



# 501(c)(4)s and the Gift Tax: Legal Analysis

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## Summary

Recent media reports of donors contributing substantial amounts to tax-exempt 501(c)(4) organizations have led some to ask whether these donations are subject to the federal gift tax. The short answer is that the gift tax statutes do not contain an exemption for these donations, thus indicating they are subject to tax. While some have argued that Congress did not intend this result, there is arguably insufficient evidence of such intent. As such, it appears the stronger argument is that contributions to 501(c)(4) groups are statutorily subject to the gift tax.

However, this analysis is complicated by two issues. First, it appears the Internal Revenue Service (IRS), while finding that these contributions are subject to tax, has not been enforcing this position for many years. This seemed to change in 2011, when the agency confirmed it had sent letters to five 501(c)(4) donors informing them that their contributions may be subject to the gift tax. In light of the agency's long silence on the issue, some asked whether the IRS inquiry was a politically motivated response to the growing involvement of 501(c)(4) organizations in campaign activities. The IRS denied having improper motivations, and the agency subsequently announced it was closing all examinations regarding the application of the gift tax and that any action would only be done prospectively. Thus, it appears that, for now at least, the gift tax will not be enforced on donations to 501(c)(4) groups.

Second, some have argued that while contributions to 501(c)(4) groups may be generally subject to the gift tax, those contributions made for advocacy-related purposes (e.g., issue advocacy, campaign activity, or lobbying) are exempt. Part of this argument is statutorily based, with the assertion that these types of donations may not be taxable gifts under at least three theories: (1) the donor may receive full and adequate consideration in the form of the organization's advocacy on his or her behalf; (2) some are made within the ordinary course of business; and (3) advocacy-related contributions were not the type of transfer that Congress intended the gift tax to cover. There is case law, albeit minimal, to support some of these conclusions; however, the holdings in these cases are not without controversy, and it is not clear the extent to which other courts would agree with their analysis.

Additionally, some have asserted that imposing the gift tax on advocacy-related donations would violate the donor's First Amendment rights to freedom of speech and association. The theory is that these types of contributions are a form of speech and since an individual could not be taxed for speaking directly on an issue or candidate, that person cannot be taxed for donating to an organization that will combine contributions from like-minded people to conduct such advocacy. On the other hand, it is not clear that a court would adopt this argument since the gift tax is a generally applicable, content neutral tax and therefore arguably does not impermissibly interfere with the donor's First Amendment rights.

## Contents

Gift Tax .....	2
Transfers to Tax-Exempt Organizations .....	3
Contributions Made for Political Purposes .....	5
Statutory Analysis.....	5
Constitutional Analysis: First Amendment.....	6

## Contacts

Author Contact Information.....	10
Acknowledgments .....	10

Recent media reports of large donations to some 501(c)(4) organizations have led to questions about whether these donations are subject to the federal gift tax.<sup>1</sup> The tax-exempt social welfare organizations described in Section 501(c)(4) of the Internal Revenue Code (IRC) must be “primarily engaged in promoting in some way the common good and general welfare of the people of the community.”<sup>2</sup> They include a broad variety of groups, some of which are politically focused, while others are not.<sup>3</sup>

The gift tax’s application to 501(c)(4) donations has recently been controversial. While the Internal Revenue Service (IRS) appears to take the position that these donations are subject to the gift tax,<sup>4</sup> it appears agency enforcement has been lax for many years.<sup>5</sup> In 2011, however, this seemed to be changing when the IRS confirmed reports that it had sent letters to five donors stating that their contributions to 501(c)(4) groups may be subject to the gift tax.<sup>6</sup> Some asked whether the IRS’s action was politically motivated,<sup>7</sup> particularly in light of the increased campaign activity by 501(c)(4) groups following the Supreme Court’s 2010 decision in *Citizens United v. FEC*.<sup>8</sup>

The IRS Commissioner denied the allegations of political motivations and explained that “the audits are part of a gift tax noncompliance project and are not connected to a broader separate project looking at the political and other activities of 501(c)(4) organizations.”<sup>9</sup> The agency subsequently announced it was closing all examinations regarding the application of the gift tax to such donations and that any action would only be done prospectively.<sup>10</sup> This has not necessarily

<sup>1</sup> See, e.g., Kenneth P. Vogel & Steve Friess, *Karl Rove hits big: The birth of a mega-donor*, POLITICO (July 13, 2012), T.W. Farnam, *Mystery donor gives \$10 million to Crossroads GPS group to run anti-Obama ads*, WASH. POST (April 13, 2012).

<sup>2</sup> Treas. Reg. §1.501(c)(4)-1(a)(2); IRC §501(c)(4) (describing among other entities “[c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare” with “no part of the net earnings of such entity inure[ing] to the benefit of any private shareholder or individual”).

<sup>3</sup> Under the IRC, 501(c)(4) groups may conduct unlimited lobbying and issue advocacy, and they may engage in campaign activity so long as it and other non-exempt purpose activities are not their primary purpose. See Treas. Reg. §1.501(c)(4)-1(a)(2). They are also regulated by election and lobbying laws. See CRS Report R40183, *501(c)(4) Organizations and Campaign Activity: Analysis Under Tax and Campaign Finance Laws*, by Erika K. Lunder and L. Paige Whitaker; CRS Report 96-809, *Lobbying Regulations on Non-Profit Organizations*, by Jack Maskell.

<sup>4</sup> See Rev. Rul. 82-216, 1982-2 C.B. 220 (“The Service continues to maintain that gratuitous transfers to persons other than [§527 political organizations] are subject to the gift tax absent any specific statute to the contrary, even though the transfers may be motivated by a desire to advance the donor’s own social, political or charitable goals.”).

<sup>5</sup> See Stephanie Strom, *I.R.S. Moves to Tax Gifts to Groups Active in Politics*, N.Y. TIMES (May 12, 2011); see also Comments of the Individual Members of the ABA Exempt Organizations Committee’s Task Force on Section 501(c)(4) and Politics at 13 (May 25, 2004), <http://www.abanet.org/tax/pubpolicy/2004/040525exo.pdf> (“There have been no public indications of IRS enforcement of gift tax on donations to §501(c)(4) entities for at least a decade, even in the obvious cases where individual donors have made very large, publicly disclosed contributions to §501(c)(4) organizations, such as ballot measure committees.”).

<sup>6</sup> See Strom, *supra* note 5.

<sup>7</sup> See, e.g., Brett Ferguson, *Camp Demands More Information From IRS on Audits of Five Donors to Nonprofits*, MONEY AND POL. REP. (June 16, 2011); Letter from Sen. Orrin G. Hatch et al., to Douglas H. Shulman, IRS Comm’r (May 18, 2011), <http://finance.senate.gov/newsroom/ranking/release/?id=ec29441e-aefd-4192-a628-d96966cf4231>.

<sup>8</sup> 130 S. Ct. 876 (2010); CRS Report R41045, *The Constitutionality of Regulating Corporate Expenditures: A Brief Analysis of the Supreme Court Ruling in Citizens United v. FEC*, by L. Paige Whitaker.

<sup>9</sup> Diane Freda, *Shulman Responds to Republican Concerns On Audits of Donations to 501(c)(4) Groups*, MONEY AND POL. REP. (June 6, 2011).

<sup>10</sup> See Internal Revenue Service, *IRS statement on applicability of gift tax on 501(c)(4) organization contributions*, <http://www.irs.gov/newsroom/article/0,,id=241592,00.html>; Memorandum from Steven T. Miller, Deputy Comm’r for (continued...)

quelled the concerns of those who questioned the agency's actions.<sup>11</sup> Nonetheless, the effect of this decision appears to be that, for now, the gift tax will not be enforced on donations to 501(c)(4) groups.

In addition to the current criticisms about the timing and targeting of the IRS's recent enforcement attempts, some have asked whether the IRS has the statutory authority to impose the gift tax on donations to 501(c)(4) organizations. Others, while recognizing that the gift tax may generally apply to donations to 501(c)(4) groups, have raised questions about whether donations made for advocacy-related purposes (e.g., issue advocacy, lobbying, and campaign activity) should be treated differently than other types of donations. Specifically, some have asked whether these types of donations might not meet the statutory definition of being a taxable gift and whether imposing the gift tax on such donations would violate the donor's First Amendment rights. These statutory and constitutional questions are analyzed below.

## Gift Tax

The federal gift tax is imposed on an individual's lifetime gifts of property.<sup>12</sup> The amount of the taxable gift is generally the fair market value of the gift at the time it was made, less certain exclusions and deductions.<sup>13</sup> Among other provisions, taxpayers may exclude from the federal gift tax base the first \$13,000 (\$26,000 for married couples) of cash or property given to each donee annually.<sup>14</sup> Additionally, taxpayers may be able to reduce any gift tax owed by claiming a life-time credit, which is known as the unified credit since it applies to both the gift and estate taxes. Using the credit to reduce the gift tax owed in one year will reduce the amount that can be used to reduce gift and estate taxes in future years. For 2012, the unified credit is \$5,120,000.<sup>15</sup>

For gift tax purposes, the amount of a gift is ascertained when "property is transferred for less than an adequate and full consideration in money or money's worth."<sup>16</sup> Treasury regulations provide that "a sale, exchange, or other transfer of property made in the ordinary course of

(...continued)

Services and Enforcement, to Comm'r, Small Bus./Self-Employed Div. and Comm'r, Tax-Exempt and Gov't Entities Div. (July 7, 2011), [http://www.irs.gov/pub/newsroom/guidance\\_for\\_irs\\_sbse\\_estate\\_and\\_gift\\_tax\\_and\\_tege\\_exempt\\_organizations.pdf](http://www.irs.gov/pub/newsroom/guidance_for_irs_sbse_estate_and_gift_tax_and_tege_exempt_organizations.pdf).

<sup>11</sup> Stephanie Strom, *I.R.S. Drops Audits of Donors to Political Groups*, N.Y. TIMES, July 7, 2011.

<sup>12</sup> IRC §2501(a). Treasury regulations provide that shareholders may be responsible for gift taxes when a corporation gives a gift. *See* Treas. Reg. §25.2511-1(h)(1). Note, however, that a transfer made for a business purpose is not a "gift." *See* Treas. Reg. §25.2512-8 ("a sale, exchange, or other transfer of property made in the ordinary course of business (a transaction which is bona fide, at arm's length, and free from any donative intent), will be considered as made for an adequate and full consideration ..."). For more information on the gift tax, see CRS Report 95-416, *Federal Estate, Gift, and Generation-Skipping Taxes: A Description of Current Law*, by John R. Luckey.

<sup>13</sup> IRC §2512.

<sup>14</sup> IRC §§2503(b), 2513; Rev. Proc. 2011-52, 2011-45 I.R.B. 701. The statutory amount for the exclusion is \$10,000, which is then adjusted for inflation.

<sup>15</sup> IRC §2010; Rev. Proc. 2011-52, 2011-45 I.R.B. 701. The unified credit's statutory amount is \$5 million, which is adjusted for inflation. However, the \$5 million threshold is scheduled to expire at the end of 2012, at which time the unified credit amount will be reduced to \$1 million (adjusted for inflation), absent congressional action. For information on the estate tax, see CRS Report 95-416, *Federal Estate, Gift, and Generation-Skipping Taxes: A Description of Current Law*, by John R. Luckey.

<sup>16</sup> IRC §2512(b); Treas. Reg. §25.2501-1(a).

business (a transaction which is bona fide, at arm's length, and free from any donative intent), will be considered as made for an adequate and full consideration in money or money's worth," and therefore is not a gift.<sup>17</sup>

## Transfers to Tax-Exempt Organizations

The gift tax statutes expressly address the treatment of donations to two types of tax-exempt organizations. First, transfers to political organizations, which are exempt under IRC Section 527, are excluded by statute from the gift tax.<sup>18</sup> Thus, under current law, donations of any size to a political organization may be given tax free (although federal or state election law may impose limitations).<sup>19</sup> Second, with respect to donations to charities, the gross estate is reduced by the value of certain charitable bequests and devises to qualified charitable organizations.<sup>20</sup> An estate tax deduction is generally permitted for any transfer which, if made during the decedent's lifetime would have been deductible for income tax purposes, though the rules are not identical.<sup>21</sup>

There is no similar statutory exclusion or deduction for transfers to 501(c)(4) organizations or other types of tax-exempt organizations. No regulation addresses the matter either. In rulings, the IRS has taken the position that these donations are subject to the gift tax.<sup>22</sup> If this position is to be challenged in court, it is not clear a court would give it much deference. The level of deference generally provided to these types of rulings varies, depending on such things as "the degree of the agency's care, its consistency, formality, and relative expertness, and... the persuasiveness of [its] position."<sup>23</sup> Here, given the long history of apparent non-enforcement and inconsistency regarding application of the gift tax to these groups, the IRS's interpretation is, arguably, entitled to little, if any, weight.

Nonetheless, it seems likely that a court would reach the same conclusion as the IRS and find that the statute's silence means donations to 501(c)(4) organizations are statutorily subject to the gift tax. This conclusion reflects the manner in which the gift tax is structured: the tax applies to all transfers, absent a specific exemption. And, it is supported by two fundamental canons of

<sup>17</sup> Treas. Reg. §25.2512-8; *see also* Treas. Reg. §25.251-1 ("The gift tax is not applicable to a transfer for a full and adequate consideration in money or money's worth, or to ordinary business transactions, described in §25.2512-8").

<sup>18</sup> IRC §2501(a)(4).

<sup>19</sup> *See, e.g.*, 2 U.S.C. §441a(a) (imposing monetary limits on the amounts that may be contributed to federal candidates, authorized political committees, and national party political committees, among others).

<sup>20</sup> IRC §2055.

<sup>21</sup> *Compare* IRC §§2055(a) and 170(c).

<sup>22</sup> *See* Rev. Rul. 82-216, 1982-2 C.B. 220 ("The Service continues to maintain that gratuitous transfers to persons other than organizations described in section 527 (e) of the Code are subject to the gift tax absent any specific statute to the contrary, even though the transfers may be motivated by a desire to advance the donor's own social, political or charitable goals.").

<sup>23</sup> *United States v. Mead Corp.*, 533 U.S. 218, 228 (2001); *see also* *U.S. Freightways Corp. v. Comm'r*, 270 F.3d 1137, 1142 (7<sup>th</sup> Cir. 2001) (noting revenue rulings, which have some precedential value and are official IRS interpretations of the tax code, are due deference according to their power to persuade, and therefore the lower court (the U.S. Tax Court) erred "[b]y noting only that revenue rulings 'are not entitled to the deference accorded a statute or a Treasury Regulation,' without explicitly acknowledging that some deference to revenue rulings is proper...."); *McDaniel v. Chevron Corp.*, 203 F.3d 1099, 1112 (9<sup>th</sup> Cir. 2000) ("Though revenue rulings do not have the force of law, they do constitute a body of experience and informed judgment to which we may look for guidance."); *Omohundro v. United States*, 300 F.3d 1065, 1067-68 (9<sup>th</sup> Cir. 2002) (examining revenue ruling under the standard articulated in *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), which bases deference on the agency's interpretation power to persuade); *Del Commercial Props., Inc. v. Comm'r*, 251 F.3d 210, 214 (D.C. Cir. 2001) (same).

statutory construction. First, under the canon of *expressio unius est exclusio alterius* (the inclusion of one is the exclusion of others), when Congress enumerates specific exceptions to a law and is silent regarding other matters, this suggests Congress did not intend to extend the exceptions to those other matters.<sup>24</sup> Here, the fact that Congress did not provide special treatment for donations to 501(c)(4) organizations, unlike that provided to 527 and 501(c)(3) organizations, supports the conclusion that Congress intended the 501(c)(4) donations to be subject to tax. Second is the rule against surplusage, under which “[a] statute should be construed so that effect is given to all its provisions, so that no part will be inoperative or superfluous, void or insignificant....”<sup>25</sup> Here, the argument is that exempting contributions to organizations involved in political activities from gift tax payments (other than 527 organizations that are statutorily exempted) would make parts of IRC Section 2522(a)(2) surplusage.<sup>26</sup> That statute provides for a gift tax deduction for donations to groups that qualify as charitable organizations. In order for a donor to take this deduction, the donee cannot be disqualified from 501(c)(3) status due to its lobbying or campaign activities.<sup>27</sup> Following from this, there is an argument that donations to 501(c)(4) organizations that do not qualify for 501(c)(3) status must be subject to the gift tax, absent any explicit statutory exemption; otherwise, the restrictions in Section 2522(a)(2) would be meaningless.

On the other hand, it might be argued that the IRS does not have statutory authority to impose the gift tax on donations to 501(c)(4) groups because Congress did not intend for the gift tax to apply to these types of donations. This argument rests on the view that the gift tax is designed to prevent avoidance of estate taxes. Under this view, the gift tax should be read as one with the estate tax,<sup>28</sup> and thus should only be applied in cases where a gift would have also been transferred upon the donor’s death or in anticipation of death.<sup>29</sup> Arguably, contributions to 501(c)(4) organizations (perhaps especially those made for advocacy-related purpose) are not these types of transfers.<sup>30</sup> However, it is not clear a court would adopt this analysis. First, the gift tax statute is written broadly, which arguably obviates the need for IRS officials to look into the difficult-to-determine

<sup>24</sup> See, e.g., *Iselin v. United States*, 270 U.S. 245, 250 (1926) (holding that where Congress subjected specific categories of ticket sales to taxation but failed to cover another category, either by specific or general language, courts should not extend coverage because to do so, given the “particularization and detail” with which Congress had set out the categories, would amount to “enlargement,” rather than “construction,” of the statute); *Andrus v. Glover Const. Co.*, 446 U.S. 608, 616-17 (1980) (“Where Congress explicitly enumerates certain exceptions to a general prohibition, additional exceptions are not to be implied, in the absence of a contrary legislative intent.”); *but see NationsBank v. Variable Annuity Life Ins. Co.*, 513 U.S. 251, 257 (1995) (statutory listing may be “exemplary, not exclusive”).

<sup>25</sup> *Hibbs v. Winn*, 542 U.S. 88, 101 (2004).

<sup>26</sup> See IRS Gen. Couns. Mem. 38930 (Dec. 3, 1982).

<sup>27</sup> IRC §§501(c)(3), 2522(a)(2).

<sup>28</sup> This principle of statutory interpretation is known as *in pari materia* (“part of the same material”), under which “statutes addressing the same subject matter generally should be read as if they were one law.” *Wachovia Bank v. Schmidt*, 546 U.S. 303, 315-16 (2006). The estate tax is found at IRC §§2001-2210.

<sup>29</sup> See *Estate of Sanford v. Comm’r*, 308 US 39, 44 (1939) (“[t]he gift tax was supplementary to the estate tax. The two are in *in pari materia* and must be construed together.”); H.R. REP. NO. 72-708, at 8 (1932) (noting the gift tax would “assist in the collection of the income and estate taxes, and prevent their avoidance through the splitting up of estates during the lifetime of a taxpayer ... ”); S. REP. NO. 72-665, at 11 (1932) (gift tax would serve as “a protection to both estate and income taxes.”). For more on the legislative history of the gift tax, see C. Lowell Harriss, *Legislative History of Federal Gift Taxation*, 18 TAXES 531 (1940).

<sup>30</sup> See *Carson v. Comm’r*, 71 T.C. 252, 261-62, *aff’d*, 641 F.2d 864 (10<sup>th</sup> Cir. 1981) (“It is doubtful that testamentary campaign contributions are problems plaguing estate planners or clogging probate courts. The vicissitudes of politics make political candidates an unlikely object for a decedent to “settle” his estate on ... ”).

true intent of a donor in transferring property for less than it is worth,<sup>31</sup> a conclusion that also seems to find support in the legislative history.<sup>32</sup> Second, much of the argument seems based on selected excerpts from the gift and estate taxes' legislative history, and it is uncertain the extent to which a court would find the history to be useful in addressing the issue at hand, particularly since it arguably includes support for contradictory positions. This might be especially true in light of the modern view of statutory interpretation that focuses on the language of the statute itself, which would appear to marginalize whatever insight legislative history or other extrinsic aids might provide.<sup>33</sup> Thus, a court might be hesitant to place any significance on the statute's minimal and ambiguous legislative history, particularly since it does not clearly evidence congressional intent one way or the other.

## Contributions Made for Political Purposes

While the above analysis supports the conclusion that current law imposes the gift tax on contributions to 501(c)(4) organizations, some might still make the argument that the gift tax does not apply to contributions made for advocacy-related purposes (e.g., issue advocacy, campaign activity, or lobbying). There are two separate theories that could be used to justify this argument: (1) some of these donations are not taxable gifts under the existing statute and regulations; and (2) the imposition of the gift tax on these types of donations would violate the donor's First Amendment rights. As discussed below, it is not clear a court would adopt either one.

### Statutory Analysis

First, some have argued that at least some of these types of donations are not taxable gifts.<sup>34</sup> One theory is that such transfers are not gifts because they are made for full and adequate consideration in the form of the donee organization's advocacy.<sup>35</sup> It might also be argued that at least some of these donations are made in the ordinary course of business or that donations used for advocacy-related purposes are not the types of gifts intended to be covered by the tax. Support for these latter positions could be found in two cases in which federal courts of appeals held, prior to the 527 political organization exclusion, that at least some political contributions were not

<sup>31</sup> *Comm'r v. Wemyss*, 324 U.S. 303, 306 (1945) ("Congress intended to use the term 'gifts' in its broadest and most comprehensive sense ... Congress chose not to require an ascertainment of what too often is an elusive state of mind").

<sup>32</sup> See S. REP. NO. 72-665, at 39 (1932) ("[t]he terms 'property,' 'transfer,' 'gift,' ... are used in the broadest and most comprehensive sense ..."); 75 CONG. REC. 5691 (1932) (statement of Rep. Charles Robert Crisp) ("Under existing law, a wealthy man can make gifts, and if they are not made in contemplation of death, no tax is paid on them. This has been a prolific source of disputes in courts, as to whether the gifts were made in contemplation of death ... This bill ... will remove these controversies, for this bill provides a gift tax on gifts whether made in contemplation of death or otherwise.").

<sup>33</sup> See, e.g., CRS Report 97-589, *Statutory Interpretation: General Principles and Recent Trends*, by Larry M. Eig, at 3 ("The strictures of a text-based 'plain meaning rule' were once thought honored more in the breach than in the observance. However, this perception has changed: More often than before, statutory text is thought to be the ending point as well as the starting point for interpretation") (citing to James J. Brudney & Corey Ditslear, *The Warp and Woof of Statutory Interpretation: Comparing Supreme Court Approaches in Tax Law and Workplace Law*, 58 DUKE L.J. 1231, 1258 (2009) for an example of an empirical study finding decreased reliance on legislative history by the Supreme Court from 1969 to 2008).

<sup>34</sup> Barbara K. Rhomberg, *The Law Remains Unsettled on Gift Taxation of Section 501(c)(4) Contributions*, 15 TAXATION OF EXEMPTS, 2004, at 6-18.

<sup>35</sup> See *id.* at 9-10.

gifts. In one case, the court found that the political contributions of a business owner, made with the goal of electing candidates who would create a more favorable business environment in the state, were made in the ordinary course of business and therefore not subject to the gift tax.<sup>36</sup> In the other case, the court determined that political contributions were not the type of transfer that Congress intended the gift tax to cover.<sup>37</sup>

On the other hand, whether a court would adopt any of these arguments is uncertain. The argument concerning full and adequate consideration appears to be a novel one. It is not clear a court would find the intangible benefit received by the donee to be adequate consideration, and a court might be particularly hesitant to adopt such an argument because it could be difficult to distinguish donations to other types of tax-exempt organizations (e.g., adopting this analysis could arguably make the statutory exemption for transfers to 527 organizations superfluous).<sup>38</sup> Furthermore, the holdings in the two cases are not without controversy, and the IRS subsequently issued a revenue ruling that expressed disagreement with the latter case.<sup>39</sup> It does not appear that any court has addressed this issue since these cases,<sup>40</sup> and it is not clear the extent to which other courts would agree with their analysis.<sup>41</sup>

## Constitutional Analysis: First Amendment

Second, some have argued that imposing the gift tax on contributions made for advocacy-related purposes would violate the donor's First Amendment rights to freedom of speech and the related right to freedom of association.<sup>42</sup> This argument is based on the assumption that at least some of

<sup>36</sup> See *Stern v. United States*, 436 F.2d 1327, 1330 (5<sup>th</sup> Cir. 1971) (holding a business owner's political contributions, made with the goal of electing candidates who would create a more favorable business environment in the state, were not gifts because they were made in the "ordinary course of business" since "[t]he transactions in controversy were permeated with commercial and economic factors" and "motivated by appellee's desire to promote a slate of candidates that would protect and advance her personal and property interests" and, therefore, "[i]n a very real sense, ... [the taxpayer] was making an economic investment that she believed would have a direct and favorable effect upon her property holdings and business interests ....").

<sup>37</sup> See *Carson v. Comm'r*, 641 F.2d 864, 866 (10<sup>th</sup> Cir. 1981) (holding the taxpayer's campaign contributions were not subject to the gift tax because the tax's history showed that its "main purpose ... is to prevent an avoidance of estate tax by an inter vivos transfer of property" and therefore campaign contributions, "when considered in light of the history and purpose of the gift tax, are simply not 'gifts' within the meaning of the gift tax law" (quoting the Tax Court's decision, 71 T.C. 252, 263-64 (1978)).

<sup>38</sup> See *Rhomberg*, *supra* note 34 at 9-10.

<sup>39</sup> See Rev. Rul. 82-216, 1982-2 C.B. 220 ("However, the Service's acquiescence in the result in the *Carson* decision should not be interpreted as an acceptance of the rationale of either the Tax Court or the Court of Appeals. The Service continues to maintain that gratuitous transfers to persons other than organizations described in section 527(e) of the Code are subject to the gift tax absent any specific statute to the contrary, even though the transfers may be motivated by a desire to advance the donor's own social, political or charitable goals.").

<sup>40</sup> The fact that this issue has remained dormant is not unexpected since: (1) the gift tax statutes now expressly exclude donations to 527 political organizations; (2) it appears the IRS has not rigorously enforced the gift tax on donations to certain types of 501(c) organizations; and (3) prior to *Citizens United*, it appears entities other than 527 political organizations engaged in relatively minimal levels of campaign activity.

<sup>41</sup> See, e.g., *Du Pont v. United States*, 97 F. Supp. 944, 946-47 (D. Del. 1951) (holding, prior to *Stern* and *Carson*, that a taxpayer's contributions to the National Economic Council were taxable gifts since he "received no direct and personal consideration for the transfer which may be accurately reduced to a money value" and "[a]ny consideration or benefit by the plaintiff was not a benefit accruing to him alone, but one enjoyed by every citizen of the country").

<sup>42</sup> U.S. CONST. Amend. I ("Congress shall make no law .. abridging the freedom of speech ... or the right of the people peaceably to assemble ... "); see also *Roberts v. United States Jaycees*, 468 U.S. 609, 622 (1984) ("implicit in the right to engage in activities protected by the First Amendment [is] a corresponding right to associate with others in pursuit of (continued...)").

these donations would be treated as “speech.” It might be argued these types of contributions are “speech” if donors expect their contributions will be pooled with those of like-minded individuals so organizations can lobby or advocate on their collective behalf.<sup>43</sup> However, donations are often not tied to a particular issue and, in cases where a donor essentially loses control over how the donation will be used, it might be more difficult to argue that the contribution is equivalent to the donor’s speech.<sup>44</sup> So, whether a donation could be considered speech may depend on what the donee does, why the donor is contributing to the donee, and whether there are any restraints on the donee’s use of the funds.

Were a contribution to be treated as “speech,” it is not clear that imposing the gift tax would be unconstitutional. While some might argue that imposing the gift tax on political contributions is an impermissible restriction on protected speech, it is not clear a court would adopt this argument with respect to the gift tax because it is a generally applicable, content neutral tax.

The starting point for any tax-related constitutional analysis is the recognition that Congress has broad powers to tax under the Constitution.<sup>45</sup> In general, determinations by Congress to distinguish among taxpayers or to tax some activities and not others are constitutionally permissible so long as “they bear a rational relation to a legitimate governmental purpose.”<sup>46</sup> The rational basis standard is a low level of review by a court, and in the tax context in particular, courts typically show great deference in recognition of “the large area of discretion which is needed by a legislature in formulating sound tax policies.”<sup>47</sup>

However, not all exercises of Congress’s taxing power receive such deference. Sometimes, tax provisions are subject to higher levels of scrutiny. For example, tax provisions based on the content of speech are, like non-tax provisions, typically subject to strict scrutiny.<sup>48</sup> A provision subject to this highest level of scrutiny must be necessary to serve a compelling government interest and be narrowly drawn to achieve that end.<sup>49</sup> This is a heavy burden for the government to meet.<sup>50</sup> In some instances, courts will apply an intermediate standard of scrutiny. For example,

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(...continued)

a wide variety of political, social, economic, educational, religious, and cultural ends”).

<sup>43</sup> See *Buckley v. Valeo*, 424 US 1, 65-66 (“The right to join together for the advancement of beliefs and ideas ... is diluted if it does not include the right to pool money through contributions, for funds are often essential if advocacy is to be truly or optimally effective.”) (internal quotations omitted).

<sup>44</sup> See Barbara K. Rhomberg, *Constitutional Issues Cloud the Gift Taxation of Section 501(c)(4) Contributions*, 15 TAXATION OF EXEMPTS, 2004, at 2-5. Also, contributions to 501(c)(4) groups for non-advocacy related purposes may not be “speech.” See *id.* at 8 (“Contributions to (501(c)(4)) organizations may support activities that are not principally expressive....Taxing such contributions ... does not implicate the First Amendment to any significant degree.”).

<sup>45</sup> U.S. CONST. Art. I, §8, cl. 1 (“The Congress shall have Power to lay and collect Taxes, Duties, Imposts and Excises....”).

<sup>46</sup> *Regan v. Taxation with Representation of Washington*, 461 U.S. 540, 547 (1983).

<sup>47</sup> *Id.* at 547 (internal quotations omitted).

<sup>48</sup> See *Arkansas Writers’ Project, Inc. v. Ragland*, 481 U.S. 221 (1987) (striking down a state sales tax that taxed general interest magazines, but exempted newspapers and religious, professional, trade, and sports magazines).

<sup>49</sup> See *id.* at 231.

<sup>50</sup> See *Minneapolis Star & Tribune Co. v. Minn. Comm’r of Revenue*, 460 U.S. 575, 582 (1983) (“A tax that burdens rights protected by the First Amendment cannot stand unless the burden is necessary to achieve an overriding governmental interest.”); *Arkansas Writers’ Project, Inc. v. Ragland*, 481 U.S. 221, 231 (1987) (“Arkansas faces a heavy burden in attempting to defend its content-based approach to taxation of magazines. In order to justify such differential taxation, the State must show that its regulation is necessary to serve a compelling state interest and is narrowly drawn to achieve that end.”).

the Supreme Court, when reviewing the constitutionality of provisions regulating campaign contributions that involve “significant interference with associational rights,” has determined that such regulation passes constitutional muster if “closely drawn to match a sufficiently important interest.”<sup>51</sup> The level of scrutiny is important since, looking at the two extremes, courts often uphold a challenged provision examined under the rational basis standard of review, while often striking down any provision subject to strict scrutiny.

Here, it might be argued that a more rigorous analysis should apply, either strict or intermediate scrutiny, since imposition of the taxes would be related to the exercise of a constitutional right.<sup>52</sup> It might be argued that imposing the gift tax or an excise tax on advocacy-related contributions infringes on First Amendment rights—e.g., because such contributions are a type of protected speech or because they would only apply to persons coming together to speak as a group, thus raising freedom of association concerns.<sup>53</sup> Proponents of such an argument might then look to the Supreme Court’s jurisprudence in both tax and campaign finance law for support that such infringement is constitutionally impermissible. For example, it might be argued that the taxes are analogous to those that the Court has previously looked upon with disfavor because they seemed intended to penalize certain taxpayers (here, taxpayers grouping together to engage in political or advocacy speech) or were essentially a fine for engaging in protected speech.<sup>54</sup> Furthermore, it might be argued that the tax could be particularly problematic if imposed on the tax-exempt groups that may engage in an unlimited amount of lobbying, like 501(c)(4) organizations, because it would leave no mechanism by which donations to groups that substantially lobby could escape taxation.<sup>55</sup> This is because the only groups for whom donations would be tax-free—501(c)(3) and 527 organizations—are both restricted in the amount of lobbying they may do.

Looking to campaign finance cases where courts have struck down bans or limits on various forms of political contributions or expenditures,<sup>56</sup> it might be argued that taxing political

<sup>51</sup> *FEC v. Beaumont*, 539 U.S. 146, 162 (2003) (internal quotations omitted).

<sup>52</sup> *See, e.g., Rhomberg supra* note 44 at 167-68.

<sup>53</sup> *See id.* at 169.

<sup>54</sup> *See Grosjean v. American Press Co.*, 297 U.S. 233, 250-51 (1936) (striking down a state tax that applied only to large newspapers, because “in the light of its history and of its present setting, it is seen to be a deliberate and calculated device in the guise of a tax to limit the circulation of information to which the public is entitled in virtue of the constitutional guaranties” and has “the plain purpose of penalizing the publishers and curtailing the circulation of a selected group of newspapers”); *Speiser v. Randall*, 357 U.S. 513, 519 (1958) (when striking down a state property tax exemption that required taxpayers take a loyalty oath and was clearly “aimed at the suppression of dangerous ideas” on the grounds that the state’s tax administration procedures did not afford adequate due process, the Court emphasized its chilling effect on the proscribed speech and equated it to a fine for engaging in that type of speech (internal quotations omitted)).

<sup>55</sup> *See Regan v. Taxation With Representation of Washington*, 461 U.S. 540, 544 (1983) (in upholding the federal law that limits the lobbying of §501(c)(3) organizations to “no substantial part” of their activities, the Court noted the organization had the option to set up a separate tax-exempt §501(c)(4) organization that could engage in the lobbying activities). The Court has emphasized the importance of the §501(c)(4) option in subsequent cases. *See, e.g., FCC v. League of Women Voters of Cal.*, 468 U.S. 364 (1984). *See also Rhomberg, supra* note 44 at 169-70 (arguing that imposing the gift tax on §501(c)(4) organizations that engage in lobbying raises constitutional concerns since the alternative organizations (§501(c)(3) and §527 organizations) are both restricted in the amount of lobbying they may do); *but see Ellen P. Aprill, Once and Future Gift Taxation of Transfers to Section 501(c)(4) Organizations: Current Law, Constitutional Issues, and Policy Consideration*, 15 N.Y.U. J. Legis. & Pub. Pol’y 289, 320 (arguing that those “concerns are unlikely to apply” because the gift tax is a generally applicable tax, as opposed to a “direct limit on speech as were the section 501(c)(3) limits on lobbying”).

<sup>56</sup> *See, e.g., Citizens United*, 130 S.Ct. at 908 (invalidating prohibitions on corporations using their general treasury funds to make certain campaign expenditures, calling them a “ban on speech”); *Citizens Against Rent Control v. Berkeley* 454 U.S. 290 (1981) (holding that a local ordinance limiting campaign contributions to committees violated (continued...))

contributions is a similar type of limitation since it could be seen as penalizing the making of donations and donors could thus be discouraged from donating any amount subject to tax.<sup>57</sup> Further, the Court in those cases has applied a balancing test weighing the extent of a law's infringement on First Amendment rights against the government's interest in maintaining the law, and it might be argued here that the government's traditional interest in tax collection is minimal, as exemplified by such things as the IRS's apparent decades-long period of non-enforcement regarding donations to 501(c)(4) groups, in relation to the taxes' infringement on free speech and association rights.<sup>58</sup> If so, it could be argued that the taxes would be unconstitutional.

On the other hand, it is not clear a court would find the imposition of the gift tax on advocacy-related contributions to be unconstitutional. The gift tax applies broadly to all taxable gifts, unless expressly exempted, regardless of the purpose for which the transferred money or property will be used. The tax does not prohibit transfers or impose a set limit on their amount. As such, the gift tax is a generally applicable tax that is content neutral and arguably does not penalize or target taxpayers who are engaging in activity protected by the First Amendment.<sup>59</sup> Thus, it might be argued that the decision by Congress to impose a tax on certain transfers of money or property would be within its broad taxing powers and subject to minimal review by a court.<sup>60</sup> It seems likely in such case that a court would find that any First Amendment infringement does not outweigh the government's interest in collecting taxes. Furthermore, the Supreme Court has clearly stated that there is no requirement for the federal government to subsidize the

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(...continued)

the First Amendment); *see also Rhomberg, supra* note 44, at 165-171 (using the Supreme Court's campaign finance law cases to analyze the constitutionality of imposing the gift tax on 501(c)(4) organizations).

<sup>57</sup> *See Rhomberg, supra* note 44 at 169-171 (arguing that application of the Supreme Court's jurisprudence is appropriate when assessing the constitutionality of imposing the gift tax on donations to 501(c)(4) groups and that the imposition of such tax "places a cap [i.e., the annual exclusion amount] on the amount that can be contributed for concerted speech without penalty, and thus places a upper limit on contributions"); *but see Aprill, supra* note 55 at 314-15 ("I reject application of the reasoning of these [campaign finance] cases to gift taxation of transfers to section 501(c)(4) organizations. Campaign finance regulation by its very nature is aimed directly at political speech. The limits are absolute.... The gift tax, in contrast, is not aimed only at section 501(c)(4) organizations that engage in political speech or even at section 501(c)(4) organizations, but more generally at all transfers for less than full and adequate consideration," unless exempted).

<sup>58</sup> *See Rhomberg, supra* note 44 at 169-71 (using the Supreme Court's campaign finance law jurisprudence to analyze the gift tax issue and concluding that the, under the balancing test, the government's interest in collecting these taxes is minimal); *but see Aprill, supra* note 57 (rejecting the application of campaign finance cases to the gift tax analysis).

<sup>59</sup> *See, e.g., Leathers v. Medlock*, 499 U.S. 439 (1991) (upholding a state's generally applicable sales tax as applied to cable television sales because even though there were exemptions for certain media (newspaper and magazine sales), the tax was content neutral and there was no evidence it targeted cable television); *see also Aprill, supra* note 55 at 314-18 (rejecting the application of the Supreme Court's campaign finance jurisprudence to analyzing the constitutionality of imposing the gift tax on donations to 501(c)(4) groups and finding support for the constitutionality of such imposition in the Supreme Court's tax law jurisprudence, including *Leathers* and several cases regarding the Establishment and Free Exercise clauses).

<sup>60</sup> *Cf. Leathers*, 499 U.S. at 453 (upholding a generally applicable, non-content based sales tax imposed on cable television sales and noting that its prior cases stand for the ideas a "tax scheme that discriminates among speakers does not implicate the First Amendment unless it discriminates on the basis of ideas" and "differential taxation of speakers, even members of the press, does not implicate the First Amendment unless the tax is directed at, or presents the danger of suppressing, particular ideas"); *Comm'r v. Tellier*, 383 U.S. 687, 693 (1966) ("Deduction of expenses falling within the general definition of §162(a) may, to be sure, be disallowed by specific legislation, since deductions are a matter of grace and Congress can, of course, disallow them as it chooses ...") (*quoting Comm'r v. Sullivan*, 356 U.S. 27, 28 (1958)); *see also Aprill, supra* note 55, at 318 ("The gift tax is a generally applicable tax. It does not aim at the content of speech. It is tested under the rational relation test and given a presumption of constitutionality.")

constitutional rights of taxpayers,<sup>61</sup> thus indicating that the government would not have to provide an exemption from the generally applicable gift tax for contributions that may be used for campaign-related purposes.<sup>62</sup> So, in the end, the fact that the gift tax is a content-neutral, generally applicable tax might be sufficient to quell any First Amendment concerns.

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<sup>61</sup> See *Cammarano v. United States*, 358 U.S. 498 (1959) (upholding the validity of a tax regulation that disallowed a business deduction for lobbying expenditures); *Taxation With Representation*, 461 U.S. at 545-46 (upholding the federal law that limits the lobbying of 501(c)(3) organizations to “no substantial part” of their activities).

<sup>62</sup> *Cammarano*, 358 U.S. at 513 (taxpayers “are not being denied a tax deduction because they engage in constitutionally protected activities, but are simply being required to pay for those activities entirely out of their own pockets, as everyone else engaging in similar activities is required to do under” the tax laws).