DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

200151060

Date: SEP 27 2001

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UIL Nos.
501.03-17
501.38-00
527.04-00
4955.04-00

LEGEND:

X =
Y =
Z =

Dear Sir or Madam:

We have considered X's ruling request dated December 20, 2000 for rulings pertaining to the consequences under sections 501(c)(3), 527, and 4955 of the Internal Revenue Code of a charitable organization's administration of a payroll deduction plan under a collective bargaining agreement to collect and remit its employees' voluntary contributions earmarked for political action committees set up by the employees' unions.

FACTS:

X is a health plan. X, X's principal subsidiary health plans, and a related hospital (collectively, "Health Plan") are described in section 501(c)(3) of the Code and are part of the integrated health care delivery system known as Z.

Certain labor unions (the "Unions") have been recognized as the representatives of Health Plan's employees for collective bargaining purposes to settle employment issues common to Health Plan's multitude of unionized health care workers represented by the Unions and covered under many separate collective bargaining agreements. Under the National Labor Relations Act, Health Plan is legally obligated to bargain in good faith with the Unions regarding "mandatory subjects of bargaining," which are subjects that relate to wages, hours, and other terms and conditions of employment. An employer's failure to bargain on such subjects in good faith would constitute an unfair labor practice. See NLRA §§ 8(a)(5) and 8(d); NLRB v. Borg-Warner Corp., 356 U.S. 342 (1958). X represents that the National Labor Relations Board (the federal agency entrusted with administering and interpreting the NLRA) has construed "mandatory subjects of bargaining" to include the establishment of a payroll deduction plan to

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permit employees within the collective bargaining unit to instruct the employer to deduct from their wages and pay over to a union political action committee such amounts as are specified by the individual employees on a wholly voluntary basis, citing Electrical Associates, Inc. and IBEW, Local 212, 318 NLRB No. 33 (1995).

Recently, Health Plan concluded its collective bargaining negotiations with the Unions. During the negotiations, the Unions repeatedly requested Health Plan to establish a voluntary payroll deduction plan that would allow individual employees to direct a portion of their wages to the political action committees ("PACs") for their respective unions. The PACs are separate segregated funds under section 527(f)(3) of the Code. Mindful of its obligation to refrain from engaging in political activities, Health Plan repeatedly declined such requests. However, the implementation of a PAC payroll deduction plan was an essential part of the benefits package sought by the Unions, and the Unions continued to request Health Plan to establish such a plan. By the conclusion of the negotiations, Health Plan tentatively agreed to establish a voluntary payroll deduction plan to collect PAC contributions provided that it first obtained a favorable ruling from the IRS.

Under the collective bargaining agreements, Health Plan would act under the direction of the unions for specific, limited purposes in connection with the PAC payroll deduction plan. The collective bargaining agreements would establish Health Plan's role in providing ministerial administrative functions in collecting payroll-based, voluntary contributions from employees earmarked for the PACs sponsored by the Unions. Health Plan would transfer all union dues and PAC contributions collected from Health Plan employees to the Unions. See 11 CFR § 102.6(c)(3). The Unions would, in turn, transfer the PAC contributions to the respective PACs. The Unions would reimburse Health Plan for the costs it would incur in connection with establishing and operating the PAC payroll deduction plan. Health Plan would have absolutely no role in the management and governance of the PACs or any influence over the selection of candidates or political parties to be supported by the PACs. In addition, Health Plan would not be named or otherwise acknowledged in connection with any contributions made by the PACs to any candidates for public office.

Health Plan's duties with regard to its employees involve the provision of many employee benefits (such as pension and savings plans, insurance, and other programs which provide needed services to the employees) that employees may participate in on a completely voluntary basis and that involve the deduction of amounts of money from the employees' compensation. Thus, Health Plan already has an administrative staff and procedures in place to handle various payroll deductions plans. Health Plan would handle the PAC payroll deduction plan in a similar manner. No employee would be required to contribute, but each employee would have the independent opportunity to decide whether to participate.

With the exception of administering the PAC payroll deduction plan, Health Plan would not authorize or permit its employees to engage in PAC-related activities during work hours. Any personal activities of Health Plan's employees in connection with their PACs would be on a strictly voluntary basis and would depend on the willingness of each individual employee to make time available to the organization outside of his or her regularly scheduled hours of employment. Employees participating in any Union-sponsored PAC activities would not make

representations to third parties or candidates that they represent Health Plan. If Health Plan became aware of any such representations, it would take measures to stop and disavow any such activity.

RULINGS REQUESTED:

X requests the following rulings:

1. The administration by Health Plan of a payroll deduction plan to collect political contributions from its employees and remit such contributions to the Unions for transfer to Union-sponsored PACs would not violate the prohibition against intervening in or participating in a political campaign and would not jeopardize its tax-exempt status under section 501(c)(3) of the Code.

2. The personal activities of Health Plan's employees with respect to their Union-sponsored PACs would not be attributable to Health Plan and would not jeopardize its tax-exempt status under section 501(c)(3) of the Code.

3. The periodic transfer of its employees' political contributions by Health Plan to the Unions for transfer to Union-sponsored PACs and the reimbursed, associated costs would not constitute expenditures for an exempt function and would not subject Health Plan to tax under section 527 of the Code.

4. The administration of the payroll deduction plan on these facts would not constitute participation or intervention in a political campaign, and neither Health Plan nor its managers would be liable for any excise tax on political expenditures under section 4955 of the Code.

LAW:

Section 501(c)(3) of the Code exempts from federal income tax organizations organized and operated exclusively for charitable purposes, provided that the organization does not participate in, or intervene in, any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 527(f)(1) of the Code provides that, if an organization described in section 501(c) expends any amount during the taxable year directly (or through another organization) for an exempt function under section 527(e)(2), then, notwithstanding any other provision of law, there shall be included in the gross income of such organization for the taxable year, and subject to tax, an amount equal to the lesser of the net investment income of such organization for the taxable year or the aggregate amount so expended during the taxable year for such an exempt function.

Section 527(e)(2) of the Code defines "exempt function" 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

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selected, nominated, elected, or appointed. Such term includes the making of expenditures relating to an office described in the preceding sentence which, if incurred by the individual, would be allowable as a deduction under section 162(a).

Section 4955(a)(1) of the Code imposes on each political expenditure by a section 501(c)(3) organization a tax equal to 10% of the amount thereof. This tax shall be paid by the organization.

Section 4955(a)(2) of the Code imposes on the agreement of any organization manager to the making of any expenditure, knowing that it is a political expenditure, a tax equal to 2.5% of the amount thereof, unless such agreement is not willful and is due to reasonable cause. This tax shall be paid by any organization manager who agreed to the making of the expenditure.

Section 4955(d)(1) of the Code provides that the term "political expenditure" means any amount paid or incurred by a section 501(c)(3) organization in any participation in, or intervention in (including the publication or distribution of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 4955(f)(1) of the Code provides that, for purposes of section 4955, the term "section 501(c)(3) organization" means any organization which (without regard to any political expenditure) would be described in section 501(c)(3) and exempt from taxation under section 501(a).

Section 1.501(c)(3)-1(c)(3)(i) of the Income Tax Regulations provides that an organization is not operated exclusively for one or more exempt purposes if it is an "action organization."

Section 1.501(c)(3)-1(c)(3)(iii) of the regulations provides that an organization is an "action organization" if it participates or intervenes, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office. The term "candidate for public office" means 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. Activities which constitute participation or intervention in a political campaign on behalf of or in opposition to a candidate include, but are not limited to, 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.

Section 1.527-2(c)(1) of the regulations provides that an "exempt function," as defined in Section 527(e)(2) of the Code, includes all activities that are directly related to and support the process of influencing or attempting to influence the selection, nomination, election, or appointment of any individual to public office or office in a political organization (the "selection process"). Whether an expenditure is for an exempt function depends upon all the facts and circumstances. Generally, where an organization supports an individual's campaign for public office, the organization's activities and expenditures in furtherance of the individual's election or appointment to that office are for an exempt function of the organization.

Section 1.527-2(c)(2) of the regulations provides that expenditures that are not directly related to influencing or attempting to influence the selection process ("indirect expenses") may also be an expenditure for an exempt function by a political organization. These indirect expenses are expenses which are necessary to support the directly related activities of the political organization. Activities which support the directly related activities are those which must be engaged in to allow the political organization to carry out the activity of influencing or attempting to influence the selection process. Expenses incurred in soliciting contributions to the political organization are necessary to support the activities of the political organization.

Section 1.527-6(b)(1)(i) of the regulations provides that expenditures which are directly related to the selection process as defined in section 1.527-2(c)(1) are expenditures for an exempt function. Expenditures made by a section 501(c) organization for indirect expenses (as defined in section 1.527-2(c)(2)) are for an exempt function only to the extent provided in Section 1.527-6(b)(2). Expenditures of a section 501(c) organization that are otherwise allowable under the Federal Election Campaign Act or similar State statute are for an exempt function only to the extent provided in section 1.527-6(b)(3).

Section 1.527-6(b)(1)(ii) of the regulations provides that an expenditure may be made for an exempt function directly or through another organization.

Section 1.527-6(b)(2) of the regulations is reserved.

Section 1.527-6(b)(3) of the regulations is reserved.

Section 1.527-6(e) of the regulations provides that a transfer of political contributions or dues collected by a section 501(c) organization to a separate segregated fund is not treated as an expenditure for an exempt function if the transfer is made promptly after receipt of such amounts by the section 501(c) organization and made directly to the separate segregated fund. A transfer is considered promptly and directly made if:

(1) the procedures followed by the section 501(c) organization satisfy the requirements of applicable Federal or State campaign law and regulations;

(2) the section 501(c) organization maintains adequate records to demonstrate that amounts transferred in fact consist of political contributions or dues, rather than investment income; and

(3) the political contributions or dues transferred were not used to earn investment income for the section 501(c) organization.

Section 1.527-6(g) of the regulations provides that section 527(f) and this section do not sanction the intervention in any political campaign by an organization described in section 501(c) of the Code if such activity is inconsistent with its exempt status under section 501(c). For example, an organization described in section 501(c)(3) is precluded from engaging in any political campaign activities. The fact that section 527 imposes a tax on the exempt function (as defined in section 1.527-2(c) of the regulations) expenditures of section 501(c) organizations

and permits such organizations to establish separate segregated funds to engage in campaign activities does not sanction the participation in these activities by section 501(c)(3) organizations.

Section 53.4955-1(a) of the Foundations and Similar Excise Taxes Regulations provides that the excise taxes imposed by section 4955 of the Code do not affect the substantive standards for tax exemption under section 501(c)(3), under which an organization is described in section 501(c)(3) only if it does not participate or intervene in any political campaign on behalf of any candidate for public office.

Section 53.4955-1(c)(1) of the regulations provides that any expenditure that would cause an organization that makes the expenditure to be classified as an action organization by reason of section 1.501(c)(3)-1(c)(3)(iii) is a political expenditure within the meaning of section 4955(d)(1) of the Code.

Rev. Rul. 78-248, 1978-1 C.B. 154, held that certain "voter education" activities conducted in a non-partisan manner by a 501(c)(3) organization may not constitute prohibited political intervention. The Service stated that whether an organization is participating or intervening, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office depends upon all of the facts and circumstances of each case.

In Rev. Rul. 72-512, 1972-2 C.B. 246, the Service ruled that a university did not intervene in a political campaign under section 501(c)(3) of the Code by conducting a political science course that required the students' participation in political campaigns of their choice. As part of the course, each student participated in several weeks of classroom work to learn about political campaign methods and then was excused from classes for two weeks to participate in the political campaign of a candidate of the student's choice. The university did not influence the student in his or her choice of a candidate or control the student's campaign work. The university was reimbursed or paid for any facilities provided to the student for use in connection with the campaigns. The Service reasoned that under the circumstances, the university was not a party to the expression or dissemination of political views of the individual students in the course of their actual campaign activities.

In Rev. Rul. 72-513, 1972-2 C.B. 246, the Service ruled that a university did not intervene in a political campaign under section 501(c)(3) of the Code by providing faculty advisors and facilities for a campus newspaper that published the students' editorial opinions on political matters. Neither the university administration nor the advisors exercised any control or direction over the newspaper's editorial policy. A statement on the editorial pages made it clear that the views expressed were those of the student editors and not of the university. The Service reasoned that under the circumstances, the university's provision of assistance to the student newspaper did not make the expression of political views by the students in the publishing of the newspaper the acts of the university.

In Commissioner v. Bollinger, 485 U.S. 340 (1988), the Supreme Court held that an agency relationship was established between a corporation and its shareholders. The court reasoned that the genuineness of an agency relationship is adequately assured, and tax-

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avoiding manipulation adequately avoided, when (a) the fact that the corporation is acting as agent for its shareholders with respect to a particular asset is set forth in a written agreement, (b) the corporation functions as agent and not principal with respect to the asset for all purposes, and (c) the corporation is held out as the agent and not principal in all dealings with third parties relating to the asset.

RATIONALE:

Each of the requested rulings is discussed in turn below.

1. Health Plan, as a 501(c)(3) organization, is prohibited from participating or intervening in, directly or indirectly, any political campaign on behalf of or in opposition to any candidate for public office. Whether an organization has participated or intervened in a political campaign is based on all the facts and circumstances. A 501(c)(3) organization's provision of indirect assistance to a PAC would in many circumstances constitute prohibited political intervention. Under the circumstances described, however, Health Plan's administration of the proposed payroll deduction plan to benefit the Union-sponsored PACs will not constitute political intervention.

It is helpful to consider what is not the case here. Health Plan will not render any material financial assistance to the PACs. All funds flowing to the PACs will be earnings of the Health Plan employees, who will contribute the funds voluntarily. The employees will act in their individual capacity in making the contribution. Also, the PACs will fully reimburse Health Plan for expenses incurred in administering the program.

This is not a case of a 501(c)(3) organization establishing a PAC, which is prohibited under section 501(c)(3) of the Code. Health Plan did not select the beneficiary PACs and has no control or influence over them. The PACs are sponsored by the Unions, and on labor issues would likely have political interests differing from those of Health Plan. Thus, there is no identity of interests between Health Plan and the PACs.

Nor did Health Plan seek to establish the payroll deduction plan. Instead, the facts show that the plan is a benefit sought by the Unions. Health Plan is legally required to bargain in good faith regarding the establishment of such plan. While Health Plan understandably approached the matter with caution for fear of noncompliance with the federal tax laws, we find that it has developed a reasonable approach to accommodating the interests of its employees that complies with the requirements of section 501(c)(3) of the Code. We note that Health Plan has a legitimate interest in providing benefits to its employees in order to attract and retain a qualified workforce.

The situation is like those set forth in Rev. Ruls. 72-512 and 72-513, in which a university was held not to be intervening in political campaigns by virtue of conducting educational courses or assisting educational student programs which involved political activity by individuals not representing the university. Here, Health Plan is conducting an employee benefit program that involves political activity by the employees, not attributable to the employer.

2. General agency law governs whether the personal activities of Health Plan's

employees would be attributed to Health Plan. Only acts undertaken by Health Plan's employees within the scope of their employment or acts ratified by Health Plan would be considered activities of Health Plan. The facts presented indicate that all activities of Health Plan's employees with respect to their Union-sponsored PACS (other than the payroll deduction plan discussed above) will be undertaken in a personal capacity and thus not attributable to Health Plan. Whether all such activities are actually undertaken in a personal capacity is an inherently factual matter dependent upon future events, on which the Service cannot rule.

3. Section 527(f) of the Code imposes a tax on section 501(c)(3) organizations that expend any amount during the taxable year, directly or indirectly, for an exempt function. An exempt function includes, but is not limited to, the function of influencing or attempting to influence the selection, nomination, election, or appointment of any individual to federal, State, or local office.

The use of a corporation's payroll deduction system is one of the available methods for soliciting contributions to a political organization. Under the regulations, expenditures for soliciting contributions to a political organization are considered to be indirect expenditures. Indirect expenditures made by a 501(c) organization are considered to be for an exempt function (within the meaning of section 527(e)(2) of the Code) only to the extent provided in the regulations, which are reserved with respect to such treatment. Health Plan would be fully reimbursed for all costs associated with the administration of the PAC payroll deduction system. Therefore, these expenses would not constitute expenditures for an exempt function within the meaning of section 527(e)(2).

Similarly, the periodic transfer of political contributions by Health Plan to the Unions for transfer to the Union-sponsored PACs would not constitute an expenditure for an exempt function within the meaning of Section 527 of the Code. Health Plan would transfer such contributions promptly after receipt and directly to the Unions for transfer to the Union-sponsored PACs in accordance with the requirements of the applicable federal or State campaign finance law and regulations. Health Plan would maintain adequate records to demonstrate that amounts transferred to the Unions for transfer to the Union-sponsored PACs consist exclusively of political contributions from the employees and not amounts derived from Health Plan's investment income. In addition, Health Plan would not use its employees' political contributions to earn investment income. Accordingly, the periodic transfer of its employees' political contributions by Health Plan to the Unions for transfer to the respective Union-sponsored PACs would not constitute an expenditure for an exempt function within the meaning of Section 527.

4. Section 4955 of the Code imposes a tax on any amounts paid or incurred by a section 501(c)(3) organization in any participation or intervention in any political campaign on behalf of (or in opposition to) any candidate. As discussed above, Health Plan's administration of the payroll deduction plan would not constitute the participation or intervention in any political campaign on behalf of (or in opposition to) any candidate for public office.

RULINGS:

Accordingly, we rule as follows:

1. The administration by Health Plan of a payroll deduction plan to collect political contributions from its employees and remit such contributions to the Unions for transfer to Union-sponsored PACs would not violate the prohibition against intervening in or participating in a political campaign and would not jeopardize its tax-exempt status under section 501(c)(3) of the Code.

2. The personal activities of Health Plan's employees with respect to their Union-sponsored PACs would not be attributable to Health Plan and would not jeopardize its tax-exempt status under section 501(c)(3) of the Code, if all such activities are undertaken in a personal capacity rather than as agents of Health Plan.

3. The periodic transfer of its employees' political contributions by Health Plan to the Unions for transfer to Union-sponsored PACs and the reimbursed, associated costs would not constitute expenditures for an exempt function and would not subject Health Plan to tax under section 527 of the Code.

4. The administration of the payroll deduction plan on these facts would not constitute participation or intervention in a political campaign, and neither Health Plan nor its managers would be liable for any excise tax on political expenditures under section 4955 of the Code.

Except as we have ruled above, we express no opinion as to the tax consequences of the transaction under the cited provisions of the Code or under any other provisions of the Code.

This ruling is directed only to X. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Because this letter could help resolve any future questions about the tax consequences of your activities, you should keep a copy of this ruling in your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours,

Terrell M. Berkovsky
Manager, Exempt Organizations
Technical Group 2

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