O. ELECTION YEAR ISSUES

by
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1. Introduction

As another election year draws near, questions concerning the political activities of exempt organizations and the tax treatment of political organizations arise. This article updates the article on election year issues in the FY 1993 CPE text.

2. IRC 4955 Proposed Regulations

On December 14, 1994, the Service issued proposed regulations for IRC 4955, IRC 6852, and IRC 7409. These proposed regulations provide a structure for the implementation of these provisions.

A. Statutory Background

(1) IRC 501(c)(3) Political Campaign Prohibition

An organization described in IRC 501(c)(3) is prohibited from participating in, or intervening in (including the publishing or distributing of statements), an election campaign in support of (or opposition to) any candidate for public office. This is an absolute prohibition. However, prior to 1987, the only remedy for a violation of this prohibition was revocation of the organization's exempt status. There was some concern that this was ineffective as a remedy. For example, where the expenditure was small, the violation was unintentional, and the organization subsequently adopted procedures to assure that similar expenditures would not be made in the future, it was believed that the draconian measure of revocation was disproportionate to the violation. In other instances, the remedy of revocation might be ineffective because the IRC 501(c)(3) organization ceased operations after it diverted all of its assets to improper purposes.

(2) IRC 4955 Excise Tax on Political Expenditures

As a result of these concerns, Congress enacted IRC 4955 as part of the Omnibus Budget Reconciliation Act of 1987 (OBRA), Public Law 100-203. IRC 4955 imposes taxes on the political expenditures of IRC 501(c)(3)

organizations. IRC 4955(a)(1) provides for an initial tax of 10% of each political expenditure. IRC 4955(b)(1) imposes an additional tax on the organization of 100% of each political expenditure previously taxed and not corrected within the taxable period. In addition, IRC 4955(a)(2) imposes a tax of 2<$E1/2>% of the political expenditure on organization managers who agreed to the making of the political expenditure. Organization managers who refused to agree to all or part of the correction are subject to a tax of 50% of the political expenditure. The tax/correction structure and the rates imposed by IRC 4955 are identical to those under IRC 4945, which imposes a tax on the taxable expenditures of a private foundation, including political expenditures. To avoid duplicating excise taxes on political expenditures by private foundations, IRC 4955(e) provides that if its taxes are imposed on a private foundation, the expenditure is not treated as a taxable expenditure under IRC 4945.

The tax is imposed on the "political expenditures" of the organization. Political expenditures are defined in IRC 4955(d)(1) as "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," tracking the language of the prohibition in IRC 501(c)(3). In addition, Congress was concerned that some candidates were using IRC 501(c)(3) organizations to promote their candidacy and therefore provided that, for purposes of IRC 4955, political expenditures of IRC 501(c)(3) organizations included certain expenses of candidate-controlled organizations. IRC 4955(d)(2).

IRC 4955 applies to IRC 501(c)(3) organizations whether or not their tax-exempt status is revoked. Congress specifically noted that the enactment of IRC 4955 did not change the prohibition on political campaign activities of IRC 501(c)(3) organizations. It looked upon the provision fundamentally as an additional deterrent.

(3) Willful and Flagrant Violations

Congress also determined that existing audit and enforcement procedures were not sufficient to deter an IRC 501(c)(3) organization that was willfully and flagrantly violating the political campaign prohibition. Therefore, it also enacted IRC 6852 and IRC 7409 as part of OBRA.

IRC 6852 provides that the Service may immediately determine the amount of income and IRC 4955 tax, for that year and the immediately preceding tax year,

due from an IRC 501(c)(3) organization that flagrantly violates the political campaign prohibition, which shall be immediately due and payable. The Service will immediately assess the tax so determined and demand payment from the organization. The determination and assessment of the tax under IRC 6852 terminates the taxable year of the IRC 501(c)(3) organization.

IRC 7409 grants the Service authority to seek an injunction against an IRC 501(c)(3) organization that flagrantly violates the political campaign prohibition, to prevent further political expenditures by the organization. An injunction may be sought only if the organization has been notified that the Service intends to seek an injunction if the making of political expenditures does not immediately cease and the Commissioner has personally determined that the organization has flagrantly violated the political campaign activity prohibition and injunctive relief is appropriate to prevent future political expenditures.

B. Proposed Regulations

(1) Coordination with IRC 501(c)(3)

The proposed regulations specifically do not affect the standards for exemption under IRC 501(c)(3). See Prop. Reg. 53.4955-1(a). IRC 501(c)(3) organizations continue to be subject to the absolute prohibition on political campaign activity. Thus, an organization that is subject to the IRC 4955 excise tax may also have its exempt status revoked. The presence or absence of revocation proceedings against the organization does not affect the application of the IRC 4955 excise tax.

(2) Imposition of Tax on Organization Managers

As the structure of IRC 4955 was based upon the structure of IRC 4945, the proposed regulations would adopt the same basic standards as those contained in Reg. 53.4945-1(a)(2) for the imposition of tax under IRC 4955(a)(2) on organization managers that agree to the making of the political expenditure. Prop. Reg. 53.4955-1(b)(1) provides that the excise tax under IRC 4955(a)(2) will only be imposed on a manager if three conditions are met:

(1) A tax is imposed on the organization by IRC 4955(a)(1);

(2) The organization manager knows that the expenditure to which the manager agrees is a political expenditure; and

(3) The agreement is willful and is not due to reasonable cause.

IRC 4955(f)(2) specifies that the term "organization manager" on whom tax may be imposed means any officer, director, or trustee of the organization (or individual having similar powers or responsibilities), or any employee of the organization having power or authority with respect the expenditure. To be subject to the tax under IRC 4955(a)(2), the manager must either be authorized to approve, or to exercise discretion in recommending approval of, the making of the expenditure, or be a member of a group (such as the organization's governing body) which is so authorized. Prop. Reg. 53.4955-1(b)(2)(i). An officer of the organization is the person designated as such under the organizing documents of the organization or any person who regularly exercises general authority to make administrative or policy decisions on its behalf. An independent contractor, acting as an attorney, accountant, or other advisor, is not an officer of the organization. Prop. Reg. 53.4955-1(b)(2)(ii). An individual is only considered an employee of the organization for purposes of IRC 4955(f)(2)(B) if that individual is an employee within the meaning of IRC 3121(d)(2). Prop. Reg. 53.4955-1(b)(2)(iii).

In determining whether the organization manager knows that an expenditure is a political expenditure, the proposed regulations follow Reg. 53.4945-1(a)(2)(iii) in establishing the general rule. Prop. Reg. 53.4955-1(b)(4)(i) provides that an organization manager is considered to have known that the expenditure to which he or she agreed is a political expenditure only if the following conditions are met:

(1) The manager has actual knowledge of sufficient facts so that, based solely upon these facts, the expenditure would be a political expenditure;

(2) The manager is aware that such an expenditure under these circumstances may violate the provisions of federal tax law governing political expenditures; and

(3) The manager negligently fails to make reasonable attempts to ascertain whether the expenditure is a political expenditure, or the manager is aware that it is a political expenditure.

The proposed regulations also amplify this general rule by providing that for purposes of IRC 4955, knowing that an expenditure is a political expenditure does not mean the organization manager has reason to know that it is a political expenditure. Nevertheless, evidence showing that the manager had reason to know is relevant in determining whether the manager had actual knowledge. Prop. Reg. 53.4955-1(b)(4)(ii).

(3) Political Expenditures

Just as the statutory definition of political expenditures in general follows the language of the political campaign prohibition in IRC 501(c)(3), the proposed regulations refer to the regulations under IRC 501(c)(3). Specifically, Prop. Reg. 53.4955-1(c)(1) provides that a political expenditure for purposes of IRC 4955 is any expenditure that would cause the organization making the expenditure to be considered an "action" organization under Reg. 1.501(c)(3)-1(c)(3)(iii). In addition to repeating the statutory prohibition against political campaign activity, Reg. 1.501(c)(3)-1(c)(3)(iii) provides that both direct and indirect participation or intervention in the political campaign process will cause the organization to be considered an action organization.

With regard to other types of political expenditures, the proposed regulations would adopt a definition of "candidate-controlled organization" that is consistent with the legislative history. See H.R. 100-495, 100th Cong., 1st Sess. 1623-27 (1987). A candidate-controlled organization exists where a candidate or prospective candidate has a "continuing, substantial involvement in the day-to-day operations or management of the organization." Prop. Reg. 53-4955-1(c)(2)(i). The mere fact that an organization is affiliated with a candidate or the candidate knows the directors, officers, or employees of the organization is not sufficient to classify the organization as a candidate-controlled organization. Similarly, the organization is not a candidate-controlled organization simply because it conducts research, study, or other educational activities regarding issues of concern to the candidate.

In determining that the primary purpose of an organization is promoting the candidacy of an individual for public office, all facts and circumstances must be considered. Relevant facts and circumstances include whether the organization is making its research materials available only to a particular candidate and whether the organization is paying only for the speeches and travel of that particular candidate. If the organization makes its research material available to others besides the candidate, that the candidate uses that material is not a relevant factor

in whether the organization has the primary purpose of promoting that individual's candidacy. Prop. Reg. 53.4955-1(c)(2)(ii). The proposed regulations also provide that expenditures for voter registration, voter turnout, or voter education activities will not be treated as other political expenditures by reason of IRC 4955(d)(2)(E) unless the expenditures violate the IRC 501(c)(3) prohibition on political activity. Prop. Reg. 53.4955-1(c)(2)(iii). Thus, expenditures that conform to the standards set forth in revenue rulings concerning voter education activities will not result in the application of the excise tax under IRC 4955. See, e.g., Rev. Rul. 74-574, 1974-2 C.B. 160; Rev. Rul. 78-248, 1978-1 C.B. 154; Rev. Rul. 80-282, 1980-2 C.B. 178; and Rev. Rul. 86-95, 1986-2 C.B. 73.

(4) Termination Assessments

The proposed regulations set forth procedures for making a termination assessment under IRC 6852 when the IRC 501(c)(3) organization willfully and flagrantly violates the political campaign prohibition. The termination assessment must be authorized by the District Director. Prop. Reg. 301.6852-1(a). The termination assessment may only be made if the flagrant violation results in revocation of the organization's IRC 501(c)(3) status. The IRC 501(c)(3) organization will not be liable for income taxes for periods prior to the effective date of the revocation. Prop. Reg. 301.6852-1(b). Any tax due becomes immediately due and payable when the District Director makes a determination that income tax or IRC 4955 excise tax is due in accordance with IRC 6852. After the notice and demand for immediate payment is sent to the organization, it is required to pay the amount of the assessment within 10 days, regardless of the filing of an administrative appeal or of a court petition. Unless the organization posts a bond in accordance with IRC 6863, enforced collection action may proceed after the 10-day payment period. Normal collection procedures are not suspended since an assessment under IRC 6852 does not constitute a situation in which collection of the tax is in jeopardy. Prop. Reg. 301.6852-1(c).

(5) Injunctions

The proposed regulations also set forth procedures to be followed in seeking an injunction under IRC 7409 when the IRC 501(c)(3) organization is flagrantly violating the political campaign prohibition. First, the Assistant Commissioner (Employee Plans and Exempt Organizations) must conclude that the IRC 501(c)(3) organization has engaged in flagrant political intervention and is likely to continue to engage in political intervention that involves political expenditures. The Assistant Commissioner (Employee Plans and Exempt Organizations) must then

send a letter to the IRC 501(c)(3) organization describing the facts on which the conclusion was made. The IRC 501(c)(3) organization then has ten calendar days to respond by either agreeing to cease the political intervention or refuting the Service's evidence that it has engaged in flagrant political intervention. The Service will not seek an injunction under IRC 7409 during the ten days. Prop. Reg. 301.7409-1(a).

If the IRC 501(c)(3) organization has not responded within the 10 day period or has not provided sufficient information to convince the Assistant Commissioner (Employee Plans and Exempt Organizations) that an injunction is not needed, then the file will be forwarded to the Commissioner. The Commissioner must personally determine whether to forward a recommendation to the Department of Justice that an injunction under IRC 7409 be sought. This authority may not be delegated. The Commissioner may also request the court action include any other action that is appropriate to ensure the preservation of the IRC 501(c)(3) organization's assets. Prop. Reg. 301.7409-1(b).

C. Status of Proposed Regulations

The comment period for the proposed regulations closed March 14, 1995. The FY 1995 Business Plan includes publication of final regulations under IRC 4955 as one of the guidance priorities. See Treasury/IRS 1995 Business Plan, reprinted in Exempt Organizations Tax Review, April 1995, vol. 11, no. 4, p. 704. The Service hopes to finalize the proposed regulations in the near future.

3. Political Activities of IRC 501(c)(3) Organizations

As discussed above, an IRC 501(c)(3) organization is absolutely prohibited from engaging in political campaign activities. On December 20, 1994, in a stipulated decision, the Tax Court upheld the Service's revocation of the Coalition for Freedom, Inc.'s exempt status as an organization described in IRC 501(c)(3). Coalition for Freedom, Inc. v. Commissioner, Docket No. 5406-93X. The Service had revoked the organization's exempt status in part because it had engaged in political campaign activities.

In an unpublished technical advice memorandum that was attached to the Coalition for Freedom's Tax Court petition, the Service concluded that revocation of the organization's exemption was appropriate for three reasons. First, the organization had a substantial non-exempt purpose because it was serving a private rather than a public interest. Second, the organization's net earnings were

inuring to private shareholders or individuals. Finally, the organization intervened in political campaigns. Coalition for Freedom, Inc. Petition for Declaratory Judgment, reprinted in Exempt Organizations Tax Review, June 1993, vol. 7, no. 6, p. 1005.

Coalition for Freedom, Inc. (CFF) was part of a network of organizations controlled by the same individuals. The network of organizations generally performed activities supportive of political positions and political candidates for public office. In addition to CFF, the individuals controlled two other organizations that had been recognized as exempt as organizations described in IRC 501(c)(4) and an unincorporated political action committee, National Congressional Club (NCC). They also controlled Education Support Foundation, Inc. (ESF), which had an application pending for recognition of its status as an organization described in IRC 501(c)(4). ESF owned all of the stock of Jefferson Marketing, Inc. (JMI), a for-profit corporation, whose main activity involved campaign related political consulting and other activities supportive of political campaigns. JMI had seven wholly-owned for-profit subsidiaries that supported its activities.

The technical advice memorandum analyzed the activities of CFF and the other organizations in the network during the years at issue. It determined that CFF engaged in a number of fundraising activities seeking tax-deductible contributions for a variety of projects, most of which never materialized. Instead, most of the money raised was used to pay fees and expenses to JMI, its taxable subsidiaries, and to individuals employed by those entities.

In a suit filed by the Federal Election Commission alleging that ESF and NCC were in fact one organization, the FEC argued that two of the three members of CFF's Board controlled both ESF and NCC (as well as JMI due to ESF's ownership of JMI) and that JMI was providing services to NCC and other political clients for less than fair market value. The funds provided by CFF enabled JMI and its subsidiaries to engage in activities for its political clients at less than fair market value. In addition, the funds enabled JMI and its subsidiaries to provide services to political clients who were known to be unable or unexpected to pay their full bills timely, particularly Funderburk for Senate (FFS), the political campaign committee of former Ambassador (now Representative) David Funderburk.

CFF paid consulting fees to individuals who were heavily involved in the FFS campaign along with other political campaign activities of JMI and NCC. The

individuals paid appeared to be spending all their time on non-CFF political activities during periods when they were being paid consulting fees by CFF. CFF also hired Mr. Funderburk after his unsuccessful campaign. He was paid a monthly consulting fee, although the only work done on the project for which he was hired was done by JMI (for which JMI was also paid).

CFF engaged in a joint fundraising event with NCC and sponsored an event featuring three Presidential candidates whose views coincided with those of CFF. There was no indication that CFF took any steps to ensure that it conducted these events in a neutral manner with respect to the campaign.

The technical advice memorandum stated that the benefits flowing from CFF to JMI, its subsidiaries, and the individuals showed that CFF was operated for the substantial non-exempt purpose of serving those private interests rather than operating for the benefit of the public. In addition, the flow of funds to the benefit of the insiders of CFF constituted inurement. Finally, the technical advice memorandum noted that the interrelated structure of the organizations and the flow of benefits from CFF to support the political activities of JMI and its subsidiaries created a situation where CFF was engaging in prohibited political campaign activity.

4. Miscellaneous IRC 527 Issues

Several recent private letter rulings and technical advice memoranda have addressed the application of IRC 527.

A. Exempt Function Expenditures

IRC 527 provides that a political organization is not taxed on specified types of income to the extent they are segregated for use only for the exempt function of the political organization. Several recent technical advice memoranda have dealt with what types of expenditures will be considered to be for the exempt function of the political organization.

The exempt function of a political organization 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." Reg. 1.527-2(c)(1) refers

to this process as the "selection process." For taxable years beginning after December 31, 1986, the exempt function of a political organization also includes making expenditures relating to a public office which would be allowable as a deduction under IRC 162(a) if incurred by the office holder. IRC 527(e)(2).

(1) TAM 95-16-006

In TAM 95-16-006 (Jan. 10, 1995), the Service determined that the payment of a salary to a candidate for the candidate's services to the campaign committee was an exempt function expenditure. Rev. Rul. 87-119, 1987-2 C.B. 151, holds that payments to campaign workers for services rendered in support of the selection process are exempt function expenditures, so long as the amount paid is reasonable for services performed; it did not directly address the situation where the campaign worker was the candidate, however. In TAM 95-16-006, the candidate worked over 80 hours per week for the campaign, performing services substantially similar to services he had performed in his pre-campaign employment. The candidate was paid a reasonable salary for those services, amounting to 37 percent of the amount he earned from his regular employment and 60 percent of the amount he would earn if elected to public office. The campaign committee appropriately reported the salary paid to the candidate as wages on Form W-2 and the candidate reported the payments as income on his individual tax return. The services performed by the candidate supported the campaign selection process, so the payment of the salary was an exempt function expenditure.

Not all payments to or on behalf of a candidate will qualify as exempt function expenditures, however. In the situation described in TAM 95-16-006, the campaign committee had a clear employer-employee relationship with the candidate and consistently treated the payments as such. A different situation is presented when a campaign committee makes payments for the personal benefit of a candidate that are not paid as compensation and not treated as compensation by the organization. In that case, the amounts paid are not exempt function expenditures, although they are considered income to the candidate in accordance with Reg. 1.527-5(a)(1).

(2) TAM 94-09-003

The question of what constitutes an exempt function expenditure also arose in TAM 94-09-003 (Feb. 26, 1993). This case concerned a committee established by an individual after he had been elected to public office. The committee was

intended to make contributions to and otherwise support various candidates for public office. In addition, the committee made contributions to various tax-exempt organizations, including public charities and civic, fraternal, and labor organizations. IRC 527(d)(2) provides that amounts contributed to or for the use of an organization exempt from tax under IRC 501(a) and described in IRC 509(a)(1) or 509(a)(2) will not be considered diverted for the personal benefit of any individual. Thus, this provision applies to contributions to certain IRC 501(c)(3) organizations that are not private foundations. It does not apply to other types of exempt organizations, such as civic, fraternal, and labor organizations. Thus, payments to such organizations are not exempt function expenditures solely on the basis of the tax-exempt status of the organization.

The committee also made payments relating to office expenses of the individual who established the committee. The committee paid for maps for the individual's office. It also paid for some of the individual's employees to attend a national convention relating to their job and for a Christmas party for the individual's employees. These payments would all have been allowable as a deduction under IRC 162(a) if the office holder had incurred the expense. Consequently, under IRC 527(e)(2), the payments were exempt function expenditures.

The committee also made a number of payments for social and entertainment activities. The TAM notes that if the payments for entertainment of the individual's employees while they are attending the national convention can be characterized as compensation of those employees, then the payments would be deductible under IRC 162(a) and would be exempt function expenditures under IRC 527(e)(2). Payments for social activities and for entertainment of people other than the individual's employees at the national convention were not exempt function expenditures.

Finally, the committee made payments for unsubstantiated purposes. A political organization must keep books and records to show that its expenditures further its exempt function. Reg. 1.527-2(b)(2). Since the committee was unable to substantiate that these payments were for an exempt function, the payments were not exempt function expenditures.

(3) TAM 93-20-002

Like TAM 94-09-003, TAM 93-20-002 (Jan. 14, 1993) analyzes a variety of expenditures to determine if they qualify as exempt function expenditures. The

committee in this case was the principal campaign committee of a former member of the U.S. House of Representatives. The campaign committee was maintained for a possible campaign for the U.S. Senate by the former Representative, although the individual did not run for election during this period and ultimately did not run for a Senate seat. The committee continued to make payments for membership dues at a dinner club in order to use it for political purposes. Although the club was not used for political purposes during the years at issue, it was likewise not used for other purposes. Shortly after the decision was made not to run for the U.S. Senate, membership in the club was terminated. Thus, it appeared that the dues were paid solely to enable the former Representative to use the club for political campaign purposes, and they qualified as exempt function expenditures. Similarly, the committee continued to pay the annual fees on charge cards to use them for political campaign expenditures. However, these cards were not used solely by the committee for political purposes and the annual fees were not pro-rated. Consequently, these payments were not exempt function expenditures.

Although the former Representative was not actively campaigning during the years at issue, his wife was active in election campaign activity during those years and the committee paid a number of expenses related to her political campaign activity. The committee also made payments to support other candidates for public office. Although the payments did not support the individual in his own campaign for public office, they did support the selection process as defined in Reg. 1.527-2(c)(1). Thus, payments made to other candidates and to support the political activities of the former Representative's wife were exempt function expenditures.

In addition to those expenditures, the committee made expenditures for the former Representative and his wife to attend various local and national political campaign conventions. Since their attendance at these conventions supported the selection process, the expenditures were exempt function expenditures. However, the committee also made expenditures for the couple to attend Inaugural events. Attendance at Inaugural events is not related to nor does it support the selection process. Expenditures for election night parties and celebrations qualify as exempt function expenditures because they are the traditional culmination of the selection process. See Rev. Rul. 87-119, 1987-2 C.B. 151. In contrast, an inauguration and its associated events are the traditional commencement of a term of public office. Therefore, the amounts paid for the Inaugural events were not exempt function expenditures.

Finally, like the organization described in TAM 94-09-003, the committee

paid some expenses of a social event. Although the social event was attended by members of Congress and other politically active people, the mere presence of such people does not convert a social activity into a political campaign event. Therefore, those expenses were not exempt function expenditures.

B. "To or for the Use of" - IRC 527(d)(2)

As discussed above, IRC 527(d)(2) provides that amounts contributed "to or for the use of" an organization exempt from tax under IRC 501(a) and described in IRC 509(a)(1) or 509(a)(2) will not be considered diverted for the personal benefit of any individual. See also Reg. 1.527-5(b)(2). IRC 509(a) provides that an organization described in IRC 501(c)(3) is a private foundation unless it meets one of four tests, including those set forth in IRC 509(a)(1) and 509(a)(2).

In PLR 94-25-032, a private foundation requested a ruling that contributions to it from campaign committees would be considered "for the use of" organizations meeting the requirements of IRC 527(d)(2). As a private foundation, it did not meet these requirements itself. However, it had been formed to make contributions to colleges or universities to fund scholarships for students who need or deserve monetary assistance to further their education and to make contributions to other organizations recognized as public charities under IRC 501(c)(3) and IRC 509(a)(1). Similarly, upon dissolution, its assets would be distributed to an organization described in IRC 501(c)(3) and IRC 509(a)(1). Under the law of the state in which the private foundation was incorporated, it was considered a charitable trust and the Attorney General, as well as any other person with a sufficient special interest under a liberal standing rule, may bring an action to enforce proper administration of the charitable trust.

Under IRC 170(c), a deduction is allowed for contributions "to or for the use of" certain enumerated organizations, including charitable organizations. In that context, the Supreme Court has stated that "a gift or contribution is 'for the use of' a qualified organization when it is held in a legally enforceable trust for the qualified organization or in a similar legal arrangement." Davis v. United States, 495 U.S. 472, 485 (1990). The Court stated further:

> A defining characteristic of a trust arrangement is that the beneficiary has the legal power to enforce the trustee's duty to comply with the terms of the trust. See, e.g., 3 W. Fratcher, Scott on Trusts 200 (4th ed. 1988); 1 Restatement of Trusts 200 (1935). A qualified beneficiary of a bona fide trust for charitable purposes would have

> both the incentive and legal authority to ensure that donated funds are properly used. If the trust contributes funds to a range of charitable organizations so that no single beneficiary could enforce its terms, the trustee's duty can be enforced by the Attorney General under the laws of most States. See 4A W. Fratcher, Scott on Trusts. 391 (4th ed. 1989); G. Bogert, Trusts and Trustees. 411 (2d ed. 1977).

Id. at 483.

Applying these principles to the identical language in IRC 527(d)(2), PLR 94-25-032 held that a contribution by a political organization will be considered "for the use of" an organization meeting the requirements of IRC 527(d)(2) if it is held in a legally enforceable trust or similar legal arrangement. In this situation, although the organization may contribute its funds to a number of organizations, it is legally required to distribute them only to organizations described in IRC 501(c)(3) and IRC 509(a)(1); that requirement may be enforced by the Attorney General of the state in which the private foundation was incorporated. Accordingly, contributions to that private foundation will be considered "for the use of" organizations described in IRC 527(d)(2).

Although contributions to that private foundation would qualify under IRC 527(d)(2), contributions to many private foundations would not. In PLR 94-25-032, the organization's activities were strictly limited to making contributions to organizations that qualified under IRC 527(d)(2). In many cases, private foundations are not so limited. They frequently carry on their own charitable programs or they may be formed to contribute to IRC 501(c)(3) organizations, without regard to the their private foundation status. In addition, whether particular provisions in a foundation's governing instrument create an enforceable charitable trust or similar arrangement is a question of state law; provisions such as those present in PLR 94-25-032 might not create an enforceable trust arrangement under the laws of a different state. In those cases, contributions to the private foundation would not qualify as "for the use of" organizations meeting the requirements of IRC 527(d)(2).

Under the principles discussed in this ruling, a contribution by a political organization to an IRC 509(a)(3) organization may sometimes be considered "for the use of" an organization meeting the requirements of IRC 527(d)(2). An IRC 509(a)(3) organization is required to operate for the exclusive benefit of one or more specified IRC 509(a)(1) or IRC 509(a)(2) organizations and must be operated, supervised, or controlled by or in connection with one or more of those

organizations. If, under state law, it is considered a charitable trust or similar arrangement, the amounts contributed to the IRC 509(a)(3) organization would qualify under IRC 527(d)(2).

C. Tax Treatment of Organization

(1) Status as Political Organization

Generally, expenditures to support or oppose a referendum or initiative measure are not for an exempt function activity, as this activity does not further the purpose of influencing or attempting to influence the selection process. Instead, such expenditures typically constitute lobbying. The legislative history of IRC 527 treats ballot measure expenditures as outside the purview of exempt function activity. See S. Rep. No. 93-1357, 93d Cong., 2d Sess. 27 (1974), 1975-1 C.B. 517, 532 (stating, in discussing the primary activities test, that "a qualified organization could support the enactment or defeat of a ballot proposition, as well as support or oppose a candidate, if the latter activity was its primary activity").

In a particular case, however, ballot measure expenditures may be an exempt function activity, if their primary purpose is to influence or attempt to influence the selection process. For example, a legislative candidate's campaign committee may make expenditures to oppose a ballot initiative that would re-apportion legislative districts in a manner detrimental to the candidate's re-election effort. Since the expenditures are made for the primary purpose of influencing or attempting to influence the individual's election to public office, they are for an exempt function activity.

In TAM 92-44-003 (Apr. 15, 1992), an organization was established to promote the passage of a municipal tax by referendum. The organization did not engage in any activities to attempt to influence the selection process. It was simply engaging in lobbying activities to encourage voters to approve the municipal tax rate. As a result, it did not qualify as a political organization under IRC 527.

(2) Status as Principal Campaign Committee

Under IRC 527(h), a political organization that qualifies as the principal campaign committee of a candidate for the United States Congress is entitled to more beneficial tax rates. Generally, under IRC 527(b), political organizations pay tax on their taxable income at the highest corporate rate specified in IRC 11(b). However, IRC 527(h) provides a special rule under which principal campaign

committees of candidates for Congress pay tax on their taxable income at the graduated corporate rates specified in IRC 11(b).

To qualify for the beneficial tax treatment under IRC 527(h), the political organization must be designated as the principal campaign committee of a candidate for Congress in accordance with section 302(e) of the Federal Election Campaign Act of 1971 (2 U.S.C. 432(e)). To qualify as a principal campaign committee, the committee must not support more than one candidate. 11 C.F.R. 102.12(c)(1). However, the term "support" does not include contributions by the principal campaign committee in amounts aggregating $1,000 or less per election to the authorized committee of any other candidate. Thus, a political organization may qualify as the principal campaign committee of a candidate for Congress even though it contributes amounts to other candidates, provided those payments do not exceed $1,000 per candidate, per election. See TAM 92-24-002 (Feb. 19, 1992) and TAM 93-20-002 (Jan. 14, 1993).

In TAM 93-20-002, the committee was the principal campaign committee of a former member of the House of Representatives and had been designated as such for several years. In the second year of his last term of office, the individual announced that he would not be seeking reelection. The individual did not actively campaign for public office during the three years from the time his final term in office ended to the time when the political organization was terminated. However, the individual indicated he was considering running for a seat in the Senate. When the incumbent in that seat announced that he would seek reelection rather than run for a different office as had been speculated, the individual terminated the campaign committee.

Before the individual announced that he would not seek reelection for his seat in the House, the campaign committee clearly qualified for the beneficial tax treatment under IRC 527(h). When the individual left office, the principal campaign committee would normally terminate its status within a reasonable period of time. In this instance, however, the individual held the excess campaign funds in reasonable anticipation of running for another seat in the Congress. Accordingly, the campaign committee retained its status as a principal campaign committee under IRC 527(h).

D. Transfers to Political Organizations

The regulations under IRC 527 provide that exempt function expenditures include expenses that are not directly related to influencing the selection process if

they are necessary to support the directly related activities of the political organization. Reg. 1.527-2(c)(2). These expenses would include overhead, record keeping expenses, solicitation expenses and other administrative expenses. However, an indirect expense will only be considered an exempt function expense to the extent provided in Reg. 1.527-6(b)(2) for IRC 501(c) organizations. Reg. 1.527-6(b)(1)(i). Reg. 1.527-6(b)(2) has been reserved and the Supplementary Information to the final regulations, T.D. 7744, 1981-1 C.B. 360, explains that when this section is adopted as a final regulation, it will be applied on a prospective basis. Therefore, until that section is promulgated, an IRC 501(c) organization that pays the administrative expenses of an affiliated political organization will not be making an exempt function expenditure under IRC 527.

Exempt function expenditures may be made indirectly, as well as directly. Thus, an IRC 501(c) organization could make an exempt function expenditure if it transfers funds to another organization that makes exempt function expenditures. Although an IRC 501(c) organization is not strictly liable under IRC 527(f)(1) for amounts transferred to another organization, it must take reasonable steps to ensure that the amounts transferred are not used for an exempt function.

In TAM 94-33-001 (Jan. 26, 1994), the Service held that an IRC 501(c)(6) organization was liable for tax under IRC 527(f) as a result of payments made to an affiliated political organization. The IRC 501(c)(6) organization had attempted to take advantage of the fact that it could pay the indirect expenses of the political organization without incurring tax under IRC 527(f). However, the organization did not pay the administrative expenses of the political organization. Instead, it budgeted an amount of $1 per member, which it contributed to the political organization. Although it intended the contribution be used to pay administrative expenses, it had no agreement as to the use of the funds and it took no steps to ensure that the funds were not used for an exempt function. The political organization deposited the contribution in its general account, from which both direct and indirect expenditures were made.

TAM 94-33-001 held that the IRC 501(c)(6) organization had made an exempt function expenditure by contributing to the affiliated political organization, rather than paying administrative expenses, either directly or indirectly. The IRC 501(c)(6) organization determined the amount of its contribution by allocating an amount per member; not on the basis of actual indirect expenditures made by the political organization. Further, it took no steps to ensure that the amounts contributed would not be used for exempt function expenditures, which a political organization could reasonably be expected to

make.