NONPROFITS: POLITICAL ISSUES

The Political Ban in 501(c)(3): Its Odd History

06.23.16 | Linda J. Rosenthal, JD

We in the philanthropic community are – along with the rest of the nation – deep in the muck of perhaps the most bizarre election season in recent memory.

There's an added dimension to our bewilderment; namely, how to skirt the quicksand of the absolute ban in Section 501(c)(3) on political activities; that is: [not] "participat[ing] in, or interven[ing] in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office." (*emph. added*)

It's the tail-end of a remarkably brief (132-word) statute that defines which organizations are entitled to the most coveted tax-exempt status. But there are huge consequences for running afoul of this crisp, explicit prohibition. Surely, then, our lawmakers of long ago thought long and hard about it. Undoubtedly, it was a well-considered trade-off for the many generous benefits of the prized 501(c)(3) status. Right?

Well, … not exactly.

It's a sketchy tale. Among the highlights of this legislative saga is the image of Lyndon B. Johnson, then Minority Leader of the U.S. Senate, sitting in a back room at the Capitol in 1954, mulling an amendment to the proposed overhaul of the federal tax code. There was speculation he may have been plotting a way to get back at a political enemy.

But the story actually begins many decades earlier – in 1894.

The Early Years: No Political Ban

Charities have been given tax breaks since the Tariff Act of 1894. Back then, most revenue of the federal government had come from tariffs.

Earlier, legislators had enacted a federal tax on income, but (also in 1894) it was declared unconstitutional. It wasn't until almost two decades later that the federal income tax was successfully and permanently launched in the landmark Revenue Act of 1913.

First Hints on Restricting Political Activities

"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 IRS § 501(c)(3)." As a result, contributions to these organizations were not deductible from the new federal income tax.

There were legal challenges, of course, but "no clear standard emerged from the court decisions." Some courts denied the tax deduction if the organization "advocated for any type of change." Others considered "how controversial the advocacy was or if the organization's actions were intended to influence legislation." *Slee v. Commissioner* (1930) emerged as a leading case on this issue. There, the Second Circuit Court of Appeals crafted a different theory. It ruled 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 purposes."

Lobbying Restrictions Codified in 1934

Set against these earlier conflicting and confusing developments, Congress took action in the Revenue Act of 1934.

It's been suggested that Congress may have been "concerned with organizations that lobby also being able to receive tax-deductible contributions," but there is "very little legislative history."

There are, though, records of the discussions on the Senate floor about the proposed law. One member spoke "about the deductibility of donations that were made for 'selfish' reasons." He called out one particular organization with which he was "apparently having problems." He believed that the statute under consideration was "too broad in that it applied to organizations without 'selfish motives.'"

Another Senator "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."

There has been some speculation that Congress intended to codify the *Slee* ruling. The problem with that premise is that "the focus of the test under *Slee* is whether the lobbying furthers the organization's exempt purpose, whereas the focus of the lobbying provision [in the 1934 Revenue Act] is whether the lobbying is a substantial part of the organization's activities."

As enacted, the 1934 lobbying provision includes the concept that is familiar to us from the current Section 501(c)(3); no "substantial part" of the activities of an exempt organization can be the "carrying on of propaganda" or "attempting to influence legislation."

It's significant that the Revenue Act of 1934, as originally proposed, had included an explicit "provision that would have restricted the ability of charities to participate in partisan politics." But there were concerns that it was "too broad," so that language was stricken in conference. It would take another two decades before there was action on a statutory politics ban.

The Electioneering Ban in 1954

This brings us back to that (presumably smoke-filled) room with Lyndon Johnson. He was the hard-hitting, aggressive leader of the Senate Democrats then in the minority. (That would change the following year when his party took control; he continued as Majority Leader until January 1961 when he was inaugurated as vice-president.

The comprehensive restructuring of the federal tax laws in the Internal Revenue Code was a crowning achievement for Congress in 1954. The statutory provisons on tax exemption were collected and codified in the new section 501(c) which defines all of the different categories of tax exemption available. New subsection (3) of section 501(c) defines which organizations qualify for the most favorable type of tax exemption. The language of section 501(c)(3) enacted in 1954 is almost identical to current version of 501(c)(3).

It begins with the definition of which organizations qualify for the most favorable tax-exemption category: "Corporations, and any community chest, fund, or foundation, 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, …."

It continues in the same uninterrupted paragraph by listing the primary way an applicant can doom its eligibility: "…no part of the net earnings of which inures to the benefit of any private shareholder or individual, …."

Next up is the language that explains the lobbying restrictions: "… no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation,…."

The final fragment of this brief statute is the politics ban: "… and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office."

The only two items left out of the 1954 version are: (1) a short phrase mentioning a lobbying "election" added in 1976; and (2) the words "or in opposition to" enacted for clarification in 1987 of the politics ban.

That politics ban language was added as a floor amendment by Minority Leader Johnson.

"What is a 'floor amendment,'" you ask? According to current Senate procedures – "… Senators may … propose floor amendments that are not germane to the subject or purpose of the bill being debated. This permits individual Senators to raise issues and potentially have the Senate vote on them, even if they have not been studied and evaluated by the relevant standing committees…."

When Senator Johnson introduced this floor amendment, he analogized it to the lobbying limitation. Of course, it's important to note that he had mixed up and mischaracterized these clauses by telling his Senate colleagues that organizations that lobbied were *denied* tax-exempt status. That, of course, is inaccurate: only organizations that engage in "substantial" lobbying are denied tax exemption. The legislative history includes no further details, including whether anyone noticed the Minority Leader's error.

So, to recap: (1) the total ban on political campaigning for 501(c)(3) charities was offered as a last-minute, "non-germane" amendment to the massive new Internal Revenue Code; and (2) Senator Johnson's rationale was based on a significantly incorrect characterization of extent and consequences of the 1934 Act's lobbying-restriction language. Commentators explaining these 1954 deliberations note that Johnson, who only began to serve in the House of Representatives in 1937, would not be expected to know what happened in the 1934 session. Nevertheless, they point out, the lobbying language plucked from the 1934 Act were plopped right down without change in the 1954 bill, so the language was right there on the page in front of him – in the sentence just before the phrase he added as a floor amendment.

Senator Johnson's motives and reasoning for his floor amendment are not clear from the legislative history. But, reportedly, he may have proposed it in part to get back at a local organization that had supported a political opponent.

Post-1954 Changes: Political-Ban Language

The Revenue Act of 1987 "clarified that political campaign activities may not be conducted 'in opposition to' a candidate" as well as "on behalf of" any candidate for public office.

Also added that year was Internal Revenue Code section 4955, with new penalties for violating the campaigning ban. In addition to the remedy available to the IRS to revoke the organization's tax exemption, the agency may impose – either in addition to, or as an alternative – an excise tax and a termination assessment for all taxes owed. The agency may also seek an injunction against any further prohibited expenditures.

Conclusion

There it is.

We thought you'd like to know how we got to this point.

— Linda J. Rosenthal, J.D., FPLG Information & Research Director

[Note 1/21/24]*: The legislative history links to the Joint Committee on Taxation appear not to be working at this time. We'll try to find those missing URLs.*