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Campaign Finance and Prohibiting Contributions by Tax-Exempt Corporations: *FEC v. Beaumont*

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Summary

The Federal Election Campaign Act (FECA) prohibits corporations, including tax-exempt, advocacy corporations, from using treasury funds to make direct contributions and expenditures in connection with federal elections. Corporations seeking to make such contributions and expenditures may legally do so only through a political action committee or PAC, 2 U.S.C. § 441b. The Supreme Court has long upheld the ban on corporate contributions, including those made by corporations that are tax-exempt under the Internal Revenue Code. However, in *FEC v. Massachusetts Citizens for Life, Inc.*, 479 U.S. 238 (1986), the Court created an exception for independent expenditures made by such entities that do not accept significant corporate or labor union money finding that restrictions on contributions require less compelling justification under the First Amendment than restrictions on independent expenditures. In *FEC v. Beaumont*, 123 S. Ct. 2200 (2003), North Carolina Right to Life (NCRL), a tax-exempt corporation, unsuccessfully attempted to extend the *MCFL* exception to contributions by tax-exempt corporations. Finding that limits on contributions are more clearly justified under the First Amendment than limits on expenditures, the Court reaffirmed the prohibition on *all* corporations making direct treasury contributions in connection with federal elections and upheld the ban on corporate contributions as applied to NCRL. This report provides an analysis of the Court's decision, including a brief discussion of possible implications for a pending Supreme Court case, *McConnell v. FEC,* which involves the constitutionality of the Bipartisan Campaign Reform Act (BCRA), also known as McCain-Feingold, P.L. 107-155 (H.R. 2356, 107th Cong.). Related CRS reports include CRS Report RS21551, *Campaign Finance: Issues Before the U.S. Supreme Court in McConnell v. FEC,* and CRS Report RL30669, *The Constitutionality of Campaign Finance Regulation: Buckley v. Valeo and Its Supreme Court Progeny*.

Background

The Federal Election Campaign Act (FECA) at 2 U.S.C. §441b prohibits corporations, including non-profit corporations that are tax-exempt under the Internal Revenue Code, from using treasury funds to make direct contributions and expenditures in connection with federal elections. Corporations seeking to make such contributions and expenditures may legally do so only through a political action committee or PAC, 2 U.S.C. § 441b. FECA further restricts who can contribute to such PACs, limits the amount of such contributions, and requires PACs to disclose their activities to the Federal Election Commission (FEC).[1] The Supreme Court has long upheld the ban on corporate contributions, including those made by Internal Revenue Code tax-exempt corporations. However, in *FEC v. Massachusetts Citizens for Life, Inc.*[2] the Court created an exception for independent expenditures made by such entities that do not accept significant corporate or labor union money. Consistent with its opinion in the landmark campaign finance decision *Buckley v. Valeo,*[3] the *MCFL* Court found that restrictions on contributions require less compelling justification under the First Amendment than restrictions on independent expenditures because contributions carry a greater risk of corruption.

Case History

Plaintiff NCRL brought suit in federal district court seeking to extend the *MCFL* exception to the Section 441b prohibition on corporate treasury fund direct contributions as applied to tax-exempt corporations. The district court granted summary judgment to NCRL and held that the prohibition is unconstitutional as applied to NCRL.[4] Likewise, the U.S. Court of Appeals for the Fourth Circuit ruled that the ban was unconstitutional as applied to NCRL, relying primarily on the Supreme Court's decision in *MCFL*. According to the Fourth Circuit, the rationale behind the *MCFL* exception for independent expenditures made by entities that do not accept significant corporate or labor union money also applies to *contributions*, and as an *MCFL*-type corporation, NRCL is constitutionally exempt from the prohibition.[5]

Supreme Court Decision

On June 16, 2003, in a 7-2 decision, the Supreme Court in *FEC v. Beaumont*[6] reversed the Fourth Circuit, and reaffirmed the prohibition on *all* corporations making direct treasury contributions in connection with federal elections and upheld the ban on corporate contributions as applied to NCRL. Maintaining the distinction between contributions and expenditures, the Court found that limits on contributions are more clearly justified under the First Amendment than limits on expenditures because of their greater link to corruption.[7]

[1] 2 U.S.C. §§ 441a, 441b(b)(3),(4).

[2] 479 U.S. 238 (1986).

[3] 424 U.S. 1 (1976).

[4] 137 F. Supp. 648 (EDNC 2000).

[5] 278 F. 3d 261 (4th Cir. 2002).

[6] Christine Beaumont is an eligible voter in North Carolina who joined NCRL in filing suit against the FEC.

[7] FEC v. Beaumont, 123 S. Ct. 2200 (2003).

Writing for the Court, Justice Souter said that any attack on the federal prohibition against corporate contributions from treasury funds is contrary to a century of congressional efforts to curb the potential of corporate "deleterious influences on federal elections." The current law originated from public opinion in the late 19th century "that aggregated capital unduly influenced politics, an influence not stopping short of corruption," which resulted in President Theodore Roosevelt supporting enactment of the Tillman Act of 1907, the first federal statute to prohibit corporate political contributions. The Court noted that the public policy interest behind today's law still focuses on restricting the influence of political war chests funneled through the corporate structure that "threaten the integrity of the political process."[8] In elaborating on the rationale behind the prohibition, the Court quoted from its 1990 decision in *Austin v. Michigan Chamber of Commerce*:

> State law grants corporations special advantages—uch as limited liability, perpetual life, and favorable treatment of the accumulation and distribution of assets—hat enhance their ability to attract capital and to deploy their resources in ways that maximize the return on their shareholders' investments. These state-created advantages not only allow corporations to play a dominant role in the Nation's economy, but also permit them to use 'resources amassed in the economic marketplace' to obtain 'an unfair advantage in the political marketplace.'[9]

The Court further stated that subsequent amendments to the federal election law have consistently strengthened the original, core prohibition on direct corporate treasury contributions and, as its decision in *Austin v. Michigan Chamber of Commerce* and other recent Supreme Court campaign finance opinions have demonstrated, the rationale behind the prohibition has endured.[10]

In addition to preventing corruption or the appearance of corruption, the Court found that the prohibition on corporate treasury fund contributions protects individuals who have paid money into a corporation for reasons other than to support candidates from having their money used to support candidates to whom they may be opposed. Moreover, the Court determined that the prohibition protects against a corporation serving as a conduit for "circumvention of [valid] contribution limits."[11] That is, the persons who created, own, or are employed by the corporation could exceed their individual contribution limits by diverting money through the corporation, which could in turn make political contributions. Invoking its recent decision regarding limits on coordinated expenditures by political parties, the Court cautioned, "experience 'demonstrates how candidates, donors, and parties test the limits of the current law, and it shows beyond serious doubt how contribution limits would be eroded if inducement to circumvent them were enhanced.'"[12]

In summarizing its findings, the Court emphasized that its campaign finance decisions "represent respect for the 'legislative judgment that the special characteristics of the corporate structure require particularly careful regulation,'" and demonstrate that the Court understands that such "deference to legislative choice is particularly warranted when Congress regulates campaign contributions, carrying as they do a plain threat to political integrity and a plain warrant to

[8] *Id.* at 2205-06, (citing United States v. Automobile Workers, 352 U.S. 567, 585 (1957)).

[9] 494 U.S. 652, 658-659 (1990)(quoting Massachusetts Citizens for Life, 479 U.S. at 257).

[10] Beaumont, 123 S. Ct. at 2206, (citing FEC v. National Right to Work Comm., 459 U.S. 197, 207 (1982); FEC v. National Conservative Political Action Comm., 470 U.S. 480, 500-01 (1985)).

[11] Id. at 2207, (quoting FEC v. Colorado Republican Federal Campaign Comm., 533 U.S. 431, 456, and n. 18 (2001)).

[12] *Id.* (quoting Colorado Republican Federal Campaign Comm., 533 U.S. at 457).

counter the appearance and reality of corruption and the misuse of corporate advantages."[13] The Court also clarified that limits on contributions are more clearly justified than limits on other kinds of political spending, "corruption being understood not only as *quid pro quo* agreements, but also as undue influence on an officeholder's judgment, and the appearance of such influence."[14]

Turning to the specific question of whether 2 U.S.C. §441b applies to NCRL, the Court determined that its holding in *FEC v. National Right to Work Comm.*, as interpreted by subsequent Court decisions, generally approves of the applicability of the Section 441b prohibition to tax-exempt corporations "without great financial resources." For example, in *FEC v. National Conservative Political Action Comm.*, the Court noted that it interpreted *National Right to Work* as consistent with the "well established constitutional validity of ... regulat[ing] corporate contributions," including contributions by membership corporations that "might not exhibit all the evil that contributions by traditional economically organized corporations exhibit."[15] Stating its refusal to "second-guess a legislative determination as to the need for prophylactic measures where corruption is the evil feared," the Court rejected the argument that deference to congressional judgments is determined by whether the corporations affected by a regulation are for-profit or non-profit.[16]

The Fourth Circuit relied on *MCFL* in concluding that Section 441b cannot constitutionally apply to a tax-exempt advocacy corporation such as NCRL. However, *MCFL* made an important distinction between restrictions on contributions and restrictions on expenditures, *i.e.*, "restrictions on contributions require less compelling justification than restrictions on independent spending."[17] In *Beaumont*, the Court found that the "corrupting potential" underlying the ban on using corporate treasury funds "may indeed be implicated by advocacy corporations."[18] Like for-profit corporations, non-profit advocacy corporations enjoy substantial state-conferred advantages, are able to amass significant funds for political use, and are also capable of serving as conduits for individuals attempting to circumvent contribution limits.[19]

The *Beaumont* Court also clarified the standard for review applicable to campaign finance regulation under the First Amendment. In the view of the Court, determining the appropriate standard of review depends on the nature of the activity being regulated. Commencing with its 1976 ruling in *Buckley*, the Court said that it has treated the regulation of contributions as only a "marginal" speech restriction, subject to "relatively complaisant review under the First Amendment," since contributions are a less direct form of speech than expenditures.[20] Hence, the Court concluded that instead of requiring a contribution regulation to pass strict scrutiny by

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[13] *Id.* (quoting National Right to Work Comm., 459 U.S. at 209-10).

[14] *Id.* (quoting Colorado Republican Federal Campaign Comm., 538 U.S. at 440-41).

[15] *Id.* at 2208 (quoting National Conservative Political Action Comm., 470 U.S. at 500-01).

[16] *Id.* at 2209-10 (quoting National Right to Work Comm., 459 U.S. at 210).

[17] *Id.* at 2209 (quoting National Right to Work Comm., 459 U.S. at 260).

[18] *Id.* at 2209-10.

[19] *Id.* at 2207. Indeed, the Court further notes that some of the most powerful organizations in the U.S. are tax-exempt, advocacy corporations such as the American Association of Retired Persons, the National Rifle Association, and the Sierra Club. *Id.* at 2209-10.

[20] The Court explained that "[w]hile contributions may result in political expression if spent by a candidate or an association ..., the transformation of contributions into political debate involves speech by someone other than the contributor." *Id.* at 2210 (quoting Buckley, 424 U.S. at 20-21).

meeting the requirement that it be narrowly tailored to serve a compelling governmental interest, a contribution regulation involving "significant interference with associational rights" passes constitutional muster by merely satisfying the lesser requirement of "being 'closely drawn' to match a 'sufficiently important interest.'"[21] With regard to the Section 441b prohibition, the Court held that it passes this lower level of scrutiny because it does not render a complete ban on corporate contributions, *i.e.*, corporations are still permitted to use treasury funds to establish, solicit funds for, and pay the administrative expenses of a political action committee or PAC, which can then in turn make contributions.[22] Invoking its unanimous holding in *FEC v. National Right to Work*, the Court rejected the argument that the regulatory burdens on PACs, including restrictions on their ability to solicit funds, renders a PAC unconstitutional as the only way that a corporation can make political contributions.[23]

In summary, the Supreme Court in *FEC v. Beaumont* upheld the ban on corporate contributions as applied to NCRL because corporate campaign contributions—including contributions by tax-exempt advocacy corporations—pose a risk of harm to the political system; consequently, the courts owe deference to legislative judgments on how best to address their risk of harm; and limits on contributions are merely "marginal" speech restrictions subject to a "relatively complaisant" or lesser review under the First Amendment than the strict scrutiny standard of review.

In his dissent, Justice Thomas, joined by Justice Scalia, maintained that the strict scrutiny standard of review should apply in *Beaumont*, and that under that standard, Section 441b would be unconstitutional. Justice Anthony Kennedy wrote a concurrence agreeing with the majority on the specific prohibition at issue, but noting that if a comprehensive examination of the distinction between contributions and expenditures were under review, he might have joined with the dissent.[24]

Possible Implications for BCRA in *McConnell v. FEC*

The Supreme Court's ruling in *FEC v. Beaumont* has prompted commentary regarding possible implications for the pending campaign finance litigation, *McConnell v. FEC*, where the Court will be considering the constitutionality of major provisions of the recently enacted Bipartisan Campaign Reform Act (BCRA), P.L. 107-155. Although BCRA places significant restrictions on corporations, including a ban on corporations using treasury funds to pay for "electioneering communications" 30 days before a primary and 60 days before a general election (Section 203), it does not affect the statutory provision that was upheld in *Beaumont*. Among other provisions, BCRA also prohibits political parties from raising unregulated soft money contributions from corporations and labor unions (Section 101).

On the one hand, commentators supporting BCRA infer from the *Beaumont* ruling that the Court will continue to exercise "deference to legislative choice" in order to uphold key provisions of

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[21] *Id.* (quoting Buckley, 424 U.S. at 25; *cf.* Austin, 494 U.S. at 657).

[22] In the Court's view, "[t]he PAC option allows corporate political participation without the temptation to use corporate funds for political influence, quite possibly at odds with the sentiments of some shareholders or members, and it lets the government regulate campaign activity through registration and disclosure, see §§ 432-434, without jeopardizing the associational rights of advocacy organizations' members." *Id.* at 2211.

[23] *Id.* (citing National Right to Work, 459 U.S. at 201).

[24] *Id.* at 2211.

BCRA.[25] In addition, BCRA supporters note that *Beaumont* expressly held that prohibiting corporate treasury contributions does not violate the First Amendment because corporations are still permitted to use treasury funds to establish, solicit funds for, and pay the administrative expenses of a PAC, which can then in turn make political contributions.[26]

On the other hand, commentators challenging the constitutionality of BCRA emphasize that the *Beaumont* decision narrowly affirms corporate contribution limits and is restricted to the issue of campaign *contributions*, while the *McConnell* case involves political expenditures.[27] Any implications for BCRA, they maintain, are extremely narrow.[28]

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[25] Linda Greenhouse, *Supreme Court Roundup; Ban on Corporate Contributions Is Upheld*, N.Y. TIMES, June 17, 2003.

[26] Eliza Newlin Carney, *Rules of the Game, Beaumont's Clues for McConnell*, NATIONAL JOURNAL, June 30, 2003.

[27] *Id.* (citing statements by election lawyer James Bopp, Jr., who argued on behalf of plaintiff North Carolina Right to Life, Inc. in *Beaumont* and represents clients in *McConnell v. FEC*).

[28] Frank J. Murray, *Campaign-Fund Caps Imposed on Non-profits*, THE WASHINGTON TIMES, June 17, 2003 (citing statements by Kenneth W. Starr, who represents Senator McConnell in *McConnell v. FEC*.)