected for examination. As of the last IRS update in 2007, 60 of these cases remained open. In the 40 closed cases, the IRS issued written advisories in 26 of them, and did not find substantiated political intervention in the other 14 cases. The IRS also identified 269 instances of § 501(c)(3) groups apparently making direct contributions to political candidates.

## **Political Activity by § 501(c)(4), (c)(5), and (c)(6) Organizations**

### **Organizational Definitions**

#### ***IRC § 501(c)(4)***

The organizations described in § 501(c)(4) include those that are commonly referred to as social welfare organizations. The section describes:

[c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes. [This paragraph] shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

Treasury regulations clarify that “[a]n organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community.”<sup>64</sup>

#### ***IRC § 501(c)(5)***

Section (c)(5) organizations are described as “labor, agricultural, or horticultural organizations.” Most of them are labor unions.

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<sup>63</sup> TIGTA Report 2005-10-035 (Feb. 2005).

<sup>64</sup> Treas. Reg. § 1.501(c)(4)-1(a)(2). The purposes described in sections IRC §§ 501(c)(3) and (c)(4) overlap, so that an organization may be able to qualify under either section. A § 501(c)(3) organization is eligible to receive tax-deductible contributions, while a § 501(c)(4) organization is not, but a § 501(c)(3) organization is more limited in the amount and types of political activity it may do. Thus, an organization that could qualify under either section will generally choose based on which is more important: receiving tax-deductible contributions or participating in political activity. With the exception of churches and related organizations, an organization that loses its § 501(c)(3) status because of political campaign activity or substantial lobbying may not then seek recognition as a § 501(c)(4) organization. *See* IRC § 504.

### **IRC § 501(c)(6)**

The organizations described in § 501(c)(6) are generally thought of as trade associations. The section describes these organizations as

[b]usiness leagues, chambers of commerce, real estate boards, boards of trade, or professional football leagues ... not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

### **Lobbying by § 501(c)(4), (c)(5), and (c)(6) Organizations**

The organizational definitions in § 501(c)(4), (c)(5), and (c)(6) do not contain any explicit limitations on lobbying. The organizations described in these three sections may participate in an unrestricted amount of lobbying so long as the lobbying is related to the organization's exempt purpose. In fact, organizations whose sole activity is lobbying may be recognized under these sections so long as they serve the appropriate tax-exempt purpose.<sup>65</sup> For example, a business association whose only activity is lobbying for and against legislation according to its members' interests may qualify for § 501(c)(6) status.<sup>66</sup>

If an organization engages in lobbying, it can impact the deductibility of any dues paid by its members. While dues are potentially deductible under IRC § 162, that section disallows a deduction for the portion of dues that represents lobbying expenditures. In general, the organization must either notify its members of the amount that is nondeductible or pay a tax on its lobbying expenditures.<sup>67</sup>

### **Political Campaign Activity by § 501(c)(4), (c)(5), and (c)(6) Organizations**

The organizational definitions in § 501(c)(4), (c)(5), and (c)(6) do not contain any explicit restrictions on political campaign activity. Thus, these organizations may engage in such activity under the tax laws. However, campaign activity (along with any other activities that do not further an exempt purpose) cannot be the organization's primary activity.<sup>68</sup>

Additionally, because a § 501(c)(4) organization must be "primarily engaged in promoting in some way the common good and general welfare of the people of the community,"<sup>69</sup> it cannot qualify for § 501(c)(4) status if it primarily serves a private benefit. Thus, it appears an organization that primarily benefits partisan interests could jeopardize its § 501(c)(4) status.<sup>70</sup>

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<sup>65</sup> See Rev. Rul. 61-177, 1961-1 C.B. 117; Rev. Rul. 71-530, 1971-2 C.B. 237.

<sup>66</sup> See Rev. Rul. 61-177, 1961-1 C.B. 117.

<sup>67</sup> See IRC § 6033(e).

<sup>68</sup> See Treas. Reg. § 1.501(c)(4)-1(a)(2)(ii); Rev. Rul. 81-95, 1981-1 C.B. 332 (ruling that lawful participation in campaign activity would not affect the § 501(c)(4) status of an organization whose primary activity was promoting social welfare); Rev. Rul. 67-368; 1967-2 C.B. 194 (ruling that an organization whose primary activity was rating candidates using non-partisan criteria did not qualify for § 501(c)(4) status); Gen. Couns. Mem. 34233 (Dec. 30, 1969).

<sup>69</sup> Treas. Reg. § 1.501(c)(4)-1(a)(2).

<sup>70</sup> See *American Campaign Academy v. Comm'r*, 92 T.C. 1053 (1989) (ruling that an organization that operates for the benefit of private interests, such as members and entities of one political party, on a more than insubstantial basis may (continued...))

## Political Activity by Other Types of § 501(c) Organizations

While the majority of § 501(c) organizations fall into one of the types discussed above, the IRC describes numerous other types of organizations. The limitations the IRC places on the ability of these organizations to participate in political activity is often less clear, and there is minimal IRS guidance on the topic. This may be because the need for guidance has not arisen due to the fact that there are not as many of these organizations and they do not appear to participate in political activities to the same extent as the organizations discussed above.

The other types of § 501(c) organizations appear to fall into two categories. The first are those that seem to be prohibited from participating in most, if not all, types of political activity. This category would likely include the § 501(c) trusts whose funds must be dedicated to their exempt purpose (e.g., § 501(c)(17) supplemental unemployment benefit trusts, § 501(c)(21) black lung benefit trusts, and § 501(c)(22) multi-employer pension plan trusts). It also appears to include the organizations that the IRS has indicated in unofficial guidance may not participate in political activities “because the subparagraph in which they are described limits them to an exclusive purpose (for example, IRC 501(c)(2) title holding companies, IRC 501(c)(20) group legal services plans).”<sup>71</sup> This rationale could also prohibit § 501(c)(10) domestic fraternal societies, for example, from participating in political activities because their net earnings must be devoted exclusively to certain purposes. To the extent that any organizations are precluded from participating in political activities, there could still be exceptions for such things as lobbying for legislation that affects the organization’s existence or status.<sup>72</sup>

The second category are those § 501(c)s that appear able to participate in political activity under the rules applicable to § 501(c)(4), (c)(5), and (c)(6) organizations. Examples would appear to include § 501(c)(7) social and recreational clubs,<sup>73</sup> § 501(c)(8) fraternal benefit societies and associations,<sup>74</sup> and § 501(c)(19) veterans’ groups.<sup>75</sup>

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(...continued)

not qualify for § 501(c)(3) status); *see also* Democratic Leadership Council v. United States, 542 F. Supp. 2d 63 (D.D.C. 2008) (ruling retroactive revocation of group’s § 501(c)(4) status was improper because case did not meet circumstances required for retroactive revocation; IRS had revoked the group’s § 501(c)(4) status after determining the group had impermissibly benefitted private interests, specifically Democratic elected officials).

<sup>71</sup> 2002 EO CPE TEXT, *supra* footnote 13, at 434. Some might argue this rationale is suspect because § 501(c)(3) requires those organizations be organized and operated “exclusively” for an exempt purpose, but the IRS has interpreted the term to mean “primarily” in this context and permits them to engage in nonpartisan political activity. *See* Treas. Reg. § 1.501(c)(3)-1(c)(1).

<sup>72</sup> *See* Webster & Abegg, 613-3<sup>rd</sup> T.M., *Lobbying and Political Expenditures*, at A-89.

<sup>73</sup> *See* Rev. Rul. 68-266, 1968-1 C.B. 270.

<sup>74</sup> *See* Priv. Ltr. Rul. 8342100 (July 20, 1983); Priv. Ltr. Rul. 8852037 (October 4, 1988).

<sup>75</sup> *See* Regan v. Taxation with Representation of Washington, 461 U.S. 540, 546 (1983); Priv. Ltr. Rul. 7904064 (October 25, 1978).

## Tax Under IRC § 527(f)

Even though certain § 501(c) organizations may engage in political activity, they are subject to tax if they make an expenditure for a § 527 “exempt function.”<sup>76</sup> An “exempt function” is the “influencing or attempting to influence the selection, nomination, election, or appointment of any individual to any Federal, State, or local public office or office in a political organization, or the election of Presidential or Vice-Presidential electors....”<sup>77</sup>

The tax is imposed at the highest corporate rate on the lesser of the organization’s net investment income or the total amount of “exempt function” expenditures.<sup>78</sup> Thus, for organizations with little or no net investment income or those making low-cost expenditures, the tax is of minimal import. For others groups, however, it might serve as a disincentive to directly engage in the activities giving rise to the taxable expenditures.

Section 501(c) organizations may lawfully avoid the tax by setting up a separate segregated fund under § 527(f)(3) to conduct the taxable political activities. Assuming the fund is set up and administered properly, it will be treated as a separate § 527 political organization and the § 501(c) organization will not be subject to tax. However, a § 501(c) organization may not set up such a fund to accomplish activities the organization itself may not do.<sup>79</sup> Thus, for example, a § 501(c)(3) organization may not use such a fund as a way to get around the prohibition on campaign intervention.

## IRC Reporting and Disclosure Requirements

Under the IRC, § 501(c) organizations are generally required to file an annual information return (Form 990) with the IRS.<sup>80</sup> Filing organizations are required to report information regarding their political activities on the Form’s Schedule C.<sup>81</sup>

On the Schedule C, § 501(c)(3) organizations are required to describe their direct and indirect political campaign activities and report information on their political expenditures, volunteer hours, and any § 4955 excise taxes incurred. Section 501(c)(3) organizations must also report information about their lobbying activities on the Schedule. The specific information that must be reported differs depending on whether the organization made the § 501(h) election.

Meanwhile, organizations other than those described in § 501(c)(3) must: (1) describe their direct and indirect political campaign activities; (2) report the amount spent conducting campaign activities and the number of volunteer hours used to conduct those activities; (3) report the amount directly spent for § 527 exempt function activities; (4) report the amount of funds

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<sup>76</sup> I.R.C. § 527(f).

<sup>77</sup> I.R.C. § 527(e)(2).

<sup>78</sup> I.R.C. § 527(f).

<sup>79</sup> See Treas. Reg. § 1.527-6(g).

<sup>80</sup> See I.R.C. § 6033.

<sup>81</sup> The Schedule C is available at <http://www.irs.gov/pub/irs-pdf/f990sc.pdf>. The Schedule C is new, beginning with Tax Year 2008. It is part of the significant revisions to the Form 990 that the IRS made in order to encourage tax compliance, accountability, and transparency.

contributed to other organizations for § 527 exempt function activities; (5) report whether a Form 1120-POL (the tax return filed by organizations owing the § 527 tax) was filed for the year; and (6) report the name, address, and employer identification number of every § 527 political organization to which a payment was made and the amount of such payments, and indicate whether the amounts were paid from internal funds or were contributions received and directly transferred to a separate political organization. There is also space for § 501(c)(4), (c)(5), and (c)(6) organizations to report information regarding their lobbying activities with respect to the deductibility of dues paid by their members.

On the Form 990's Schedule B, § 501(c) organizations must report the names and addresses of significant donors, which are generally individuals who contributed at least \$5,000 during the year. These are all donors meeting this threshold, and not just those who contributed for political activities.

The organization and the IRS must make the organization's Form 990 and accompanying schedules publicly available.<sup>82</sup> However, identifying information about the donors reported on the Schedule B is not subject to public disclosure, except for donors to private foundations.<sup>83</sup>

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<sup>82</sup> See IRC § 6104(b) and (d). The organization is subject to a penalty of \$20 per day per return (limited to \$10,000) for failing to do so. See IRC § 6652(c)(1)(C).

<sup>83</sup> See IRC § 6104(b) and (d).

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