

2-22-2014

# Comments on Guidance for Tax-Exempt Social Welfare Organizations on Candidate-Related Political Activities

Brian D. Galle

*Boston College Law School*, [brian.galle@bc.edu](mailto:brian.galle@bc.edu)

Donald B. Tobin

*University of Maryland Francis King Carey School of Law*, [dtobin@law.umaryland.edu](mailto:dtobin@law.umaryland.edu)

Follow this and additional works at: <http://lawdigitalcommons.bc.edu/lspf>



Part of the [Election Law Commons](#), and the [Taxation-Federal Income Commons](#)

---

## Recommended Citation

Brian D. Galle and Donald B. Tobin. "Comments on Guidance for Tax-Exempt Social Welfare Organizations on Candidate-Related Political Activities." *Ohio State University Moritz College of Law Working Paper Series* no.239 (2014).

This Article is brought to you for free and open access by Digital Commons @ Boston College Law School. It has been accepted for inclusion in Boston College Law School Faculty Papers by an authorized administrator of Digital Commons @ Boston College Law School. For more information, please contact [nick.szydowski@bc.edu](mailto:nick.szydowski@bc.edu).



**Comments on Guidance for Tax-Exempt Social  
Welfare Organizations on Candidate-Related  
Political Activities**

Brian Galle

Donald Tobin

**Working Paper Series  
No. 239**

**February 22, 2014**



This working paper series is co-sponsored by the  
Center for Interdisciplinary Law and Policy Studies  
at the Moritz College of Law

This paper can be downloaded without charge from the  
Social Science Research Network Electronic Paper Collection:  
<http://ssrn.com/abstract=2399315>



**Comments on Guidance for Tax-Exempt Social  
Welfare Organizations on Candidate-Related  
Political Activities**

Brian Galle

Donald Tobin

**Working Paper Series  
No. 239**

**February 22, 2014**



This working paper series is co-sponsored by the  
Center for Interdisciplinary Law and Policy Studies  
at the Moritz College of Law

This paper can be downloaded without charge from the  
Social Science Research Network Electronic Paper Collection:  
<http://ssrn.com/abstract=2399315>

**Comments on Guidance for Tax-Exempt Social Welfare  
Organizations on Candidate-  
Related Political Activities**

**Submitted by:**

**Brian Galle  
Associate Professor  
Boston College Law School**

**Donald Tobin,  
John C. Elam/Vorys Sater Professor of Law,  
Ohio State University Moritz College of Law.**

**Feb. 22, 2014**

**SSRN Cover Sheet**

February 24, 2014

The Honorable John A. Koskinen  
Commissioner of Internal Revenue  
CC:PA:LPD:PR (REG-134417-13), Room 5205  
Internal Revenue Service  
1111 Constitution Avenue NW  
Washington, DC 20224

**Re: Comments on Guidance for Tax-Exempt Social Welfare Organizations on Candidate-Related Political Activities, 78 Fed. Reg. 71,535 (proposed Nov. 29, 2013) (to be codified at 26 C.F.R. pt. 1)**

**Submitted By:**

**Brian Galle, Associate Professor, Boston College Law School; and  
Donald Tobin, John C. Elam/Vorys Sater Professor of Law, Ohio State University Moritz  
College of Law.**

Dear Commissioner Koskinen:

We respectfully submit these comments in response to the Notice of Proposed Rulemaking (the “Notice”) issued by the Internal Revenue Service (the “IRS” or “Service”) and the Treasury Department on November 29, 2013. :

### **Executive Summary**

The Notice is a good first step. It creates bright-line standards that are easy to apply and that will eliminate much of the gray area regarding permissible political activity. Clearer lines will reduce the discretion on the part of the IRS. By decreasing the IRS’s discretion, the regulation will reduce the opportunity for the IRS to be used as a political tool in an Administration’s tool box.

However, the Notice does not go far enough. Congress has established a regulatory regime that has as its central purpose the disclosure of any significant campaign contributions by individuals or firms. In recent years many organizations have exploited the confidentiality rules of § 501(c)(4) to evade that regime, to the detriment not only of U.S. political discourse but also

the non-profit sector. The Final Rule should ensure that groups with significant partisan political activity cannot obtain exemption under § 501(c)(4), or indeed under any parallel provision of § 501.

We believe, however, that groups carrying out “substantial” electioneering activities should generally be eligible for exemption under § 527, and that the IRS should make that clear in the Final Rule. The main consequence of any ruling denying § 501(c)(4) status based on the political activity of the organization, therefore, would simply be to require the disclosure of an organization’s donors, and to ensure that the organization’s political expenditures are disclosed contemporaneously with the election they seek to influence.

Accordingly, the Final Rule should be designed in a way that channels organizations with any substantial amount of undisclosed electioneering activity into § 527. For example, we propose a strong presumption that any group with candidate-related political activity of more than 10% of its budget, or of more than an overall cap of some amount, such as \$1 million, whichever is lesser, should be recognized as a § 527 political organization and not as a § 501(c)(4) social welfare organization. The final rule should interpret “electioneering” broadly to include facially non-partisan activities that can be used to partisan advantage, including candidate-related advertising that falls outside the window immediately surrounding an election. Groups that voluntarily disclose their donors could retain c(4) status.

Additionally, we suggest that the IRS seriously consider developing rules to limit the use of for-profit entities to evade § 527. We urge the IRS to take a clearer stand on its enforcement plans and legally dubious Forms 990. And we argue that nothing in the Notice, or in what we additionally suggest here, would raise serious First Amendment concerns.

## **Congressional Purpose to Bring Transparency to Campaign Funding Should Be the Cornerstone of the Regulations**

The Final Regulation should ensure that sections 501 and 527 work together seamlessly to ensure that political expenditures of any significant size are disclosed to the American public in a timely fashion. Transparency was a key Congressional purpose when it amended § 527 in 2000, and we believe it remains a critically important policy. The Final Regulation can achieve that result by adhering closer to the statutory language in § 501(c)(4) and adopting a definition of the statutory term “exclusively” that is closer to the ordinary meaning of that word. The current regulation allows an organization to claim social welfare status as long as social welfare is its primary activity, instead of requiring the organization to be exclusively involved in such activity. In doing so, the regulations allow organizations to circumvent congressional intent with regard to campaign disclosure contained in § 527. By adopting a definition closer to the ordinary meaning of exclusively, instead of the more liberal definition, campaign contributions will be funneled into § 527 political organizations and governed by the applicable disclosure rules.

The legislative history of §527 demonstrates Congress’ desire to reveal the sources of political spending. As was widely reported in the run-up to the amendments, voters and congresspersons alike were “outraged” by news that “shadowy political organizations” had spent millions influencing that term’s elections.<sup>1</sup> Senator Lieberman, a sponsor of the legislation expressed his fear that:

None of us should doubt that the proliferation of these groups– with their potential to serve as secret slush funds for candidates and parties, their ability to run difficult-to-trace attack ads, and their promise of anonymity to those seeking to spend huge amounts of money to influence our elections – poses a real and significant threat

---

<sup>1</sup> *Mobile Republican Assembly v. United States*, 353 F.3d 1357, 1359-60 (11th Cir. 2003) (noting that § 527(j) was enacted in part “in response to the spectacular increase in the use of § 527 organizations for tax-exempt political expenditures with limited public scrutiny”). For cogent reviews of the history of the § 527 amendments, see Ellen P. Aprill, *Regulating the Political Speech of Noncharitable Exempt Organizations After Citizens United*, 10 ELECTION L.J. 363 (2011); Richard Briffault, *The 527 Problem ... and the Buckley Problem*, 73 GEO. WASH. UNIV. L. REV. 949 (2005).

to the integrity and fairness of our elections. . . .<sup>2</sup>

Congress had earlier attempted to shine a light on political spending in an amendment to FECA, which provide for disclosure of all direct contributions of \$200 or more to candidates for federal public office. Another key motivation for the §527 amendments was to prevent the use of nonprofits to evade FECA's disclosure limits.<sup>3</sup>

In response, Congress amended §527 to provide for disclosure of all but the smallest political contributions and expenditures. Donee organizations must disclose all contributors of \$200 or more, and all expenditures by the firm of \$500 or more.<sup>4</sup> Not coincidentally, the \$200 individual contribution threshold mirrors FECA.

Section 527 also ensures that disclosure of political activities will be available to the public in time for voters to make use of that information. While § 501(c)(4) organizations must disclose "political campaign and lobbying activities" on their annual tax return, that document need not be filed until after the close of the organization's fiscal year. In contrast, § 527(j) requires disclosures no later than twelve days before and thirty days after each election.

A relatively restrictive definition of "exclusively" thus effectuates congressional purpose to the extent that it prevents groups from using § 501(c)(4) to circumvent the §527 and FECA disclosure rules, as many have done. Organizations wishing to organize as social welfare organizations instead of as political organizations embraced several techniques to putatively meet the social welfare purpose requirement. While some groups mixed their electioneering with substantial amounts of recognized social welfare activities, such as lobbying, others sought

---

<sup>2</sup> See 146 CONG. REC. S8333 (daily ed. May 17, 2000) (statement of Sen. Lieberman).

<sup>3</sup> See 146 CONG. REC. S4110 (daily ed. May 17, 2000) (statement of Rep. Haughton); *Mobile Republican Assembly*, 353 F.3d at 1359-60 (describing § 527(j) as a response to judicial opening of loopholes in the original text of FECA); April, 10 ELECTION L.J. at 385-86.

<sup>4</sup> I.R.C. § 527(j)(1), (j)(3)(A), (j)(3)(B) (requiring disclosure of donors who contribute more than \$200, and expenditures by the organization over \$500).

to meet § 501(c)(4)'s requirements by classifying campaign related activities as social welfare activities. Contrary to rulings from the IRS, many of these groups appeared to take the position that as long as the activity was not election related under the Federal Election Commission (FEC) rules, it was a social welfare activity.<sup>5</sup> Some groups even took the position that communication that was reported to the FEC was not campaign intervention activity for purposes of determining social welfare status.<sup>6</sup>

Since there is little net tax advantage to § 501(c)(4) status --- indeed, § 527 organizations appear to fall outside the coverage of major nonprofit regulatory regimes that might impose excise taxes, such as § 4958<sup>7</sup> --- it is evident that the purpose for the camouflage we have described is to evade § 527(j).<sup>8</sup> The IRS should not allow groups to avoid disclosure by impersonating social welfare organizations when the organizations are really political organizations. Nor should the IRS permit groups that are not wholly political, but wish to conceal political contributions or expenditures that would be disclosable under §527(j), from hiding under the cloak of § 501(c)(4).

### **Separating Elections and Social Welfare Is Good Nonprofit Policy**

Election law aside, limiting electioneering by nonprofit organizations is necessary to preserve a well-functioning independent sector. Because nonprofits offer only weak mechanisms for oversight of their managers, and because of the absence of any disciplining market for

---

<sup>5</sup> *E.g.*, Joe Hallett, *It'll be a long campaign for Ohio's fact-checkers*, COLUMBUS DISPATCH, June 9, 2013 (noting that We the People Convention, Inc., claimed activities were education but that conventions were "showcases for conservative politics and candidates."); Club for Growth, IRS Form 990 for Fiscal Year 2012, Sched. C p.3.

<sup>6</sup> Barber, *How Nonprofits Spend Millions on Elections and Call it Public Welfare*, ProPublica, Aug. 18, 2012, available at <http://www.propublica.org/article/how-nonprofits-spend-millions-on-elections-and-call-it-public-welfare>.

<sup>7</sup> See I.R.C. § 4958(e) (stating that intermediate sanctions regime applies to 501(c)(3), (4), and (29) organizations).

<sup>8</sup> Contributions to section 501(c)(4) and 527 organizations may differ slightly in their effects on donors. For example, transfers to § 527 organizations may escape the federal gift tax, while donations to § 501(c)(4) arguably do not. Aprill, 10 ELECTION L.J. at 384-85; *see also* Tobin, *The Application of the Gift Tax Provisions in the Internal Revenue Code to § 501(c)(4) Organizations*, ElectionLaw@Moritz, available at <http://moritzlaw.osu.edu/electionlaw/comments/index.php?ID=8335>.

corporate control, nonprofit stakeholders have only tenuous influence over the behavior of those who run the firm. In such an environment, partisan political activity presents a danger of deeply disrupting the original charitable or social welfare aims of the organization. Managers may trade off the firm's resources for personal gain or ideological goals, or otherwise distort the mission of the organization to please possible political allies, and stakeholders will be largely powerless to intervene.

Even if relatively few managers actually misuse their influence in these ways, the very possibility that they might do so can damage all nonprofits.<sup>9</sup> Rational donors will not give money knowing that their contribution can easily be diverted to private goals without their knowledge. Indeed, most commentators now believe that the very existence of the nonprofit form is a response to exactly this problem of managerial opportunism.<sup>10</sup> More generally, public confidence in the mission and efficacy of the nonprofit sector could be undermined by perceptions that it is involved in partisan conflict. Since these effects are all "externalities" --- that is, they harm outsiders as well as those within any individual nonprofit --- stakeholders of each individual nonprofit will rationally under-invest in efforts to prevent them. Government intervention is necessary.

These considerations also make a strong case for mandating transparency of nonprofit political involvement. If nonprofits could credibly disclose the extent of outside political influence, donors and other supporters would no longer have reasons to doubt that firms are committed to their social welfare mission. In the absence of regulatory mandates and oversight, however, no such disclosures are credible, since it is in the interest of all managers to claim there

---

<sup>9</sup> The undersigned have addressed these issues in greater depth elsewhere. Brian Galle, *Charities in Politics: A Reappraisal*, 54 WM. & MARY L. REV. 1561, 1591-1614 (2013); Donald B. Tobin, *Political Campaigning by Churches and Charities: Hazardous for 501(c)(3)s, Dangerous for Democracy*, 95 GEO. L.J. 1313, 1319-42 (2007).

<sup>10</sup> Henry B. Hansmann, *Reforming Nonprofit Corporation Law*, 129 U. PA. L. REV. 497, 506-07 (1981).

is little outside influence and stakeholders have no reliable means of verifying the claim. We emphasize the importance of disclosing outside support because stakeholders also cannot easily observe nonprofit outputs; it is hard to tell if the manager is trading off some aspect of the social welfare mission for political gain. By requiring disclosure of both politically-motivated donors and firms' political spending, the government could somewhat alleviate the other stakeholders' dilemma.

We acknowledge, however, that transparency to such a degree would potentially conflict with the apparent congressional policy of maintaining confidentiality for donors to most non-political nonprofit organizations. Accordingly, to the extent that greater transparency is not possible within the bounds of § 501(c)(4), we believe that the best remaining approach would be to separate most political spending from charitable and social welfare firms. As we explain below, however, we do think some incrementally greater transparency is possible, even within the strictures of § 6103.

### **The Final Regulation Should Revisit the “Primary Purpose” Standard**

Although the Notice does not address the primary purpose standard, it does invite comment regarding whether the standard should be revised, what amount of activity should constitute primary purpose and how that amount should be calculated. If the final regulations are going to usefully curtail abusive activity, they must clarify the primary purpose standard. Under the current vague standard, groups, and it appears the IRS, have no clear guidance regarding what constitutes the primary purpose of an organization.<sup>11</sup> The vague standard, especially in light of the IRS's lack of enforcement, allows groups to self-determine the amount of social welfare activity that is sufficient to justify exempt status. If the IRS cannot articulate a standard

---

<sup>11</sup> Commentators have suggested anywhere from 10% to 49.9% might be allowed under the standard.

for organizations to follow there is a significant risk that the IRS will once again find itself being accused of biased enforcement.

Therefore the Final Regulation should clarify the amount of non-exempt activity that is allowed under the primary purpose standard. In the church and charity context, the IRS has provided guidance regarding the primary purpose standard and through regulations has indicated that in order to satisfy the primary purpose standard an organization may engage in only an insubstantial amount of non-exempt activity. An ABA task force recommended that forty percent of a group's activity could be for a non-exempt purpose, and the IRS appears to have been, at some point, applying a fifty-percent standard.<sup>12</sup> In related contexts, courts have generally rejected a firm percentage rule in favor of generalized balancing tests.<sup>13</sup>

In keeping with the principles we outlined above, we would propose a much more restrictive standard whose primary effect would be that most cash contributions be subject to the § 527 disclosure regime, as Congress intended. As we will explain, we believe that any organization that fails to qualify for § 501(c)(4) by reason of its political activity should, and under current law could, be eligible for exemption under §527. Therefore, since disclosure is the main justification we see for separate classification of 527 and c(4) groups, § 501(c)(4) organizations that voluntarily disclose all donations should be exempt from additional scrutiny.<sup>14</sup>

---

<sup>12</sup> See *Comments of the Individual Members of the Exempt Organizations Committee's Task Force on Section 501(c)(4) and Politics* 9, May 25, 2004. In a presentation on this issue, the then Director of the IRS's Exempt Organizations Division indicated "[w]hen it comes to political activities, that is, giving money to a candidate, telling people to vote for a certain candidate, the rule is that it has to be less than primary. If it's 49 percent of their income, that is less than primary." Marcus Owens, *Practicing Law Institute Program on Corporate Political Activities*, 3 EXEMPT ORG. TAX REV. 471 (June 1990).

<sup>13</sup> *Christian Echoes Nat'l Ministry v. United States*, 470 F.2d 849, 855-56 (10th Cir. 1972); *Manning Assoc. v. Comm'r*, 93 T.C. 596, 610-11 (1989).

<sup>14</sup> Again, since c(4) organizations appear to be subject to more exacting oversight of potential "excess benefit" transactions than do § 527 groups, we believe it is preferable to encourage groups to obtain exemption under § 501(c)(4).

Further, we believe that clarity, predictability, and ease of administration are more important than achieving the most perfectly nuanced determinations. Given the political pressures that inevitably are brought to bear in this area, and the scarcity of IRS resources for nonprofit enforcement generally, a process that is as nearly mechanical as possible would be preferable to one that calls for complex (and inevitably somewhat subjective) balancing. Though (as we will explain) we do not see constitutional objections to the current or proposed regime, we also note that a more mechanical process is less subject to the criticism that it is unconstitutionally vague.

Thus, the Final Rule should adopt a bright-line test that is mainly based on the expenditures of an organization and its non-527 related entities. Though this is a very crude measure of an organization's activity and purpose, it is fairly easy to measure and quantify. Some questions will remain about what items should be included in the "numerator" as partisan, but the minimal consequences of any adverse determination should make the importance of these questions minor as well. We will return to these definitional issues, and additional steps the IRS can take to ease any possible burden of subjecting some organizations to regulation under § 527, shortly.

For example, the Final Rule could adopt an approach modeled on the safe harbor set out by Congress in § 501(h). Organizations could make expenditures up to a percentage of their revenues, such as 10%. Since we see no reason why large organizations should be more secret or more influential than smaller ones, we would also suggest adopting an overall cap, as § 501(h) does. We would set that cap at a level rather lower than § 501(h)'s \$ 1million, however, in order to better implement Congress' intent that all expenditures of over \$500 be disclosed.

In the event the Treasury concludes that a § 501(h) model standing alone is insufficiently flexible, organizations that fail the expenditures test could also attempt to satisfy a “facts and circumstances” type of inquiry. But we recommend attaching conditions before the group can avail itself of that option.

Most importantly, the Final Rule should condition eligibility for facts & circumstances determinations on the organization’s waiver of § 6103 confidentiality in the audit processes and outcomes.<sup>15</sup> Complex examinations of political activity simply cannot succeed in secrecy. As recent experience suggests, public confidence in IRS evaluation of political activity is crucial both to the success of the Exempt Organizations unit and the Service overall. Voters are rightly concerned about the possibility of subjectivity creeping into complex balancing tests. Disclosure of all audit materials (except perhaps those related to confidential donor information, trade secrets, or the like), IRS deliberations, and final outcomes would greatly alleviate these fears. Further, in the past many organizations under investigation have opportunistically relied on confidentiality to claim selective prosecution, undermining meaningful enforcement efforts.

It might be argued that a test based primarily on expenditures unfairly favors groups that can rely on volunteer efforts, but we think excluding volunteer time can be justified based on congressional intent and good policy. For one, as we have argued, the central problem confronting the c(4) regime is that groups are using the c(4) form to evade the disclosure provisions in § 527(j) and FECA. Those provisions relate only to the disclosure of contributions and expenditures of cash or property. Congress chose not to require disclosures of campaign-

---

<sup>15</sup> In our view such a requirement would not contravene § 6103. Since the organization under examination is not compelled to waive, and since (given the availability of §527) there is no dollar impact of refusing the facts & circumstances review, we think it is at least a reasonable interpretation of § 6103 to hold that disclosure in such circumstances is not “making known in any manner whatever...return information.” I.R.C. § 6103(b)(8); *cf.* Donald Tobin, *Campaign Disclosure and Tax-Exempt Entities: A Quick Repair to the Regulatory Plumbing*, 10 ELECTION L.J. 427, 441-42 (2011) (arguing that voluntary disclosure by taxpayer in exchange for additional benefits from government does not violate §6103).

related volunteer time, and it would be at best odd for an anti-abuse regime to require more disclosure than the underlying law it is aimed at shoring up.

Furthermore, the line Congress drew was a sensible one. Accounting for all volunteers would be cumbersome. Volunteerism also tracks genuine intensity of human commitment far more closely than does money. While expenditures also allow voters to signal the strength of their beliefs, the meaningfulness of that signal is clouded by the diminishing marginal utility of money. A one-million dollar expenditure by a multi-national corporation---representing an average cost of a few pennies for each of its shareholders---is not remotely comparable, in terms of genuine “utility” cost, to the same total expenditure by hundreds of middle-class families. If disclosure is intended to accomplish anything, it is to allow the voting public to recognize when some interests are wielding money to acquire influence that far exceeds their relative welfare gains. Moreover, volunteering is “republican”; it creates opportunities for real human interactions, conversations, and debate in a way that a one-directional bombardment of paid political advertising does not. Finally, to the extent that subsidies are relevant, tax subsidies magnify the impact of money, but not of volunteers.

Having said that, when money is required to build and maintain volunteer networks, that money should be disclosed. Donations of phone or e-mail lists should be valued at their real cost or the price they could command from for-profit ventures. Although our focus here is not on § 501(c)(3) organizations, the Treasury may also wish to consider whether, when such lists are donated by § 501(c)(3) organizations or shared by them with non-charitable subsidiaries, they should be treated the same as contributions of cash by such firms.

## **We Agree With the Proposed Broad Definition of Electioneering**

Turning, then, to the question of which kinds of activities would count against any expenditure limit, we generally agree with the Proposed Rule's broad approach, although we think it could be broader still. Including "quasi-political" activity as campaign related is important if we seek a regulation that recognizes political realities. Over and over again, the types of activities referenced by the Notice have been used by groups as integral parts of groups' strategies to influence elections, while at the same time, arguing the activity is not political. In fact, social welfare organizations rarely engage in these activities in a nonpartisan manner. If the social welfare organization was engaged in a substantial amount of nonpartisan activities listed in the regulation, the organization would organize as a § 501(c)(3) organization and receive the more favorable tax treatment. The Notice tackles the problem of quasi-political activity by recognizing political reality and classifying this activity as campaign related political activity.

For example, social welfare groups have held political events designed to motivate "base" supporters, and invited political candidates to rallies and claimed that activities were social welfare educational activities.<sup>16</sup> Groups have also engaged in get-out-the-vote activities designed to defeat a particular candidate, and distributed literature on behalf of a candidate while claiming the activity was not political.<sup>17</sup> These quasi-campaign related activities are very difficult to police and are often political activities masquerading as social welfare or educational activities. The bright-line test in the proposed regulations makes clear that these quasi-campaign activities are treated as campaign related for the purposes of determining whether an organization's primary purpose is social welfare.

---

<sup>16</sup> *E.g.*, Joe Hallett, *It'll Be a Long Campaign for Ohio's Fact-Checkers*, COLUMBUS DISPATCH, June 9, 2013.

<sup>17</sup> Nicholas Confessore & Michael Luo, *Groups Targeted by I.R.S. Tested Rules on Politics*, N.Y. TIMES, May 26, 2013, at A1 (Tetumpka Tea Party get-out-the-vote drive designed to defeat President Obama, and Ohio Liberty Coalition claimed the distribution of door hangers for Romney was not political).

Because social welfare organizations may engage in some level of candidate-related political activity, it is less troublesome that some of the advocacy may be advocacy that would traditionally not be considered intervention in a political campaign. These activities are simply part of the allowed activities of social welfare organizations that are not part of the organization's primary purpose. Since a social welfare organization is still allowed to engage in some of this activity, the fact that this activity is not considered intervention in a political campaign in the § 501(c)(3) context is not problematic. In passing § 501(c)(4) Congress used the term "exclusively" in the statute. The current regulations expand on that term, so a definition of candidate-related political activity that is restrictive is still consistent with congressional intent. In fact, even this definition is broader than the statutory language because it still allows some amount of activities that are not social welfare activities. To the extent organizations want to engage in significant non-partisan activities that are classified as candidate-related activities under the proposed regulations, the organizations can conduct such activities through a connected § 501(c)(3) or § 527 organization.

On this basis, we agree with the Notice's bright-line definition of candidate-related political activity, and would additionally urge the Treasury to treat most communications directed to the general public, and which mention the name of a candidate for office, as electioneering, regardless of when in an election cycle the communication occurs. Our experience is that all or nearly all such communications are in fact motivated by electoral politics. As most organizations know, mass-market advertising is an exceptionally inefficient way to convey lobbying information, because only a fraction of the "eyeballs" that advertisers must pay to reach are those who are known to be sympathetic to the lobbying endeavor. In contrast, electioneering communications outside the window close to an election can still work to

“frame” and “define” candidates for voters before they begin to pay close attention to the race, and are especially cost-effective given that political ad rates are much cheaper outside the 60-day window. We acknowledge that such a rule would risk sweeping in some small fraction of lobbying speech, but the downsides of that outcome are small. We emphasize again that there would be few meaningful consequences for organizations if their communications are treated as candidate-related; those expenditures would simply have to be made out of a related firm or segregated fund subject to § 527 disclosure rules. However, to the extent that effective lobbying may sometimes require that activists be able to connect legislative outcomes with named individuals, and the IRS deems separate filing for such communications to be unduly burdensome, the Final Rule could permit a narrow exception for communications outside the near-election window that mention a candidate’s name only in connection with a specific vote on a specific piece of legislation.

### **An Anti-Abuse Rule to Prevent Cash Cycling Is Necessary and the Service’s Approach is Sensible**

The bright-line rule that the entire contribution will be considered campaign related unless the recipient certifies that it spends no money on campaign related activity is very strict, but it has the significant benefit of seriously limiting major abuse. A social welfare organization that legitimately wants to contribute to another social welfare organization that engaged in some campaign related activity could still make the donation. The only consequence under the proposed regulation is that the spending will not count as social welfare spending in determining an organization’s primary purpose.

## **Eligibility for Exemption Under § 527**

If the meaning of “primarily” in § 1.501(c)(4)-1(a)(2)(i) is interpreted as we propose, and no corresponding changes are made to the regulations under § 527, certain organizations may arguably be ineligible for exemption under any provision of the Code. Section 527(e)(1) limits the scope of 527 exemption to an “organization ... organized and operated primarily for the purpose of directly or indirectly accepting contributions or making expenditures, or both, for an exempt function.” Some lobbying organizations may engage in such “substantial” electioneering that they are ineligible under § 501(c)(4), but not so much that electioneering is their “primary” activity. Depending on how § 527(e)(1) is read, these groups might fail to qualify under either standard.

It is highly improbable that Congress could have intended such a result. In effect, groups that devote either most or only a small fraction of their resources to electioneering would be exempt, but not those that allocate an intermediate amount. Further, as we have suggested, Congress’ central goal in the 2000 amendments to § 527 was to allow for greater public scrutiny of groups engaged in partisan politics. There is no reason Congress would have wanted to exclude from the § 527 regulatory regime organizations that make “substantial” electioneering expenditures. Instead, Congress could plausibly have included the “primarily” language to exclude for-profit businesses from obtaining tax exemption.

It might be argued that this gap is a reason to reject our reading of the term “exclusively” in § 501(c)(4), but we think instead that the gap can easily be eliminated by interpreting § 527 to permit eligibility for groups with only “substantial” amounts of electioneering. For example, the Service could rule that exempt activities under another provision of section 501 would also be exempt under § 527. That is, § 501 exempt activities would not count in the “denominator” when assessing the share of the organization’s efforts devoted to “exempt function” activity

under § 527. In this way, groups that lobby in pursuit of the common good, as permitted under § 501(c)(4), but that engage in too much electioneering to be eligible under that section would still qualify under § 527.

The IRS can further mitigate any administrative burdens of the § 527 regime by permitting joint recognition of organizations as exempt under both § 501(c)(4) and § 527. For example, the Service could provide that an otherwise-qualifying § 501(c)(4) organization can retain that status so long as any disqualifying candidate-related expenditures are incurred through a segregated fund, and contributions to and expenditures by the fund comply with § 527. That is, the organization would not need to separately incorporate an affiliated firm, and could comply with both § 501(c)(4) and § 527 simply through accounting fully and publicly for the source of candidate-related expenditures.

In addition, the IRS should clarify, through regulation, that the provisions in §527 apply to all organizations that have as their primary purpose influencing elections. The statute is written in a way that makes § 527 status mandatory for all entities that are primarily engaged in influencing elections.<sup>18</sup> If §527 treatment is mandatory, then an organization could not escape § 527's disclosure provisions merely by claiming, for example, to be a taxable organization.

### **The Final Rule Should Also Cover Other Tax-Exempt Organizations**

The Notice invites comment regarding whether the Final Rule should apply to other tax-exempt organizations. The history in this area is very clear. If the final regulations do not apply similar requirements to all 501(c) organizations other than charities, organizations will simply reorganize under another provision of the Code. Organizations are already using § 501(c)(6)

---

<sup>18</sup> See *Nat'l Fed'n of Republican Assemblies v. United States*, 148 F. Supp. 2d 1273, 1282 (S.D. Ala. 2001); *Nat'l Fed'n of Republican Assemblies v. United States*, 218 F. Supp. 2d 1300, 1308 n.7 (S.D. Ala. 2002); Rev. Rul. 2003-49 Answer 20 (indicating that an organization is subject to § 527 if it meets the definition of political organization in § 527(e)).

business leagues and § 501(c)(19) veterans organizations as a means of engaging in campaign related activity, and § 501(c) contains numerous opportunities for organizations that could be used as an end run around these regulations. Allowing any of these avenues to remain open would frustrate Congress's disclosure goals.

We think that the absence of language specifically limiting political activity in many of these sections is not an obstacle to applying the Final Rule to them. As courts and the Treasury have recognized, §§ 501(c)(5), (6), and (7) impliedly limit the activities of eligible organizations to those implicitly contemplated by the statute.<sup>19</sup> Further, §527(f) applies a surtax on electioneering expenditures to all 501(c) organizations, suggesting that Congress contemplated that the §527 regime would work together with all of the provisions of § 501(c). At a minimum, then, we believe it would not be unreasonable for Treasury to interpret §527(j) also to extend to c(5), (6), and (7), as we have argued it does for §501(c)(4).

### **Extending the Final Rule to § 501(c)(3) Organizations Presents Special Considerations**

While we recognize that § 501(c)(3) presents special considerations we have not closely considered here, we believe that extending the reach of the Final Rule to § 501(c)(3) has some distinctive advantages. For one, the public, government, and practitioners would all be better served if political activity rules moved towards simplification rather than proliferation. For another, the lesson of history again is that leaving one organizational form outside the disclosure regime will only shift campaign spending towards those firms. The Final Rule should not generate new incentives to use c(3) organizations for electioneering purposes.

Admittedly, however, both the Proposed Rule and our comments here presume that the definition of campaign activity can be broadened because the organizational consequences of

---

<sup>19</sup> See I.R.S. Gen. Couns. Mem. 34,233 (Dec. 3, 1969); Aprill, 10 Election L.J. at 381-82.

excessive electioneering are minor. That presumption may not hold for charitable organizations, which under current law are putatively forbidden from engaging in any campaign activities. And the loss of eligibility for deductible contributions (along with any affiliated state tax advantages) would be a major blow to many firms.

Accordingly, we believe that further study and public comment are necessary before extending the definitions proposed in the Notice to § 501(c)(3) organizations.

### **Treasury Should Consider Issuing Complementary Rules that Would Also Apply to Some For-Profit Firms**

Organizations have consistently sought organizational forms that allow them to engage in anonymous campaign advocacy. Clarification of the rules surrounding tax-exempt organizations and campaign advocacy may encourage organizations to seek out alternative entity classifications as a means of avoiding restrictions created by the new regulations. Absent further clarification of the tax treatment of taxable entities involved in campaigns, there is significant risk that organizations will forgo tax-exempt status and instead organize as taxable organizations. At the moment, it is not clear what the tax ramifications would be to a taxable organization involved in campaign advocacy. Without further clarification by the IRS, taxable organizations may be the next vehicle of choice to avoid campaign finance disclosure, and may once again embroil the IRS in unnecessary political decisions.<sup>20</sup>

Although any taxable campaign organization would be subject to tax, the amount of taxable income for an organization might be small. Section 162(e) prohibits an organization from deducting political expenditures as an ordinary and necessary business expense, so presumably a taxable organization would have some tax liability if its primary purpose was

---

<sup>20</sup> It is outside the scope of this article to discuss all the difficult questions raised by the use of taxable entities for political campaign advocacy. For a more thorough discussion of this issue pre-*Citizens United* see Donald Tobin, *Political Advocacy and Taxable Entities, Are They the Next "Loophole"?*, 6 FIRST AMEND. L. REV. 41 (2007). *Post-Citizens United*, taxable corporations are an even more attractive vehicle for campaign advocacy.

campaign related because it could not deduct campaign related expenditures. However, if the organization had little to no income, there would be nothing to tax. Thus, if contributions to the taxable organization were not considered income, then there would be very little tax consequences to using a taxable form as a campaign vehicle.

The IRS rulings in this area are very old, and are ambiguous regarding whether contributions to a taxable campaign organization would be income. The IRS should clarify that contributions to taxable organizations for campaign advocacy are income to the corporation and subject to tax. Alternatively, the IRS should conclude that contributions are gifts and thus subject to gift tax. It should also clarify that taxable entities cannot circumvent this treatment by claiming that payments to the taxable entity are contributions to capital.

In addition, the IRS should clarify, through regulation, that the provisions in §527 apply to all organizations that have as their primary purpose influencing elections. The statute is written in a way that makes §527 status mandatory for all entities that are primarily engaged in influencing elections. If §527 treatment is mandatory, then an organization could not escape §527's disclosure provisions merely by claiming to be a taxable organization.

### **The IRS Should Get Serious on Enforcement and Reporting**

Another omission in the Proposed Rule is that the regulations do not do enough to address the enforcement issues that surfaced as part of the current crisis. The Administration should set out clear and transparent guidance regarding when and how it will enforce the current rules governing tax-exempt organizations. In the past it appears the IRS has failed to enforce these rules because it feared entering the political fray, and there have been almost no court cases involving the enforcement of political restrictions on tax-exempt organizations. The regulations will have no effect if the IRS continues its practice of failing to enforce the requirements.

Regardless of whatever course the Final Rule follows, the IRS should ensure that government officials and the public can assess the true scope of political activities by nonprofit organizations. Due to easily-remedied failures in updating its reporting methods, IRS electronic databases for fiscal years after 2008 fail to include a line item for political expenditures by § 501(c)(4) organizations. Even more critically, in our individualized examination of the tax returns of both § 501(c)(3) and § 501(c)(4) organizations, we see again and again that even those organizations reported publicly to have engaged in extensive lobbying and partisan activity declare little if any such activity on their tax returns. In many cases it appears that organizations take the position that they do not need to report expenditures as lobbying or electioneering-related to the extent that the activities in question could plausibly (or in some cases, in our view, implausibly) be defended as “educational.”

Just as individual taxpayers must disclose uncertain legal positions, nonprofit organizations should be required to disclose the legal reasoning behind their reporting position. Given that the border between lobbying communications and those that merely “educate” the public is rarely self-evident, organizations should at a minimum be asked to disclose the total cost of all their public communications.

### **There Are No First Amendment Concerns With the Proposed Rule**

Finally, we wish to respond to other commenters who have argued that IRS regulation of political activity infringes on their First Amendment rights. As the Supreme Court has held, § 501’s political limitations do not burden free speech, at least in the case in which organizations have alternative opportunities for exercising their political views. Both the Proposed Rule and other suggestions here would leave groups free to engage in electioneering through an affiliated § 527 organization.

*Citizens United* and other recent decisions do not undermine that rule, and indeed arguably strengthen it. It is true that the *Citizens United* Court held that the administrative difficulties of establishing a separate PAC could constitute a burden on the free speech rights of corporate shareholders. We agree with Professors Aprill and Galston that the 501/527 regime is distinguishable.<sup>21</sup> For example, once a group has already filed a Form 1023, and is regularly filing Form 990's, the added burden of also filing a §527 notice is modest, especially if the IRS simply permits the group to conduct candidate-related activities through a segregated fund.

More importantly, the government can assert compelling interests in regulating nonprofit political activity that were not available to it in *Citizens United*. First, as *Citizens United* recognizes, the government retains a compelling interest in revealing the sources of campaign spending. We argued earlier that the Notice is essential to the proper functioning of both §527(j) and FECA's disclosure regime more generally.

Next, the government has compelling interests in preserving the proper functioning of the non-profit sector its subsidies have helped to build and support. As discussed above, separating electioneering from other social welfare activities helps to preserve public support for the non-profit mission. Political limits also ensure that the § 170 matching grant does not distort the political process. While § 501(c)(4) organizations of course do not directly receive such subsidies, many c(4) organizations benefit from the resources, staff, and name recognition of an affiliated c(3).

Accordingly, we believe that the Constitution offers no reason for the Treasury to turn aside from policies that would best serve the non-profit sector and the nation as a whole.

\*\*\*

---

<sup>21</sup> Aprill, 10 Election L.J. at 398; Miriam Galston, *When Statutory Regimes Collide: Will Citizens United and Wisconsin Right to Life Make Federal Tax Regulation of Campaign Activity Unconstitutional?*, 13 U. PA. J. CONST. L. 867, 907-11 (2011).

We thank the Service for taking the time to review our comments. We welcome additional follow-up questions at [brian.galle@bc.edu](mailto:brian.galle@bc.edu) or [tobin.46@osu.edu](mailto:tobin.46@osu.edu)

Respectfully submitted,

/s/

**Brian Galle**  
Associate Professor, Boston College Law School

**Donald Tobin**  
John C. Elam/Vorys Sater Professor of Law,  
Ohio State University Moritz College of Law.

**Comments on Guidance for Tax-Exempt Social Welfare  
Organizations on Candidate-  
Related Political Activities**

**Submitted by:**

**Brian Galle  
Associate Professor  
Boston College Law School**

**Donald Tobin,  
John C. Elam/Vorys Sater Professor of Law,  
Ohio State University Moritz College of Law.**

**Feb. 22, 2014**

**SSRN Cover Sheet**

February 24, 2014

The Honorable John A. Koskinen  
Commissioner of Internal Revenue  
CC:PA:LPD:PR (REG-134417-13), Room 5205  
Internal Revenue Service  
1111 Constitution Avenue NW  
Washington, DC 20224

**Re: Comments on Guidance for Tax-Exempt Social Welfare Organizations on Candidate-Related Political Activities, 78 Fed. Reg. 71,535 (proposed Nov. 29, 2013) (to be codified at 26 C.F.R. pt. 1)**

**Submitted By:**

**Brian Galle, Associate Professor, Boston College Law School; and  
Donald Tobin, John C. Elam/Vorys Sater Professor of Law, Ohio State University Moritz  
College of Law.**

Dear Commissioner Koskinen:

We respectfully submit these comments in response to the Notice of Proposed Rulemaking (the “Notice”) issued by the Internal Revenue Service (the “IRS” or “Service”) and the Treasury Department on November 29, 2013. :

### **Executive Summary**

The Notice is a good first step. It creates bright-line standards that are easy to apply and that will eliminate much of the gray area regarding permissible political activity. Clearer lines will reduce the discretion on the part of the IRS. By decreasing the IRS’s discretion, the regulation will reduce the opportunity for the IRS to be used as a political tool in an Administration’s tool box.

However, the Notice does not go far enough. Congress has established a regulatory regime that has as its central purpose the disclosure of any significant campaign contributions by individuals or firms. In recent years many organizations have exploited the confidentiality rules of § 501(c)(4) to evade that regime, to the detriment not only of U.S. political discourse but also

the non-profit sector. The Final Rule should ensure that groups with significant partisan political activity cannot obtain exemption under § 501(c)(4), or indeed under any parallel provision of § 501.

We believe, however, that groups carrying out “substantial” electioneering activities should generally be eligible for exemption under § 527, and that the IRS should make that clear in the Final Rule. The main consequence of any ruling denying § 501(c)(4) status based on the political activity of the organization, therefore, would simply be to require the disclosure of an organization’s donors, and to ensure that the organization’s political expenditures are disclosed contemporaneously with the election they seek to influence.

Accordingly, the Final Rule should be designed in a way that channels organizations with any substantial amount of undisclosed electioneering activity into § 527. For example, we propose a strong presumption that any group with candidate-related political activity of more than 10% of its budget, or of more than an overall cap of some amount, such as \$1 million, whichever is lesser, should be recognized as a § 527 political organization and not as a § 501(c)(4) social welfare organization. The final rule should interpret “electioneering” broadly to include facially non-partisan activities that can be used to partisan advantage, including candidate-related advertising that falls outside the window immediately surrounding an election. Groups that voluntarily disclose their donors could retain c(4) status.

Additionally, we suggest that the IRS seriously consider developing rules to limit the use of for-profit entities to evade § 527. We urge the IRS to take a clearer stand on its enforcement plans and legally dubious Forms 990. And we argue that nothing in the Notice, or in what we additionally suggest here, would raise serious First Amendment concerns.