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The IRS Publishes Proposed Regulations On Political Activities of 501(c)(4) Organizations

The day after Thanksgiving, the Internal Revenue Service published proposed regulations that, if adopted, will dramatically affect the extent to which non-profit organizations can participate in political activities and the manner in which the IRS regulates those organizations. Although the regulations are targeted at social welfare organizations that qualify for tax-exempt status under Internal Revenue Code (IRC) § 501(c)(4), the comments the IRS published with these regulations suggest that the scope of the IRS's regulatory initiative will ultimately cover many non-profit organizations. Because the IRS may ultimately sweep charities (exempt under IRC § 501(c)(3)), unions and agricultural associations (exempt under IRC § 501(c)(5)), and tax-exempt trade associations (exempt under IRC § 501(c)(6)) into this regulatory undertaking, virtually all non-profit organizations should become familiar with how these new proposed regulations could ultimately affect them.

Although the proposed regulations will not take effect until at least 2015, non-profit organizations should be reviewing them now. Any non-profits that determine that they could be significantly affected should consider retaining experienced legal counsel to prepare comments on the proposed regulations, which are due as early as January 28, 2014.

Introduction

For decades, most non-profit organizations have been limited in the degree to which they can participate in elections for candidates for public office. Charities are prohibited from "intervening" in elections for public office. Other organizations – including social welfare organizations, agricultural organizations, unions, and tax-exempt trade associations – are allowed "intervene" in political campaigns (i.e., participate in elections for public office) so long as they are not "primarily" engaged in election campaigning. But when these activities influence or attempt to influence an election for public office, the expenditures for those activities are subject to federal tax.

These restrictions apply only to campaigns to elect individuals to public office. They do not apply to lobbying. In additional to supporting or opposing proposed legislation, lobbying also includes (a) supporting or opposing referenda and (b) supporting or opposing confirmation of political and judicial appointees.

The lines between political campaigning, lobbying, and other types of tax-exempt activities are sometimes uncertain, and the IRS decides on a case by case basis (under the "facts and circumstances" test) whether or not a particular activity qualifies as political campaigning. Over the years, many non-profit organizations and legal professionals have criticized the IRS's approach as being too vague and too difficult to properly enforce. The critics grew louder in recent years as more and more groups took advantage of the recent Supreme Court decision in Citizens United to form (c)(4) organizations that engage aggressively in political campaigning. These groups sometimes prefer establishing a (c)(4) organization instead of a PAC because PACs are required by federal and state campaign laws to disclose their donors while (c)(4) organizations are not. The IRS's new proposed regulations are a response to this recent trend.

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Summary of the Proposed Regulations

The proposed regulations take four steps that significantly expand the IRS's regulatory authority over the campaign political activities of IRC § 501(c)(4) organizations.

1. Replaces the "Campaign Intervention Standard" with a more clearly defined "Candidate-Related Political Activity." By adopting this new term, the IRS is abandoning its case-by-case "facts and circumstances" test in favor of a more bright-line approach. Under the new regulations, "candidate-related political activity" would include:

- Expressly advocating the election or defeat of a particular candidate. The IRS dervied its definition of "express advocacy" from the expanded definition developed by the courts and the Federal Election Commission in the wake of the McCain-Feingold law.
- A "public communication" that clearly identifies a candidate within 30 days of a primary or 60 days of a general election. "Public communication" is broadly defined and includes, among other things, statements the (c)(4) posts on its website long before the election but leaves on the site as the election approaches.
- Any communication if the expenditure paying for the communication must be reported to the Federal Elections Commission.
- Any gift or expenditure that must be reported as a campaign contribution under federal, state, or local law.
- Any contribution (including in-kind donations) to a 501(c) organization that engages in candidate-related political activity.
- Distributing campaign materials prepared by or on behalf of candidates.
- Voter registration and get-out-the-vote drives.
- Voter guides, even if they are non-partisan.
- Hosting any event within 30 days of a primary or 60 days of a general election at which one or more candidates appear. This rule applies even if it is a non-partisan event, such as a candidate debate.

The last three are particularly surprising because IRS has always treated non-partisan voter registration, voter guides, and candidate nights as non-political activities that even charities could engage in if they were fair and balanced.

2. With respect to "public communcations", intent does not matter. Even if the (c)(4) organization did not intend a "public communication" to influence an election, it still constitutes a "candidate-related political activity" that is taxable and counts as a non-exempt activity. Any (c)(4) that, for example, seeks to correct a misstatement of fact in a candidate debate shortly before a primary or general election would have to weigh the impact of this regulatory change before making a public statement.

3. Imports standards from IRC § 527 governing political organizations to cover political and judicial appointments. Current regulations concerning political campaigning apply only to elections and to party conventions. They do not apply to organizations taking positions on political or judicial nominees. This would change under the proposed regulations.

4. Potential regulations significantly limiting how much of candidate-related political activities a (c)(4) organization could do. The current regulations allow a (c)(4) organization to intervene in elections so long as the organization "primarily" engages in its exempt activities. The legal profession has commonly advised (c)(4) clients to spend less than 50% of their revenues on political campaigning. But the draft regulations call this advice into question, as the IRS requested comments on whether it should evaluate something other than an organization's expenditures

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(such as the number of volunteer hours spent on a project), to determine whether the organization engages “primarily” in exempt activities or in non-exempt political campaigning. The IRS also made it clear that it might change the percentage of activities required so that 50% would no longer be feasible as a rule of thumb.

How Might the Proposed Regulations Affect Other Types of Nonprofit Organizations?

Although the proposed regulations only target (c)(4) organizations, they could have significant implications for charities and other nonprofit organizations as well. Here is what we see in store for those organizations.

1. Charities. Charities could be directly affected in at least two ways. First, many of the concepts and terms that apply to the regulation of political activities of (c)(4) organizations apply to charities as well. For example, many charities have routinely engaged in non-partisan voter registration and education efforts. It is difficult to imagine the IRS telling (c)(4) organizations that these activities are political, but not applying the same standard to charities. If the IRS does apply the same standards to charities, continuing these activities would jeopardize the charities’ tax-exempt status.

Second, the IRS has requested comments about whether to apply some or all of its proposed regulations to charities. Charities, therefore, should review these regulations and carefully consider whether to comment on how the regulations would affect their activities if they were applied to charities.

2. Unions, Agricultural Organizations, and Tax-Exempt Trade Associations. The IRS asked for comments about whether it should broaden the proposed regulations to cover (c)(5) organizations (unions and agricultural organizations) and (c)(6) organizations (tax-exempt trade associations). These organizations should also study the proposed regulations and carefully consider whether to comment on them.

What is Next?

The IRS has given organizations until January 28, 2014 to comment on one portion of the proposed regulations, and until February 27, 2014 to comment on all other aspects of the proposed regulations. The IRS will also likely hold public hearings on its proposed regulations.

If the IRS decides to apply some or all of these regulations to charities, agricultural organizations, unions, or tax-exempt trade associations, there will likely be another round of proposed regulations and comments. The same holds true if the IRS decides to draft additional regulations defining the word “primarily.”

Given how aggressively the proposed regulations expand the scope of the IRS’s regulatory authority and the controversy surrounding its past handling of regulation of politically active (c)(4) organizations, we anticipate a robust and boisterous debate over these proposed regulations. The final regulations could also be challenged in court, which could delay implementation. But even before these regulations take final form or are implemented, they have already cast the IRS’s regulatory intentions in a much different light and changed the regulatory landscape facing nonprofit organizations.

Butzel Long, with its DC and Lansing offices, is uniquely positioned to help you navigate these and other federal and state regulatory issues. Look for more information to come from us on this and other lobbying and election issues. Please feel free to contact us with any questions.

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