M. POLITICAL ORGANIZATIONS AND IRC 501(c)(4)

by
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1. Introduction

Otto Bismarck once said that politics is not an exact science; and indeed, the work of exempt organizations specialists reflects diverse ways in which political agendas are forwarded. Today, political agendas are being forged by political parties, candidates, legislative caucuses, educational organizations, and political action committees. When entities employed in this process seek recognition of exemption under IRC 501(c)(3) or 501(c)(4), questions arise about the scope of political campaign, legislative, and political educational activities permitted under these sections.

This article focuses on the extent to which political activities may be conducted by organizations exempt under IRC 501(c)(4). It will discuss the requirements for, and bars to, exemption under IRC 501(c)(4), and describe types of politically-oriented organizations that may seek exemption under that section. In addition, consequences under IRC 527 of political activities by IRC 501(c)(4) organizations will be discussed. Throughout this article, issues arising under IRC 501(c)(3) will be compared with those under IRC 501(c)(4). Political activities issues arising under IRC 501(c)(3) were discussed in the 1993 CPE article entitled "Election Year Issues."

2. Requirements for Exemption - In General

Social welfare organizations were first exempted from federal income tax by the Revenue Act of 1913. The legislative history does not explain the rationale of this exemption in any detail. In practice, IRC 501(c)(4) has sometimes been used by both the courts and the Service as a "catchall" exemption provision for organizations that lack the accepted essential characteristics of taxable entities, but elude classification under other subparagraphs of IRC 501(c). See discussion in G.C.M. 33495 (Apr. 27, 1967); see also 1981 CPE text, at pp. 95-127.

IRC 501(c)(4) provides for exemption from federal income tax of civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Reg. 1.501(c)(4)-1(a)(2)(i) provides that an 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, i.e., primarily for the purpose of bringing about civic betterment and social improvements. Whether an organization is "primarily" engaged in promoting social welfare is a "facts and circumstances" test.

As a result, one major distinction between IRC 501(c)(3) and IRC 501(c)(4) organizations is the amount of activity that may be devoted to nonexempt purposes. In contrast to the "primarily engaged" standard under Reg. 1.501(c)(4)-1(a)(2)(i), Reg. 1.501(c)(3)-1(c)(1) says an organization will not be regarded as "operated exclusively" for IRC 501(c)(3) exempt purposes "if more than an insubstantial part of its activities is not in furtherance of an exempt purpose." The difference between "primary" and "insubstantial" is significant.

Whether an organization is "primarily engaged" in promoting social welfare is a "facts and circumstances" determination. Relevant factors include the amount of funds received from and devoted to particular activities; other resources used in conducting such activities, such as buildings and equipment; the time devoted to activities (by volunteers as well as employees); the manner in which the organization's activities are conducted; and the purposes furthered by various activities. See, e.g., Rev. Rul. 74-361, 1974-2 C.B. 159 (volunteer fire company that provides recreational facilities for members is primarily engaged in promoting social welfare where providing facilities primarily furthers exempt purposes); Rev. Rul. 68-45, 1968-1 C.B. 259 (organization's principal source of income is not sole factor determining whether it is "primarily engaged" in promoting social welfare).

3. Basis for Exemption

A. Political Educational Organizations

IRC 501(c)(4) requires that organizations operate primarily in promoting in some way the common good and general welfare of the people of the community. To meet this requirement, many IRC 501(c)(4) organizations engage in educating the community.

Guidance regarding educational activities under IRC 501(c)(4) is derived from revenue rulings and court decisions regarding the educational activities of IRC 501(c)(3) organizations.[1] Generally, political educational organizations must

[1] At one time, educational and research activities conducted

conduct their activities in a non-partisan manner.

Reg. 1.501(c)(3)-1(d)(3) provides that the term "educational" relates to (a) the instruction or training of the individual for the purpose of improving or developing his capabilities; or (b) the instruction of the public on subjects useful to the individual and beneficial to the community. An organization may be educational even though it advocates a particular position or viewpoint if it presents a sufficiently full and fair exposition of the pertinent facts to permit an individual or the public to form an independent opinion or conclusion. An example of an educational organization is an organization whose activities consist of presenting public discussion groups, forums, panels, lectures, or other similar programs.

In Rev. Rul. 76-456, 1976-2 C.B. 151, the Service approved exemption under IRC 501(c)(3) for an organization formed to elevate the standards of ethics and morality in the conduct of political campaigns. The organization collected, collated, and disseminated, on a non-partisan basis, information concerning general campaign practices, through the press, radio, television, mail, and public speeches. It qualified as an educational organization under IRC 501(c)(3) because it instructed and encouraged the public about political campaigns, a subject useful to the individual and beneficial to the community. A key fact in the Service's decision was that the organization's activities were conducted on a non-partisan basis.

In contrast, in American Campaign Academy v. Commissioner, 92 T.C.

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to achieve specific goals were deemed to promote social welfare purposes under IRC 501(c)(4), but not to further "exclusively" educational purposes under IRC 501(c)(3). For example, in Rev. Rul. 60-193, 1960-1 C.B. 195, modified, Rev. Rul. 66-258, 1966-2 C.B. 213, modified and superseded, Rev. Rul. 76-456, 1976-2 C.B. 151, an organization conducted educational programs to encourage greater interest and participation in governmental and political affairs. The ruling concluded that while such activities promoted social welfare, they did not further "exclusively" educational purposes described in IRC 501(c)(3), but were merely ancillary to the organization's non-educational purposes.

Rev. Rul. 66-258, however, indicates the activities described in Rev. Rul. 60-193 were "educational" under IRC 501(c)(3), in addition to qualifying under IRC 501(c)(4). Accordingly, aside from "action organization" issues, little difference exists between the types of "educational" activities considered exempt under the two sections.

1053 (1989), a school that trained individuals as campaign managers was denied exemption under IRC 501(c)(3) because it operated for the substantial nonexempt purpose of benefiting the private interests of Republican Party entities and candidates. Although the school had a legitimate educational program, the Tax Court held that it conducted its educational activities with the partisan objective of benefiting Republican interests. The court noted that the school's partisan purpose distinguished its activities from the educational organization in Rev. Rul. 76-456, supra.

The following examples illustrate how the definition of "educational" applies in the context of "political" organizations claiming exemption under IRC 501(c)(4):

> **Example (1)** Organization A conducts research, seminars, forums, and other educational programs for the public on issues of public concern. It also engages in substantial lobbying activities. Its activities are under the direction of a Board of Directors consisting of prominent individuals with backgrounds in academics and/or government. While A's philosophy on the issues is generally consistent with that of a major political party, it conducts its activities in a non-partisan manner and is not affiliated in any way with the political party. B's activities are primarily "educational"; accordingly, it qualifies for exemption under IRC 501(c)(4).
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> **Example (2)** Organization B conducts research, seminars, forums, and other educational programs for the public on issues of public concern. It also engages in substantial lobbying activities. Its activities are under the direction of a Board of Directors whose members were appointed by the national committee of a major political party. It selects issues to study based on the needs of the party, and receives substantial financial support from the party. B's activities are not primarily "educational," given their partisan nature; accordingly, it does not qualify for exemption under IRC 501(c)(4).

B. "Action" Organizations

Reg. 1.501(c)(4)-1(a)(2)(ii) says that a social welfare organization may qualify for exemption under IRC 501(c)(4) even though it is an "action organization" described Reg. 1.501(c)(3)-1(c)(3)(ii) (substantial lobbying activities) or (iv) (main or primary objective can only be attained by legislation and advocacy to attain objective), if it otherwise qualifies for exemption.

Several published rulings have concluded that organizations primarily engaged in advocating a particular point of view on an issue of public concern, through lobbying and public education, qualified for exemption under IRC 501(c)(4). In Rev. Rul. 67-293, 1967-2 C.B. 185, the Service held that an organization that substantially engages in promoting legislation to protect or otherwise benefit animals is not exempt under IRC 501(c)(3), but may be exempt under IRC 501(c)(4). The organization was instrumental in having a bill introduced in the state legislature to provide for investigations and sanctions against mistreatment of laboratory animals. It wrote legislators to support the bill, and sent pamphlets and notices urging its members and other interested citizens to contact their representatives on behalf of the bill.

Similarly, Rev. Rul. 68-656, 1968-2 C.B. 216, concluded that an organization that informs the public on controversial subjects and attempts to influence legislation germane to its program may qualify for exemption under IRC 501(c)(4). The organization sought changes in the law and educated the public about a currently illegal activity, by circulating printed material and legislative proposals. Also, in Rev. Rul. 76-81, 1976-1 C.B. 156, the Service ruled that a nonprofit organization formed to educate the public on the subject of abortions, promote the rights of the unborn, and support legislative and constitutional changes to restrict access to abortion was exempt under IRC 501(c)(4). The primary activity of the organization was participation in forums, lectures, and other educational programs dealing with questions relating to legalized abortions and alternatives to abortions.

For additional examples of "advocacy" organizations exempt under IRC 501(c)(4), see Rev. Rul. 71-530, 1971-2 C.B. 237 (organization formed to represent the public interest at legislative and administrative hearings on tax matters); and Rev. Rul. 67-6, 1967-1 C.B. 135, modified, Rev. Rul. 76-147, 1976-C.B. 151 (organization that sought to preserve the traditions, architecture, and scenic appearance of a community, through individual and group action before local legislature and administrative agencies).

4. Possible Bars to Exemption

A. Political Campaign Activities

Reg. 1.501(c)(4)-1(a)(2)(ii) provides that the promotion of social welfare does not include direct or indirect participation in political campaigns on behalf of or in opposition to any candidate for public office. Thus, an organization exempt under IRC 501(c)(4) may engage in political campaign activities if those activities are not the organization's primary activity. In contrast, organizations exempt under IRC 501(c)(3) are absolutely prohibited from engaging in political activities (and may, in addition, be subject to tax under IRC 4955 if they make any "political expenditures").

In Rev. Rul. 67-368, 1967-2 C.B. 194, the Service held that an organization, formed for the purpose of promoting an enlightened electorate, whose primary activity was rating candidates for public office, was not exempt under IRC 501(c)(4) because such activity is not "the promotion of social welfare." The ruling stated that comparative rating of candidates, even though on a non-partisan basis, is participation or intervention on behalf of candidates favorably rated and in opposition to those less favorably rated.

In Rev. Rul. 81-95, 1981-1 C.B. 332, the Service considered the effect of engaging in political campaign activities on an IRC 501(c)(4) organization. The organization was primarily engaged in activities designed to promote social welfare. In addition, it conducted activities involving participation and intervention in political campaigns on behalf of or in opposition to candidates for nomination or election to public office. The ruling concluded that since the organization's primary activities promoted social welfare, its lawful participation or intervention in political campaigns on behalf of or in opposition to candidates for public office would not adversely affect its exempt status under IRC 501(c)(4). However, the organization was subject to the tax imposed by IRC 527 on expenditures for political activities as defined in IRC 527(e)(2), pursuant to IRC 527(f)(1). (See Part E., below.)

IRC 501(c)(4) does not define political campaign activities; instead, the definition and interpretation of terms used has occurred principally under IRC 501(c)(3). See generally 1993 CPE text, at pp. 400-444. Reg. 1.501(c)(3)-1(c)(3)(iii) provides that activities that constitute participation or intervention in a political campaign on behalf or in opposition to a candidate include, but are not limited to, publishing or distributing written or printed statements or making oral statements on behalf of or in opposition to such

candidate. In addition, the regulation says the term "candidate for public office" means an individual who offers himself, or is proposed by others, as a contestant for a national, State, or local elective public office.

As discussed in the 1993 CPE text, at p. 410, whether an organization has participated or intervened in a political campaign is a "facts and circumstances" test. Endorsing candidates clearly is political campaign intervention, as are such typical campaign activities as polling the public on behalf of a candidate. For other examples of participation or intervention in political campaigns, see Rev. Rul. 76-456, 1976-2 C.B. 151 (publicizing names of political candidates signing and refusing to sign code of fair campaign practices); Rev. Rul. 78-248, 1978-1 C.B. 154 (certain voter's guides); and Rev. Rul. 80-282, 1980-2 C.B. 178 (same); Association of the Bar of the City of New York v. Commissioner, 858 F.2d 876 (2d Cir. 1988), cert. denied, 490 U.S. 1030 (1989) (non-partisan candidate rating).

The following examples illustrate how political campaign intervention principles apply in the context of an organization claiming exemption under IRC 501(c)(4):

> **Example (3)** Organization D conducts activities designed to secure greater public involvement in the electoral process. Its activities include sponsoring candidate debates, open to all legally qualified candidates; disseminating written materials and advertising through the media about the importance of voting; conducting polls to determine what issues are of interest to the voting public and disseminating the results to candidates; and providing transportation for people who would otherwise be unable to vote. It also engages in substantial lobbying activities with regard to voting laws. Its activities are non-partisan. Organization D qualifies for exemption under IRC 501(c)(4).
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> **Example (4)** Organization E sponsors public appearances of candidates favoring its positions on issues; conducts non-scientific polls designed to create the appearance of public support for candidates who support its positions on issues; and provides transportation for people who have indicated their support for selected candidates, and who would

> otherwise be unable to vote. It also engages in substantial lobbying activities with regard to voting laws. Organization E is primarily engaged in political activities, and does not qualify for exemption under IRC 501(c)(4).

To summarize, an organization that cannot qualify under IRC 501(c)(3) because of its political activities may qualify for exemption under IRC 501(c)(4), if it is primarily engaged in activities promoting social welfare. However, as a result of IRC 504, organizations must carefully assess if they will engage in political activities when deciding to seek exemption under IRC 501(c)(3) or IRC 501(c)(4). In 1987, Congress amended IRC 504 to provide that an IRC 501(c)(3) organization that loses its exemption because it intervenes in political campaigns may not at any time thereafter be treated as an organization described in IRC 501(c)(4).

B. Community Benefit vs. Private Benefit

Reg. 1.501(c)(4)-1(a)(2) provides that to be operated exclusively for the promotion of social welfare, an organization must be operated primarily to benefit the community. The regulations do not define "community" nor do they specifically prohibit private benefit. Where benefits are limited, an organization must show that limiting its services to a particular group benefits the community as a whole. Many cases involve a weighing of private interest against community interests and deciding which is "primary."

Two rulings involving tenant rights organizations illustrate the IRC 501(c)(4) "private benefit" concept. Rev. Rul. 73-306, 1973-2 C.B. 179, denied exemption under IRC 501(c)(4) to an organization formed to represent member-tenants of an apartment complex in negotiations with landlords, in litigation, and in regulatory matters affecting tenants' interests. In contrast, Rev. Rul. 80-206, 1980-2 C.B. 185, held that an organization formed to promote the legal rights of all tenants in a community qualified for exemption under IRC 501(c)(4). It distinguished the earlier ruling:

> Rev. Rul. 73-306 is distinguishable because in that revenue ruling the organization's activities are directed primarily toward benefitting its member-tenants rather than, as in the instant case, all tenants in the community.
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> By promoting the legal rights of tenants in a particular community . . ., the

organization is promoting the common good and general welfare of the people of the community.

Rev. Rul. 80-107, 1980-1 C.B. 117, also denied exemption to an "advocacy" organization due to private benefit. The organization represented the interests of public utility shareholders in rate and regulatory matters before administrative agencies and legislative bodies. The ruling held that because the primary beneficiaries of the organization's activities were its members, "together with other individuals who own shares in the public utility companies," it was primarily operated to serve private interests rather than the community as a whole. Thus, it did not qualify for IRC 501(c)(4) exemption.

Other precedents have similarly distinguished between organizations primarily benefitting a limited class--usually of members--rather than a community. Rev. Rul. 79-316, 1979-2 C.B. 228, approved exemption under IRC 501(c)(4) for an organization whose purpose was to prevent liquid spills (primarily oil spills) in a city port area and to develop a program to contain and clean up spills that occurred. Although the organization was a membership organization, it participated in the cleanup of spills regardless of whether they were caused by members or nonmembers, with no difference in charges for members and nonmembers. Since all spills were cleaned up and uniform prices were charged, benefits to members were incidental to the organization's primary activity, which provided benefits to the community as a whole. In contrast, in Contracting Plumbers Cooperative Restoration Corp. v. United States, 488 F.2d 684 (2d Cir. 1973), cert. denied, 419 U.S. 827 (1974), an organization formed as a cooperative of plumbers repaired "cuts" members made in city streets. While the court found the program to be highly beneficial, it concluded the organization principally served the private economic interests of its members and thus, was not exempt under IRC 501(c)(4).

No published precedent discusses the community vs. private benefit dichotomy in the context of educational or "advocacy" organizations benefitting a political party or candidate. By analogy, however, the American Campaign Academy case, supra, might support a conclusion that an organization whose educational or advocacy activities primarily benefit a particular political party or candidate does not qualify for exemption under IRC 501(c)(4). The National Office is currently studying the applicability of the IRC 501(c)(4) private benefit doctrine in this context.

5. IRC 527

The tax treatment of "political organizations" under IRC 527 is addressed in depth in the 1993 CPE text, at pp. 444-488. In general, "political organizations," as defined in IRC 527(e)(1), are subject to tax on their "political organization taxable income" under IRC 527(b). To equalize the treatment of IRC 501(c) organizations that engage in political activities, exempt organizations are taxed on the lesser of their expenditures for political activities or their net investment income, under IRC 527(f)(1). Where an exempt organization conducts political activities through a "separate segregated fund," the fund is subject to tax as a political organization, pursuant to IRC 527(f)(2).

Organizations that do not qualify for exemption under IRC 501(c)(4) because they primarily engage in political activities may qualify as "political organizations" as defined in IRC 527(e)(1). IRC 527(e)(1) defines a "political organization" as--

> a party, committee, association, fund, or other organization (whether or not incorporated) organized and operated primarily for the purpose of directly or indirectly accepting contributions or making expenditures, or both, for an exempt function.

Whether an organization that does not qualify under IRC 501(c)(4) because its activities primarily benefit a political party or candidate(s) qualifies as a "political organization" under IRC 527 is problematic. The "exempt function" of political organizations is defined in IRC 527(e)(2) as--

> the function of 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, whether or not such individual or electors are selected, nominated, elected, or appointed.

Regulations under IRC 527 divide exempt function activities (expenditures) into "directly related expenses" (Reg. 1.527-2(c)(1)) and "indirect expenses" (Reg. 1.527-2(c)(2)). Generally, directly related expenses include anything that supports an individual's campaign, while indirect expenses are for activities necessary to support the directly related activities. Expenditures for "educational" or "advocacy" activities may or may not be for an "exempt function." Where such activities are conducted by a political organization (e.g., a political party), Reg.

1.527-2(c)(5), Example (8), supports finding an "exempt function":

> Q is a political organization described in section 527(e)(2). Q finances seminars and conferences which are intended to influence persons who attend to support individuals to public office whose political philosophy is in harmony with the political philosophy of Q. The expenditures for these activities are for an exempt function.

Where, however, similar activities are conducted by organizations lacking a close connection to political organizations or individuals who are seeking public office, the result under IRC 527 is less clear.

Are there organizations that provide so much private benefit to political organizations or individuals that they do not qualify for exemption under IRC 501(c)(4), yet are so remote from the political "selection process" that they do not qualify under IRC 527? The answer to this question is unclear.

As the National Office studies this question, a major concern relates to the interrelationship between tax and election law. As discussed in the 1993 CPE text, requirements under the Federal Election Campaign Act and the Internal Revenue Code with respect to political organizations and activities are not entirely symmetrical. Nevertheless, Service conclusions regarding status under IRC 501(c) may affect organizations' election law obligations. For example, corporations are generally prohibited from contributing to political parties or candidates; the amount of non-corporate contributions to any political party or candidate is limited, and must be disclosed. In contrast, no law prohibits contributions to IRC 501(c) organizations, which need not disclose their donors' identities. While Service recognition of exempt status does not preclude the Federal Election Commission (or a state election commission) from finding violations of laws within its jurisdiction, it may complicate these agencies' determinations.

On the other hand, where tax and election law diverge, a non-profit organization may qualify under neither IRC 501(c) nor IRC 527. While this result may be technically correct, it seems somewhat anomalous for these organizations to be considered taxable entities.