

Parting the Dark Money Sea: Exposing Politically Active Tax-Exempt Groups Through FEC-IRS Hybrid Enforcement

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PARTING THE DARK MONEY SEA: EXPOSING POLITICALLY
ACTIVE TAX-EXEMPT GROUPS THROUGH FEC-IRS HYBRID
ENFORCEMENT

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INTRODUCTION

The Internal Revenue Service (IRS) grants tax exemptions to non-profit entities organized under § 501(c)(4), and in exchange, restricts these groups to a “social welfare” purpose.¹ Such a restriction limits how much political activity § 501(c)(4) organizations can fund.² Engaging in political action necessarily involves the Federal Election Commission (FEC), the Agency founded to enforce the federal election laws (campaign finance restrictions in particular),³ and so there is an unavoidable intersection of tax law and election law when these tax-exempt groups participate in partisan activity. This Note aims to improve the system designed to regulate this overlapping area of the law by pooling the respective powers of the IRS and the FEC. The collaborative framework proposed herein presents an opportunity for an enhanced regulatory landscape, in which the two Agencies work better together than either can alone.

Consider the following examples of the murky campaign finance world, where funding sources are obscured and the true messages of campaigns are confused. In the 2010 election, the § 501(c)(4) organization Commission on Hope, Growth, and Opportunity ran a series of television advertisements with cartoon depictions of prominent Democrats, including President Obama and Representative Nancy Pelosi, dancing in a conga line and “living it up” in Washington.⁴ The ads called on viewers to “join” the Republicans, whom the Commission presumably viewed as more viable candidates.⁵ This message likely appeared partisan for many viewers—a call to action for Republican voters—but the Commission did not register as a political committee or report any political spending to the FEC. The group also declared no political spending to the IRS, despite listing

1. I.R.C. § 501(c)(4) (2014); see *infra* Part I for a description of the statutory scheme that applies to politically active exempt groups.

2. See *infra* Part I.A.

3. See *The FEC and the Federal Campaign Finance Law*, FEC, <http://www.fec.gov/pages/brochures/fecfeca.shtml> [<http://perma.cc/Z9SQ-QUBP>] (last updated Jan. 2015).

4. Kim Barker, *How Nonprofits Spend Millions on Elections and Call it Public Welfare*, PROPUBLICA (Aug. 18, 2012, 11:25 PM), <http://www.propublica.org/article/how-nonprofits-spend-millions-on-elections-and-call-it-public-welfare> [<http://perma.cc/V9QB-3FGU>].

5. See *id.*

on its tax return that *96 percent* of its total expenditures (\$4.6 million) were on advertisements like the one described.⁶

In the 2014 North Carolina Senate race, the Iowa-based § 501(c)(4) American Future Fund (AFF) launched a series of online advertisements endorsing libertarian candidate Sean Haugh and praising him for supporting marijuana legalization.⁷ AFF did report the expenditures to the FEC,⁸ but more significant here is the confusion such an advertisement creates. AFF actually supported Republican candidate Thom Tillis, but the point of the ad was to portray Haugh as the best choice for “progressive values”—a preferable alternative, then, to Democrat incumbent Kay Hagan. The ads also provided a new slogan for Haugh—“More weed, less war”—which his campaign did not approve.⁹ To the average North Carolina voter, it may have appeared that Haugh, or a group supporting Haugh, paid for or approved of the advertising. The true story, however, reveals that without stricter guidelines, independent political spending can and does skew campaign messaging.

Various proposed means of campaign finance reform, such as broader disclosure requirements¹⁰ and more nuanced contribution restrictions,¹¹ may, in the long term, correct the problems illustrated

6. See *id.* The Commission, similar to the Republican Jewish Coalition, see *infra* notes 146-52 and accompanying text, reported no intent to engage in political activity on its application for exempt status but then spent nearly all of its funds on campaign intervention. John Spratt, former Chairman of the House Budget Committee, said of his defeat, “I still don’t know who they are It’s a classic case [of a secret organization].” Jonathan Weisman, *Tax-Exempt Group’s Election Activity Highlights Limits of Campaign Finance Rules*, N.Y. TIMES (July 16, 2012), http://www.nytimes.com/2012/07/17/us/politics/hope-growth-and-opportunity-shows-limits-of-disclosure-rules.html?_r=0 [<http://perma.cc/T8HY-MCQB>].

7. Alex Roarty, *GOP Group Urges Young Voters to Support Weed Candidate*, NAT’L J. (Oct. 21, 2014), <http://www.nationaljournal.com/politics/koch-allied-group-urges-young-voters-to-support-weed-candidate-20141021> [<http://perma.cc/MKP9-LEJY>]. In a likely effort to target young, left-leaning voters, the AFF ran the ads on various online platforms, including video site Hulu. *Id.*

8. See *2014 Senate Independent Expenditures*, FEC, <http://fec.gov/disclosure/eie/national.do?candOffice=S> [<http://perma.cc/6DHU-GBM9>] (click map for “North Carolina” then search “Candidate Name” for “Haugh” then follow “Submit” hyperlink).

9. See Roarty, *supra* note 7.

10. See *infra* notes 137-45 and accompanying text.

11. See, e.g., Joel M. Gora, *Free Speech, Fair Elections, and Campaign Finance Laws: Can They Co-Exist?*, 56 HOW. L.J. 763, 784 (2013) (“[O]ne of the main reasons we are witnessing [these developments] is precisely because we have imposed limits on the ability of individuals and groups to contribute directly to candidates and parties.... It might be far better for accountability and transparency in our political system to think about raising or even

above. The grave lack of enforcement in this area, though, allows current abuses of both the tax and electoral systems to continue. Despite the Supreme Court's recent stripping away of campaign finance restrictions, this Note operates under the presumption that some regulation of tax-exempt organizations' political speech is constitutionally permissible under the First Amendment¹²—regulation which is indispensable to fulfilling Congress's wish for robust and fair elections.¹³ A more immediately powerful solution, and what this Note proposes, is to ramp up enforcement by empowering both the IRS and the FEC to make internal changes and then cooperate to hold politically active social welfare organizations responsible when they violate the tax and election laws. Only if both Agencies work together will they be able to fulfill their respective obligations and prevent corruption and exploitation of the electoral and tax systems.

This Note proceeds in three parts. Part I compares and contrasts the tax code provisions that apply to politically active tax-exempt groups. It also traces the recent evolution of the Supreme Court's First Amendment election law jurisprudence. *Citizens United v.*

eliminating those contribution limits so that the funding would be back inside the tents of the parties and the candidates, and they would be responsible for its use.”)

12. See 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, 891 n.84, 893-94, 903-04 (2011) (“[A] failure to subsidize does not, in and of itself, constitute a burden and does not infringe the [First Amendment] right.... [In addition,] economic hardship resulting from a denial of government benefits does not necessarily implicate the Constitution, even when First Amendment protections are affected.”) (citations omitted). The Court has struck down laws that prohibit anonymous speech by requiring speaker disclosure. See, e.g., *Brown v. Socialist Workers’74 Campaign Comm.*, 459 U.S. 87, 101-02 (1982); *NAACP v. Alabama ex rel. Patterson*, 357 U.S. 449, 466 (1958). But these cases involved protecting speakers from threats and harassment, which may justify an exception from a disclosure regime. See *Brown*, 459 U.S. at 101-02; *NAACP*, 357 U.S. at 462-63; see also *Citizens United v. FEC*, 558 U.S. 310, 370 (2010) (remarking that political speech regulations, such as disclosure requirements, “would be unconstitutional as applied” to organizations only if “there were a reasonable probability that the group’s members would face threats, harassment, or reprisals”) (citing *McConnell v. FEC*, 540 U.S. 93, 198 (2003)); *Buckley v. Valeo*, 424 U.S. 1, 74 (1976). More recently, the Court recognized that “[r]equiring people to stand up in public for their political acts fosters civic courage, without which democracy is doomed.” *Doe v. Reed*, 561 U.S. 186, 228 (2010) (Scalia, J., concurring); see also *Citizens United*, 558 U.S. at 367.

13. See Federal Election Campaign Act (FECA) of 1971, Pub. L. No. 92-225, 86 Stat. 3 (1972) (prior to amendments) (“AN ACT[:] To promote fair practices in the conduct of election campaigns for Federal political offices.”).

FEC is the hallmark case, but other doctrinal decisions have also added to the enormous influx of undisclosed independent spending, referred to as “dark money.” Part II explains how social welfare organizations have been pushed to the forefront of the campaign finance debate and addresses weaknesses in the tax code that allow for abuse. Because political activity that § 501(c)(4) groups engage in is treated more leniently than that which § 527 groups engage in, § 501(c)(4)s have become an ideal, and indeed preferred, mouthpiece for wealthy donors with special interests.

Part III proposes a way forward: administrative alterations that can facilitate effective enforcement of current regulations. Providing for stricter enforcement by enabling the FEC and IRS to work together would cut through some of the debilitating FEC gridlock and truly empower the IRS to hold organizations responsible for abusing the tax code. There is no stopping money from entering politics, but rigorous enforcement can help control its effects in future elections.

I. TAX LAW AND ELECTION LAW FOUNDATIONS

Incorporated entities face graduated tax rates under the current regime, ranging from 15 percent to 35 percent depending on annual income.¹⁴ In order to encourage certain social-minded activities, though, Congress has exempted from the corporate tax scheme organizations that make no profit and exist for the public good.¹⁵ With some exceptions, § 501 of the Internal Revenue Code (I.R.C.) captures the full range of exempted conduct, which includes charitable pursuits like churches and schools,¹⁶ as well as labor unions,¹⁷ trade associations,¹⁸ and social welfare groups.¹⁹ This Note focuses on activity by social welfare groups, § 501(c)(4) organizations, because they have become the corporate form of choice for entities wishing to participate in political speech.²⁰ This Part first describes the incongruent provisions that apply to politically active tax-exempt

14. I.R.C. § 11(b)(1) (2014).

15. *See, e.g., id.* §§ 501(c), 527.

16. *Id.* § 501(c)(3).

17. *Id.* § 501(c)(5).

18. *Id.* § 501(c)(6).

19. *Id.* § 501(c)(4).

20. *See infra* Part II.

entities and then traces recent election law developments in this area.

A. Internal Revenue Code Provisions

A basic understanding of the differing rules that apply to tax-exempt entities helps reveal why § 501(c)(4) organizations have become “the keys to the political kingdom.”²¹ The I.R.C. includes a separate, express provision, § 527, for organizations that engage in partisan political activity.²² Despite Congress’s intention that political groups organize themselves under § 527,²³ § 501(c)(4) groups have become the political speech vehicle of choice.²⁴ Most importantly, although entities organized under both sections engage in “political activity,” § 527 political groups and § 501(c)(4) social welfare groups are held to drastically different definitions and standards.²⁵

1. Section 501(c)(4) Social Welfare Organizations

Section 501(c)(4) groups get their moniker directly from the text of the I.R.C., which states that these organizations should be “operated *exclusively* for the promotion of social welfare ... the net earnings of which are devoted *exclusively* to [these] purposes.”²⁶ Social welfare groups are designed to be issue advocacy groups focused on a particular policy area, and are permitted to conduct unlimited lobbying efforts in support of their public-minded missions. Increasingly, though, these organizations have become involved in elections, participating in partisan political activity, which does not honor their exempt purpose.²⁷

21. Douglas Oosterhouse, Note, *Campaign Finance Reform and Disclosure: Stepping-Up IRS Enforcement as a Remedial Measure to Partisan Deadlock in Congress and the FEC*, 65 RUTGERS L. REV. 261, 263 (2012).

22. I.R.C. § 527.

23. See *infra* note 79.

24. See *supra* notes 4-9 and accompanying text; *infra* Part II.

25. The IRS has considered issuing a unified definition of “political activity” but has yet to act. See Hillary Flynn & Rachael Bade, *IRS May Broaden Rule to Police Political Nonprofits*, POLITICO (Mar. 18, 2015, 8:20 PM), <http://www.politico.com/story/2015/03/irs-may-broaden-rule-to-police-political-nonprofits-116206.html> [<http://perma.cc/LGP7-D2RH>].

26. I.R.C. § 501(c)(4)(A) (emphasis added).

27. See *infra* Part II.A for deeper discussion of this issue.

Social welfare groups face few functional and procedural requirements. Unlike some tax-exempt organizations, § 501(c)(4)s do not have to notify the IRS of their formation, nor are they required to apply for exempt status.²⁸ There is but one filing requirement: social welfare organizations must provide an informational tax return (Form 990) to the IRS, which lists some donor information and expenditures, as well as donations to other tax-exempt groups.²⁹

Of course, even this requirement is not without a loophole. The Form 990 is due by the fifth month following the end of the tax year, so depending on their date of formation, social welfare groups may take advantage of an eighteen-month delay in filing.³⁰ Augmenting this already prolonged interval, organizations can request extensions, pushing the filing deadline past twenty-two months after formation.³¹ Because these groups are not required to file anything when they organize, the IRS may not even know a tax-exempt social welfare organization exists until twenty-two months after it forms, and by then, it may have disbanded. As discussed in Part III, this lax reporting structure is problematic when accounting for political spending, particularly because the IRS is tasked with enforcing already vague restrictions.

The IRS also requires little public disclosure from social welfare organizations.³² Although each Form 990 is made publicly available, either posted online or issued by request, the organization may redact the donor list it contains before public release.³³ As discussed below, organizing under § 527 as a political organization results in a very different regulatory scheme—even when participating in the same political activity that § 501(c)(4) groups engage in.

28. See Oosterhouse, *supra* note 21, at 266-68; Donald B. Tobin, *FAQs on 501(c)(4) Social Welfare Organizations*, THE OHIO STATE UNIV. MORITZ COLL. OF LAW (May 20, 2013), [http://moritzlaw.osu.edu/electionlaw/analysis/documents/FAQs%20on%20501\(c\)\(4\)%20Social%20Welfare%20Organizations%20v.6.pdf](http://moritzlaw.osu.edu/electionlaw/analysis/documents/FAQs%20on%20501(c)(4)%20Social%20Welfare%20Organizations%20v.6.pdf) [<http://perma.cc/FY3N-C6VS>]. Compare I.R.C. § 501(c)(4), with I.R.C. § 501(c)(3), and I.R.C. § 527.

29. See Oosterhouse, *supra* note 21, at 266-68; Tobin, *supra* note 28.

30. See Oosterhouse, *supra* note 21, at 268; Tobin, *supra* note 28.

31. See Tobin, *supra* note 28.

32. Many reformers consider disclosure to be the one remaining constitutional campaign finance regulation. For a full discussion of this topic, see *infra* Part II.B.

33. See Tobin, *supra* note 28. See generally *supra* note 12.

2. Section 527 Political Organizations

Congress also provided a tax exemption in the I.R.C. for bodies that are organized specifically for political involvement.³⁴ These groups, exempt under § 527, can engage in unlimited political activity but, as a result, are very limited in other activities.³⁵ This tax classification includes all types of political committees: candidate and party committees, traditional Political Action Committees (PACs), leadership PACs (those tied to a particular candidate or elected official), and Super PACs (those that coordinate with other PACs).³⁶

Although both § 501(c)(4)s and § 527s engage in political activity, the IRS requirements imposed on § 527 groups are much stricter and more comprehensive than those that apply to § 501(c)(4) organizations. Political entities must essentially “account for every dollar in and every dollar out”³⁷ through detailed and frequent disclosure reports.³⁸ Unless required to register as a political committee with the FEC,³⁹ § 527 groups must report to the IRS all expenditures made over \$500 and all contributions received over \$200.⁴⁰ Regardless of which agency the § 527 entity files with, this financial information is publicly available online.⁴¹ In order to function legally, § 527 groups must also notify the IRS of their formation and operation.⁴² The full significance of these discrepancies is explored

34. See I.R.C. § 527 (2014).

35. See *id.*

36. See Oosterhouse, *supra* note 21, at 265-66.

37. Ciara Torres-Spelliscy, *Hiding Behind the Tax Code, the Dark Election of 2010 and Why Tax-Exempt Entities Should Be Subject to Robust Federal Campaign Finance Disclosure Laws*, 16 NEXUS: CHAP. J. L. & POL'Y 59, 73 (2011).

38. Oosterhouse, *supra* note 21, at 266.

39. See *FEC Filing Required for Some 527 Organizations*, IRS, <http://www.irs.gov/Charities-&-Non-Profits/Political-Organizations/FEC-Filing-Required-for-Some-527-Organizations> [<http://perma.cc/247N-CP93>] (last updated Feb. 4, 2014).

40. See *FAQs About the Annual Form Filing Requirements for Section 527 Organizations*, IRS, <http://www.irs.gov/Charities-&-Non-Profits/Political-Organizations/FAQs-about-the-Annual-Form-Filing-Requirements-for-Section-527-Organizations> [<http://perma.cc/JQY9-7TX5>] (last updated June 10, 2015) (follow “Periodic Reports of Contributions and Expenditures” then follow “Contents of Report” hyperlink).

41. Torres-Spelliscy, *supra* note 37, at 73, 82.

42. *Form 8871 Initial Notice*, IRS, <http://www.irs.gov/Charities-&-Non-Profits/Political-Organizations/Initial-Notice-Form-8871> [<http://perma.cc/QP2N-WNYA>] (last updated July 21, 2015).

in Part II.B. Importantly, although § 501(c)(4) organizations are still free to engage in political activity by establishing and acting through an affiliated § 527 group,⁴³ they were, until recently, required to do so.⁴⁴

B. Campaign Finance Doctrinal Framework

The complications detailed in this Note are typically traced to *Citizens United v. FEC*, but other cases have also contributed. Although *Citizens United* did have a profound impact on subsequent elections,⁴⁵ the influence of the decisions discussed here should not be understated. They demonstrate the Court's evolving First Amendment election law jurisprudence and, as a practical matter, have resulted in social welfare groups' expanded bank accounts. The foundational campaign finance regulations, and the cases that dismantled them, are detailed below.

1. Statutory Basis and Underlying Values

In 1972, Congress passed the first comprehensive campaign finance law, which provided limits on different types of political spending.⁴⁶ After the rise of "soft money"—funds not subject to these limits contributed to and spent by political parties in federal elections—Congress amended the law with the 2002 Bipartisan Campaign Reform Act (BCRA), which attempted to control the flow of soft money and the increasing influence of issue ads.⁴⁷ Some of BCRA's provisions have now been repealed,⁴⁸ but certain restrictions and disclosure provisions remain vital campaign finance regulations.

43. See Oosterhouse, *supra* note 21, at 268.

44. See *Citizens United v. FEC*, 558 U.S. 310, 336-40 (2010) ("[T]he option to form PACs does not alleviate the First Amendment problems.").

45. See *infra* Part II.B.1.

46. Federal Election Campaign Act (FECA) of 1971, Pub. L. No. 92-225, 86 Stat. 3 (codified as amended at 52 U.S.C. §§ 30101-30126 (2002)).

47. Bipartisan Campaign Reform Act (BCRA) of 2002, Pub. L. No. 107-155, 116 Stat. 81.

48. See *infra* Part I.B.2.

Traditionally, there are four recognized government interests that drive campaign finance restrictions.⁴⁹ The most compelling is the anti-corruption interest: the idea that money corrupts politics generally, and politicians in particular.⁵⁰ The other three are: the equality interest, that voters should enjoy equal access to candidates and elected officials, and that the majority of political donors are not representative of the voting public; the participation interest, that more money, especially if undisclosed, leads to lower voter turnout; and the information interest, that voters should have as much information as possible about the speakers behind political messages.⁵¹ As detailed below, the Court has discarded three of these interests; the anti-corruption rationale remains the one stronghold, though it has been narrowed in recent years.⁵² Each of these rationales, however, is crucial to maintaining a fair and honorable election system.

2. *Evolving Case Law*

The BCRA restrictions were first narrowed in the 2007 case *FEC v. Wisconsin Right to Life*, in which a § 501(c)(4) organization challenged the BCRA “blackout” provisions. BCRA prohibited corporate- and union-funded electioneering communications (including issue advocacy and express candidate advocacy) from running close in time to an election.⁵³ The Court invalidated the blackout periods as applied to the challenger’s issue advocacy.⁵⁴ Though a significant setback for BCRA supporters, the decision dealt an incomplete blow

49. Jocelyn Benson, *Saving Democracy: A Blueprint for Reform in the Post-Citizens United Era*, 40 *FORDHAM URB. L.J.* 723, 726 (2012).

50. *See id.* at 736-37.

51. *See id.* at 726, 730, 733.

52. *See generally* *Citizens United v. FEC*, 558 U.S. 310 (2010).

53. *FEC v. Wisconsin Right to Life, Inc.*, 551 U.S. 449, 458-60 (2007) [hereinafter *WRTL*]; *see also* Galston, *supra* note 12, at 883-84.

54. *WRTL*, 551 U.S. at 466-67 (citing *McConnell v. FEC*, 540 U.S. 93, 207 (2003), and its predecessor, *Buckley v. Valeo*, 424 U.S. 1, 42-43 (1976)); *see also* Galston, *supra* note 12, at 889-90. Notably, the facts-and-circumstances test now employed by the IRS is very similar to the FEC’s intent-and-effect test, which the Court rejected here. Although some scholars consider issue advocacy to be another form of campaign speech, the Court’s holding rejects the idea that political speech may be something other than express advocacy. *See* Galston, *supra* note 12, at 888-89.

because it upheld the facial constitutionality of the blackout provision for express advocacy.⁵⁵

Three years later, the Court again considered a challenge from a social welfare organization in a case that many consider defining of the Roberts Court.⁵⁶ Here, the § 501(c)(4) group Citizens United presented fairly narrow and specific questions about political speech distributed through cable Video-on-Demand services and the related advertising for that content.⁵⁷ The case took a turn, though, at oral argument, where the following exchange occurred:

Mr. Stewart (arguing for the government): [I]f you had Citizens United or General Motors using general treasury funds to publish a book that said at the outset, for instance, Hillary Clinton's election would be a disaster ... —

Chief Justice Roberts: Take my hypothetical. It doesn't say at the outset. It funds ... a discussion of the American political system, and at the end it says vote for X.

Mr. Stewart: Yes, our position would be that the corporation could be required to use PAC funds rather than general treasury funds.

Chief Justice Roberts: And if they didn't, you could ban it?

Mr. Stewart: If they didn't, we could prohibit the publication of the book using the corporate treasury funds.⁵⁸

After Deputy Solicitor General Malcolm Stewart all but declared the government could ban books,⁵⁹ the Court ordered reargument on a

55. *WRTL*, 551 U.S. at 477-81. Though not a total defeat, Congress originally composed BCRA to tackle the "twin loopholes" that § 527 organizations had previously enjoyed: the ability to raise soft money and to release sham issue advertising. Oosterhouse, *supra* note 21, at 274-75. The Court completely struck the provision intended to protect only bona fide issue advocacy, thus undermining one of Congress's goals.

56. See Galston, *supra* note 12, at 871 (referring to the case as a dramatic example of Roberts Court activism and explaining that "the majority [in *Citizens United*] overruled two earlier Supreme Court decisions, invalidated a federal law of long-standing, and, by implication, invalidated parallel state campaign finance provisions in at least 24 states"); see also Geoffrey R. Stone, *The First Amendment Doesn't Protect the Right to Buy the American Government*, DAILY BEAST (Apr. 5, 2014, 5:45 AM), <http://www.thedailybeast.com/articles/2014/04/05/the-first-amendment-doesn-t-protect-the-right-to-buy-the-american-government.html> [<http://perma.cc/J9B8-GVYT>].

57. See Brief for Appellant at i, *Citizens United*, 558 U.S. 310 (No. 08-205).

58. Transcript of Oral Argument at 30, *Citizens United*, 558 U.S. 310 (No. 08-205).

59. See *id.*; see also Gora, *supra* note 11, at 771.

broader question: whether prior election law decisions, including those that addressed the constitutionality of the BCRA provisions and which led to Stewart's bold statement, should be overturned.⁶⁰ The Court then struck down BCRA's ban on corporate-funded independent expenditures.⁶¹

Relying on *Citizens United* later that same year, the District of Columbia Circuit solidified "carte blanche"⁶² for unlimited donations to political groups in *SpeechNow.org v. FEC*.⁶³ The opinion protected disclosure requirements, as the Court had in *Citizens United*,⁶⁴ but banned the contribution caps for donations to independent-expenditure-only groups (those with no direct ties to a candidate).⁶⁵ Organizational power is often tied to the purse strings, so the *SpeechNow* decision is possibly the true culprit of the problems detailed herein, simply made possible by the holdings in *Wisconsin Right to Life* and *Citizens United*.⁶⁶

There is much dispute about the true significance of these cases, *Citizens United* in particular. Some believe the opinion undermines the First Amendment and democracy as a whole,⁶⁷ though this narrative has been described as "overly simplistic."⁶⁸ Others find no constitutional flaws but still fault the case's outcome for the shift of political capital to social welfare groups.⁶⁹ Taken together, these

60. See Order for Reargument, *Citizens United v. FEC*, 129 S. Ct. 2893 (2009). The Court specifically requested supplemental briefing by the parties about overruling *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990), and/or *McConnell v. FEC*, 540 U.S. 93 (2003). *Id.*

61. *Citizens United*, 558 U.S. at 365-67.

62. Leah McGrath Goodman, *As Dark Money Floods U.S. Elections, Regulators Turn a Blind Eye*, NEWSWEEK (Sept. 30, 2014, 11:03 AM), <http://www.newsweek.com/2014/10/10/dark-money-floods-us-elections-regulators-turn-blind-eye-273951.html> [<http://perma.cc/XDM5-R5V7>].

63. 599 F.3d 686, 692-96 (D.C. Cir. 2010).

64. 558 U.S. at 371.

65. *SpeechNow*, 599 F.3d at 692-98.

66. See Rick Hasen, *What Matt Bai's Missing in His Analysis of Whether Citizens United Is Responsible for the Big Money Explosion*, ELECTION L. BLOG (July 18, 2012, 10:41 AM), <http://electionlawblog.org/?p=37108> [<http://perma.cc/2L8U-AUAT>] [hereinafter *Big Money Explosion*].

67. See, e.g., Stone, *supra* note 56.

68. Matt Bai, *How Much Has Citizens United Changed the Political Game?*, N.Y. TIMES (July 17, 2012), http://www.nytimes.com/2012/07/22/magazine/how-much-has-citizens-united-changed-the-political-game.html?_r=0 [<http://perma.cc/BLV9-AQBF>].

69. See, e.g., Heather K. Gerken, *The Real Problem with Citizens United: Campaign Finance, Dark Money, and Shadow Parties*, 97 MARQ. L. REV. 903, 907-10 (2014); Richard L.

holdings boosted formation of and spending by social welfare organizations and Super PACs.⁷⁰ This Note explores evidence for these theories and provides a workable solution to such concerns.

Building on the less stringent reporting obligations social welfare groups face, the next Part reveals why many would prefer operating through a § 501(c)(4) organization, even when political intervention is a main focus. And because many social welfare organizations are not required to register with the FEC, what remains of the campaign finance laws has done little to regulate the troublesome behavior highlighted below.

II. ESCALATING POLITICAL ACTIVITY OF TAX-EXEMPT SOCIAL WELFARE ORGANIZATIONS: WHERE TAX LAW AND ELECTION LAW INTERSECT

The tax code is not generally regarded for its clarity, and this characteristic is regrettably no different when situated in the election law context. Exempt organizations operate on a type of spectrum with respect to political activity. Section 501(c)(3) represents one end, with an absolute ban on political activity, and § 527 is the other end, in which the only acceptable purpose is political activity.⁷¹ Regulating § 501(c)(4) groups is particularly challenging because they fill the middle of this spectrum⁷² and can act as

Hasen, *Three Wrong Progressive Approaches (and One Right One) to Campaign Finance Reform*, 8 HARV. L. & POL'Y REV. 21, 25-26 (2014) [hereinafter Hasen, *Progressive Approaches*]. Although Professor Gerken does not blame the case for opening the floodgates of corporate spending, because, she argues, most corporations avoided the bright-line “magic words” test with creative issue advocacy anyway, she remains very concerned with the Court’s redefinition of corruption and the subsequent and enduring shift in political power, which has transformed social welfare organizations into “shadow parties.” Gerken, *supra*, at 907-10. Professor Hasen has also written extensively on this topic and notably considers the initial supposition of the *Citizens United* opinion—that independent spending cannot corrupt the political process—entirely unfounded. Richard L. Hasen, *The Biggest Danger of Super PACs*, CNN (Jan. 9, 2012, 8:13 AM), <http://www.cnn.com/2012/01/09/opinion/hasen-super-pacs/index.html> [<http://perma.cc/56ZY-2HEV>] [hereinafter Hasen, *Danger*].

70. See Debra Erenberg & Matt Berg, *The Dark Night Rises: The Growing Role of Independent Expenditures in Judicial Elections After Citizens United*, 49 WILLAMETTE L. REV. 501, 507-12 (2013).

71. See I.R.C. §§ 501(c)(3), 527 (2014).

72. See *id.* § 501(c)(4).

conduits between both one another and § 527s.⁷³ Because of their unique position, effective enforcement against § 501(c)(4)s requires a nuanced mix of firmness and flexibility.

A. IRS Treatment of Political Activity

Regulation of political activity has been consistently problematic for the IRS.⁷⁴ The IRS's main purpose is revenue collection, so there is some institutional discomfort when tax classifications of nonprofit organizations force the Agency to stray into other areas of law.⁷⁵ This reluctance can result, as in the case of political involvement, in two very different and sometimes conflicting legal standards governing the activities of tax-exempt organizations.⁷⁶ It is clear that § 501(c)(4) organizations are not always sham § 527 groups. It is not clear, however, where the IRS draws the line that distinguishes the two and delineates which activities, or how much of them, are permissible.

1. Conflicting Threshold Standards

According to the I.R.C., § 501(c)(4) entities are to be organized “exclusively” for the promotion of social welfare and specifically not for the benefit of private individuals.⁷⁷ Historic authority suggests that there should be limits on partisan activities by § 501(c)(4) organizations, in part because partisan interests are not shared by the public as a whole, and so partisan activity cuts against the specified

73. This arrangement requires strict accounting to ensure that funds are properly disbursed, but it is by no means unusual. See *infra* Part II.B.3 for specific examples of this problem.

74. Roger Colinvaux, *Political Activity Limits and Tax Exemption: A Gordian's Knot*, 34 VA. TAX REV. 1, 3-4 (2014).

75. See Torres-Spelliscy, *supra* note 37, at 78. The IRS has no institutional interest in the integrity of elections. *Id.* Whether the IRS should have such an interest, given the implications tax status has for political regulation, is beyond the scope of this Note.

76. Galston, *supra* note 12, at 867; see also Colinvaux, *supra* note 74, at 3-4; *infra* Part II.A.

77. I.R.C. § 501(c)(4) (explaining that an entity may not organize under § 501(c)(4) “unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual”).

purpose of *social welfare* organizations.⁷⁸ From the very beginning, Congress defined these groups specifically as nonpartisan entities, in contrast with § 527 organizations, which are formed solely for political involvement.⁷⁹

In 1981, the IRS issued a Revenue Ruling that established that a § 501(c)(4) group is within its exempt purpose if it is organized “primarily” for the social welfare, despite the use of “exclusively” *twice* in the I.R.C.⁸⁰ Perhaps displaying its unwillingness to exert control in a non-tax area, the IRS provided no specific threshold on other activities that would push a § 501(c)(4) entity away from its “exclusive,” or even “primary,” purpose as a social welfare organization. Although this omission contributes to the confusion surrounding political involvement of tax-exempt groups today, it was largely insignificant at the time, because candidates and parties spearheaded political activity, and independent expenditures were only just appearing.⁸¹

Because the IRS has failed to provide an enforceable rule regarding what it means for something to be an organization’s “primary” activity, social welfare groups have been driven to decide their own limits, opportunistically drawing the line as close to a 50/50 threshold as possible.⁸² Though internal rules developed in 1987 provide some guidance, the IRS has been publicly silent on whether such a standard is appropriate.⁸³ Even at a low threshold, these groups are

78. See Terence Dougherty, *Section 501(c)(4) Advocacy Organizations: Political Candidate-Related and Other Partisan Activities in Furtherance of the Social Welfare*, 36 SEATTLE U. L. REV. 1337, 1342 (2013).

79. See S. Rep. No. 93-1357, at 30 (1974), *reprinted in* 1974 U.S.C.C.A.N. 7478, 7506 (“The committee expects that, generally, a section 501(c) organization that is permitted to engage in political activities would establish a separate organization that would operate primarily as a political organization In this way, the campaign-type activities would be taken entirely out of the section 501(c) organization, to the benefit both of the organization and the administration of the tax laws.”).

80. Rev. Rul. 81-95, 1981-1 C.B. 332.

81. See Gerken, *supra* note 69, at 906. Professor Gerken describes the 1976 case *Buckley v. Valeo* as “the snake in [the] garden of campaign-finance Eden,” marking a shift in expenditure regulation and an increase in non-candidate activity. *Id.*

82. See Dougherty, *supra* note 78, at 1339.

83. Rosenberg’s Rules of Order, which lists numerical percentages with corresponding quantifiable terms like “exclusively,” “primarily,” “substantially,” “de minimis,” and so on, were publicly released in 2013. See *Rosenberg’s Rules*, [www.taxanalysts.com/www/freefiles.nsf/Files/EO%20Measurement%20Term%20Definitions.pdf/\\$file/EO%20Measurement%20Term%20Definitions.pdf](http://www.taxanalysts.com/www/freefiles.nsf/Files/EO%20Measurement%20Term%20Definitions.pdf/$file/EO%20Measurement%20Term%20Definitions.pdf) [http://perma.cc/3RHJ-JN7L]. What appears to be the first iteration

able to spend immense sums of money to influence campaigns—all without the regulations imposed on § 527 political groups for similar, and in some cases virtually indistinguishable, actions. The IRS began an effort to clarify and streamline these definitions in 2013, but the overwhelmingly negative reception to the proposed rule changes reflects the Agency’s inability to regulate this area on its own competently.⁸⁴

2. *Vague Definitional Problem*

The IRS also encounters enforcement disputes because its rules are often over- and under-inclusive regarding what constitutes political activity. The IRS released Revenue Rulings in 2004 and 2007 to help organizations determine whether they are advancing a social welfare mission or a partisan one.⁸⁵ Although the IRS issued the 2007 version to clarify its 2004 guidance, the revised Ruling almost immediately became irrelevant because the Agency released it just weeks before the Supreme Court announced its opinion in *Wisconsin Right to Life*.⁸⁶

The two Revenue Rulings lay out a facts-and-circumstances approach, offering similar discrete lists of factors that “tend to show”⁸⁷ political activity. It is uncertain, though, how the IRS applies the factors and what weight, if any, is assigned to each.⁸⁸ For example, generally speaking, voter education activities are not con-

of this internal rubric suggests that an organization “exclusively” engages in an activity if it allocates 95 percent of its time and other resources for that activity, though a seeming second iteration equates the meaning of “exclusively” and “primarily” because of § 501(c). *See id.*

84. *See* 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). The IRS received a record-high number of comments, and groups of all political leanings were largely critical of the proposed rule. Carl Hulse, *Left and Right Object to I.R.S. Plan to Restrict Nonprofits’ Political Activity*, N.Y. TIMES (Feb. 12, 2014), <http://www.nytimes.com/2014/02/13/us/politics/both-sides-object-to-irs-plan-to-restrict-nonprofits-political-activity.html> [<http://perma.cc/949K-9R7L>].

85. *See* Rev. Rul. 04-6, 2004-1 C.B. 328; Rev. Rul. 07-41, 2007-1 C.B. 1421.

86. The IRS issued the Ruling on June 1, 2007, Rev. Rul. 07-41, 2007-1 C.B. 1421, and the Supreme Court followed with its decision on June 25, 2007. WRTL, 551 U.S. 449 (2007). *See supra* Part I.B.2 for a discussion of WRTL’s impact, notably that it struck regulation of anything but express advocacy, rendering the 2007 Revenue Ruling, which addressed the distinctions between express advocacy and other forms of political speech, obsolete.

87. Rev. Rul. 04-6, 2004-1 C.B. 328.

88. *See id.*; Rev. Rul. 07-41, 2007-1 C.B. 1421.

sidered political activity, nor is expressing a view on a public policy issue—these activities, then, may be thought to fit comfortably within a social welfare purpose.⁸⁹ If, however, a voter education activity focuses on candidates from only one party, or an advertisement about an issue is explicitly tied to a particular candidate for office during an election season, the guidelines suggest that under these circumstances such conduct may be considered political activity.⁹⁰ The Revenue Rulings are also sometimes hard to interpret because they provide vague categories of prohibited behavior, rather than well-defined lists of acceptable activities.⁹¹

This imprecision is especially salient when determining whether § 501(c)(4) organizations should be subject to taxation on certain activities. These groups enjoy tax exemption for funds used for activities that reflect their prescribed purpose, but if an entity organized under § 501(c)(4) uses any funds for activities defined in § 527⁹²—that is, for political purposes—then the § 501(c)(4) organization must pay taxes on those funds.⁹³ With such a loose and easily manipulated definition of political activity, some groups are able to circumvent this requirement by claiming their candidate-related activities are solely for educational or issue-based purposes. Organizations can also avoid tax liability simply by donating directly to a § 527 organization.⁹⁴ Loopholes like this, whereby an organization can donate funds for political activity in which it cannot itself participate (at least without some limitation), contribute to the complexity inherent in regulating the political activity of tax-exempt groups.⁹⁵

89. Rev. Rul. 04-6, 2004-1 C.B. 328; Rev. Rul. 07-41, 2007-1 C.B. 1421. Per the Revenue Rulings, voter education activities include, among other undertakings, candidate debates featuring more than one party, informational pamphlets (which provide basic information about parties, candidates, and their platforms in order to help voters decide among the options), and get-out-the-vote campaigns (which are intended to encourage civic participation regardless of ideological leanings).

90. Rev. Rul. 04-6, 2004-1 C.B. 328; Rev. Rul. 07-41, 2007-1 C.B. 1421; *see also* Colinvaux, *supra* note 74, at 16-18.

91. *See* Dougherty, *supra* note 78, at 1339.

92. This includes activities that influence “nomination, election, or appointment of any individual to any ... public office.” I.R.C. § 527(e)(2) (2014).

93. *Id.* § 527(f).

94. Oosterhouse, *supra* note 21, at 268-69.

95. *See infra* Part III for a discussion of how the IRS could combat this issue.

The Revenue Rulings have only clouded the standards with which § 501(c)(4) organizations must comply. In the now very open electoral landscape, social welfare organizations essentially operate as PACs by independently spending on elections with unclear limits or controls.⁹⁶ This confusion has left the I.R.C. and traditional campaign finance regulations open to abuse.⁹⁷

B. Section 501(c)(4) Organizations Have Emerged as the Preferred Campaign Finance Vehicle

Although there are different methods for calculating money in politics, one trend is clear: independent expenditures have increased dramatically in post-*Citizens United* elections. Each cycle has seen record-high spending overall, but more remarkable is that independent groups outspent candidates and parties by any measure in the 2010, 2012 and 2014 elections.⁹⁸ A significant portion of this spending went undisclosed, either because it was a direct expenditure from a § 501(c)(4) group (no required disclosures), or because a disclosing group received (and reported) donations only from non-disclosing entities, rather than individuals. This situation—in which organizations take advantage of the gaps left in the current disclosure regime and the original sources of funding are impossible to

96. See Barker, *supra* note 4; see also Oosterhouse, *supra* note 21, at 268-69. For instance, the Nevada-based § 501(c)(4) organization Economy Forward spent nearly \$175,000, totaling 99 percent of its reported expenditures, on advertisements that praised Senator Harry Reid during his 2010 re-election campaign.

97. See Heather K. Gerken, Wade Gibson & Webb Lyons, *Rerouting the Flow of "Dark Money" into Political Campaigns*, WASH. POST (Apr. 3, 2014), http://www.washingtonpost.com/opinions/rerouting-the-flow-of-dark-money-into-political-campaigns/2014/04/03/1517ac6e-b906-11e3-9a05-c739f29ceb08_story.html [<http://perma.cc/5LUR-SQRC>].

98. See Ctr. for Responsive Politics, *Races in Which Outside Spending Exceeds Candidate Spending, 2010 Election Cycle*, OPENSECRETS, <http://www.opensecrets.org/outsidespending/outvscand.php?cycle=2010> [<http://perma.cc/7ZFB-Z6W6>]; Ctr. for Responsive Politics, *Races in Which Outside Spending Exceeds Candidate Spending, 2012 Election Cycle*, OPENSECRETS, <http://www.opensecrets.org/outsidespending/outvscand.php?cycle=2012> [<http://perma.cc/R7MW-52XE>]; Ctr. for Responsive Politics, *Races in Which Outside Spending Exceeds Candidate Spending, 2014 Election Cycle*, OPENSECRETS, <http://www.opensecrets.org/outside-spending/outvscand.php?cycle=2014> [<http://perma.cc/DD9K-LGXA>]. For the 2010, 2012, and 2014 elections, these reports indicate outside groups topped candidate expenditures in twelve, thirty-two, and twenty-eight congressional races, respectively. As we move farther from *Citizens United*, tax-exempt entities are brazenly spending more on political causes, often not in accordance with the I.R.C.

reach—is commonly referred to as the daisy chain effect.⁹⁹ There is now a real possibility that many § 501(c)(4) organizations are created simply to avoid the disclosure provisions imposed on § 527 groups. This permits those seeking to create a politically active tax-exempt group to choose: register as a § 527 political organization and face a strict disclosure regime, or organize under § 501(c)(4) with little paperwork and imprecise restrictions on spending. As revealed below, that choice has been an easy one.

1. Increased Independent Expenditures

Two years after *Citizens United* and *SpeechNow*, the country experienced the most expensive election to date—an estimated \$6 billion was spent at the federal, state, and local levels.¹⁰⁰ Independent expenditures comprised more than \$1 billion of this total, signaling a dramatic increase after the decisions.¹⁰¹ The Supreme Court has slowly dismantled campaign finance reforms,¹⁰² and since 2010, “any outside group can use corporate money to make a direct case for who deserves your vote and why, and they can do so right up to Election Day.”¹⁰³

Some claim that campaign finance regulations have had no sway in decreasing the involvement of independent organizations,¹⁰⁴ or if anything, have increased contributions to outside groups because of candidate contribution limits.¹⁰⁵ This conclusion is questionable, though, given the decrease in outside spending from 2004 to 2006, after BCRA’s passage in 2002, and the subsequent increase in the 2008 election, after *Wisconsin Right to Life* provided the first blow

99. Torres-Spelliscy, *supra* note 37, at 87.

100. Erenberg & Berg, *supra* note 70, at 502.

101. Compare the \$1 billion independent expenditures in 2012 with the 2008 figure, \$143.6 million—a near tenfold increase. Ctr. for Responsive Politics, *Outside Spending by Cycle, Excluding Party Committees*, OPENSECRETS, <http://www.opensecrets.org/outsidespending/> [<http://perma.cc/RYS8-W2CM>].

102. *See supra* Part I.B.

103. Bai, *supra* note 68.

104. *Id.*

105. Gora, *supra* note 11, at 784. But if candidate contribution limits force funds to outside groups, this reinforces the notion that donors intended that the money be used for partisan involvement and that they gave without regard to the legally specified purpose of the organization.

to BCRA in 2007.¹⁰⁶ Additionally, the bulk of independent funds, and political funds in general, are now spent in the final weeks before an election—directly in the face of BCRA’s now-defunct blackout provisions.¹⁰⁷ Even those who may consider money’s impact to be overstated concede that a certain baseline is required to be a competitive candidate.¹⁰⁸ Regardless of how it is counted and categorized, the fact remains that money affects election outcomes, and post-election, affects legislative outcomes.¹⁰⁹

An increasing portion of this spending is undisclosed.¹¹⁰ In the 2010 election, § 501(c)(4) groups outspent Super PACs (organized under § 527) 3-to-2, and seven of the top ten outside spenders were social welfare groups.¹¹¹ The numbers are starker when compared side-by-side. In mid-September 2008, groups that did not fully disclose their donors had spent \$32 million on advertisements; at the same point in the 2012 election, this number had ballooned to \$135 million.¹¹²

The 2014 midterm election tells the same story. The mid-September mark showed a three-fold increase in the 2014 midterms compared to the 2010 election.¹¹³ In August 2014, the FEC reported over \$50 million in independent spending, and this number jumped

106. See Hasen, *Big Money Explosion*, *supra* note 66.

107. See Goodman, *supra* note 62; *infra* note 114 and accompanying text.

108. See John Cassidy, *Jeb, Hillary, and the Money Primary*, NEW YORKER (Feb. 18, 2015), <http://www.newyorker.com/news/john-cassidy/jeb-hillary-money-primary> [http://perma.cc/2FJJ-3ERY] (“[Campaign strategists] worry more about raising less cash than their opponents and falling behind in the money primary.... ‘All that matters in this first quarter is fundraising.’” (quoting “veteran G.O.P. operative” and former Bob Dole campaign manager Scott Reed)); see also Hasen, *Progressive Approaches*, *supra* note 69, at 31-32 (discussing the “money primary”).

109. See Hasen, *Progressive Approaches*, *supra* note 69, at 32. As former U.S. Congressman Steve LaTourette has explained, “I don’t think [independent groups] have to make a [direct] threat” to obtain a desired legislative result. “One, I think people are smarter than that; two, it [is] ... implicit in the scorecard.” DANIEL P. TOKAJI & RENATA E.B. STRAUSE, *THE NEW SOFT MONEY: OUTSIDE SPENDING IN CONGRESSIONAL ELECTIONS* 83 (2014).

110. See Benson, *supra* note 49, at 744.

111. *Id.*; Conor Dowling & Amber Wichowsky, *Why We Should Care About Dark Money Ads*, WESLEYAN MEDIA PROJ. (Oct. 16, 2014), <http://mediaproject.wesleyan.edu/blog/why-we-should-care-about-dark-money-ads/> [http://perma.cc/67TE-4WK2]; see also Barker, *supra* note 4.

112. Benson, *supra* note 49, at 744.

113. Nancy Kaffer, *How to Make Campaign Finance Reform Sexy*, DAILY BEAST (Sept. 22, 2014, 5:45 AM), <http://www.thedailybeast.com/articles/2014/09/22/how-to-make-campaign-finance-reform-sexy.html> [http://perma.cc/39CB-HRT5].

to over \$400 million by the end of October.¹¹⁴ Social welfare organizations spent in record numbers, meaning the American public does not have the chance to know who spent almost \$120 million (a modest estimate) to influence their votes in 2014,¹¹⁵ often more than the campaigns themselves. In the 2014 Iowa Senate race, for example, candidates spent less than half of what outside groups spent.¹¹⁶ This disparity was represented nationwide in Senate and House races,¹¹⁷ and many believe the increase in independent spending impacts House races more, because smaller expenditures can have a more significant impact at the congressional district level.¹¹⁸

The increase in independent spending is problematic for two reasons. First, independent groups are not politically accountable like candidates and parties; their vitality is not based on their political decisions. Second, and relatedly, the political involvement of independent groups has made it much harder for campaigns to control their messages and the candidates' image.¹¹⁹ Because so-called social welfare groups are not politically accountable in the same way as major parties and candidates, they tend to produce more negative advertising, focusing their efforts on opposing

114. Matea Gold, *Big Spending by Parties, Independent Groups Drowns Airwaves in Negative Attacks*, WASH. POST (Oct. 22, 2014), http://www.washingtonpost.com/politics/big-spending-by-parties-independent-groups-drowns-airwaves-in-negative-attacks/2014/10/21/b4447f66-593c-11e4-b812-38518ae74c67_story.html [<http://perma.cc/37V5-8BYA>]. "Dark money" groups were responsible for at least \$130 million of this estimate and likely spent much more on activities reported as "issue advocacy." *Id.*

115. See Ctr. for Responsive Politics, *Outside Spending, Total by Type of Spender, 2014*, OPENSECRETS, http://www.opensecrets.org/outsidespending/fes_summ.php [<http://perma.cc/6LKG-ML72>]. CRP reported nearly \$800 million in non-candidate spending, including over \$340 million from Super PACs and just over \$118 million from § 501(c)(4) social welfare organizations. When spending from unions and trade associations, which also do not disclose donors, is added to that from social welfare groups, the total undisclosed amount grows past \$160 million. Notably, party spending made up *less than one-third* of total outside spending, at around \$234 million.

116. Compare Ctr. for Responsive Politics, *2014 Outside Spending, by Race*, OPENSECRETS, <http://www.opensecrets.org/outsidespending/summ.php?disp=R> [<http://perma.cc/9UW3-U3UJ>] (revealing over \$61 million spent by outside groups), with Ctr. for Responsive Politics, *Total Raised and Spent 2014 Race: Iowa Senate*, OPENSECRETS, <http://www.opensecrets.org/races/candidates.php?cycle=2014&id=IAS2&spec=N> [<http://perma.cc/4ZAT-MSZV>] (indicating the two major party candidates, winner Joni Ernst (R) and incumbent Bruce Braley (D), together spent just over \$24 million).

117. See Gold, *supra* note 114.

118. See Bai, *supra* note 68; Hasen, *Danger*, *supra* note 69.

119. See *infra* note 191 and accompanying text.

candidates rather than supporting them.¹²⁰ Part of the rise in spending can be explained simply because the number of § 501(c)(4) groups has increased, but this proliferation only solidifies the point that such organizations are now the preferred election finance vehicle, founded for political activity in contravention of the I.R.C.

Some claim that increased independent spending is not a problem because it levels the electoral playing field.¹²¹ For example, in the 2012 presidential election, the two major party candidates and their respective parties each spent a little under \$1 billion.¹²² But outside spending on both sides exceeded \$100 million, and in the case of independent conservative groups, nearly matched candidate spending.¹²³ When special interest spending comes close to outpacing, or even matching, a presidential candidate's own campaign expenditures, it should be no comfort that aggregate spending is equivalent. As referenced above, such financial influence results in outside groups enjoying immense political capital with voters, minus the restraint of political accountability.

2. *Relaxed Reporting Provisions*

Presumably the main reason politically-minded groups choose to file under § 501(c)(4) is because of the lower disclosure provisions to which such organizations are subject.¹²⁴ Although it is unclear whether any amount of political activity is consistent with the purpose of § 501(c)(4),¹²⁵ many of these groups are formed specifically to work with Super PACs and to engage in independent political spending, rather than social welfare activities.¹²⁶ Indeed, based on their FEC reports, it seems some § 501(c)(4) groups use their whole budgets for political expenses.¹²⁷ Those funds are often

120. See *infra* note 189 and accompanying text.

121. See Gora, *supra* note 11, at 782.

122. See Ctr. for Responsive Politics, *2012 Presidential Race*, OPENSECRETS, <http://www.opensecrets.org/pres12> [<http://perma.cc/RK59-AGDP>].

123. See *id.*

124. See Colinvaux, *supra* note 74, at 22-26; Dougherty, *supra* note 78, at 1339-41; *supra* Part I.A.

125. See *supra* Part II.A.

126. See Dougherty, *supra* note 78, at 1341-42. There is some concern that § 501(c)(4) is being corrupted to promote only private interests. See *infra* note 240.

127. See *supra* notes 6, 96 and accompanying text; *infra* note 215 and accompanying text.

reported to the IRS as having been used for “educational activities” so that these groups can retain their exempt status.¹²⁸

Public disclosure of political donors has remained a valid campaign finance regulation,¹²⁹ in part because it “enables the electorate to make informed decisions and give proper weight to different speakers and messages.”¹³⁰ As discussed above, § 501(c)(4) organizations must report to the IRS donors who give more than \$5000, but they do not have to make this information public.¹³¹ In contrast, § 527 political groups must publicly disclose donors and, in some way, account for every dollar contributed and spent.¹³² If they refuse to comply with these requirements, § 527s must pay corporate tax on those funds and may risk losing their tax-exempt status altogether.¹³³ This system sufficiently encourages disclosure, though some PACs have chosen to pay the penalty rather than disclose.¹³⁴

Certain political activities do trigger FEC reporting for all actors, including § 501(c)(4) organizations, but these requirements are largely ineffective at capturing actual political expenditures because they cover only specifically earmarked donations. For example, once a social welfare organization has spent more than \$10,000 in a calendar year for electioneering communications (“express advocacy” regarding a candidate), it must file Form 9 with the FEC, which includes a list of donors who gave \$1000 or more *for the purpose of those communications*.¹³⁵ Similarly, once a group spends \$250 on independent expenditures (those made absent coordination with candidates and parties) in a calendar year, it must file an itemized list for each expenditure, as well as quarterly reports of all dona-

128. See *infra* notes 146-52 and accompanying text.

129. See *supra* note 64 and accompanying text.

130. Dowling & Wichowsky, *supra* note 111. Disclosure requirements should be easier to comply with now more than ever because of electronic reporting.

131. See Torres-Spelliscy, *supra* note 37, at 81.

132. See *supra* Part I.A.

133. See Torres-Spelliscy, *supra* note 37, at 85-86.

134. See Benson, *supra* note 49, at 744. IRS donor disclosure is also not without challenge. The § 501(c)(4) group Campaign for Liberty, associated with former Representative Ron Paul, has refused to provide donor disclosure and to pay any fines the IRS would impose. Joel Gehrke, *Ron Paul Group to Defy IRS*, WASH. EXAMINER (Apr. 15, 2014, 12:00 AM), <http://washingtonexaminer.com/ron-paul-group-to-defy-irs/article/2547261> [http://perma.cc/JY77-6ETB].

135. See Torres-Spelliscy, *supra* note 37, at 73-74 nn.66-72.

tions over \$200 given *for those expenditures*.¹³⁶ Politically active groups can therefore avoid such reporting by raising general funds, with no restricted or designated uses.

Some have suggested reforming these regulations to force robust disclosures, perhaps by requiring a public list of top funders¹³⁷ or a disclaimer at the end of a group's advertisements stating that it does not disclose donors,¹³⁸ or by passing a constitutional amendment.¹³⁹ Federal election law, after all, strongly favors disclosure obligations, because it holds political actors accountable, minimizes false information, provides cognitive shortcuts, and reveals information about financial supporters.¹⁴⁰ Nonetheless, there are always privacy concerns when making certain information available to the public, so how disclosure is structured is crucial in determining whether it is effective, appropriate, and constitutional.¹⁴¹ Disclosure reform has been deliberated at length elsewhere,¹⁴² and it may be a complicated path because social welfare groups do have some FEC reporting obligations and, more importantly, because the Supreme Court has historically protected § 501(c)(4) donor lists from the public.¹⁴³ Traditional tax law also places limits on what information is made publicly available.¹⁴⁴ Any new disclosure requirements imposed on § 501(c)(4) groups will have to be appropriately tailored to include only donors whose dollars were used for political expenditures, as opposed to legitimate issue advocacy, and regulators may face the same definitional and earmarking shortcomings discussed

136. *See id.* at 75 nn.75-78.

137. *Id.* at 87.

138. Gerken, Gibson & Lyons, *supra* note 97.

139. *See DISCLOSE Act (S.2516) and the Need for Expanded Public Disclosure of Funds Raised and Spent to Influence Federal Elections: Hearing on S. 2516 Before the S. Comm. on Rules & Admin.*, 113th Cong. (2014); *Democracy Is Strengthened by Casting Light on Spending in Elections Act*, HR. 5175, 111th Cong. (2010).

140. *See* Benson, *supra* note 49, at 746; *see also* Torres-Spelliscy, *supra* note 37, at 62-63; Dowling & Wichowsky, *supra* note 111.

141. *See* Benson, *supra* note 49, at 747; Lloyd Hitoshi Mayer, *Nonprofits, Politics, and Privacy*, 62 CASE W. RES. L. REV. 801, 812-14 (2012); *see also* Torres-Spelliscy, *supra* note 37, at 71-72.

142. *See, e.g.*, Benson, *supra* note 49, at 743-47 (outlining the benefits of disclosure and explaining how it serves the fundamental values); Colinvault, *supra* note 74, at 6-7, 11-23 (discussing the challenges of imposing restrictions on tax-exempt groups); Torres-Spelliscy, *supra* note 37, at 64-65 (urging the IRS to adopt robust disclosure requirements).

143. *See supra* note 12.

144. *See* Mayer, *supra* note 141, at 806-07.

above. The disclosure solution may also fall short, as Professor Richard Hasen has explained, because it is “a poor substitute for more serious and effective campaign regulation.”¹⁴⁵

There is some evidence that groups gamble with their exempt status, betting on a lack of IRS enforcement.¹⁴⁶ Consider the Republican Jewish Coalition (RJC), a § 501(c)(4) organization. In its application to the IRS, the RJC indicated it planned to engage in no political activity.¹⁴⁷ Leading up to the 2012 election, however, the RJC hosted a meeting where it played advertisements that attacked President Obama’s policies and then described a plan to help the election of Republican challenger Mitt Romney.¹⁴⁸ The RJC solicited donations after this presentation, reminding donors that, because the RJC is organized under § 501(c)(4), they would be shielded from public disclosure.¹⁴⁹ The group reported to the FEC more than \$1 million spent on political advertisements, but its Form 990 for the same year showed no direct political expenditures.¹⁵⁰ The RJC did list nearly \$4 million in contributions to other politically active tax-exempt groups, suggesting that the RJC may have also funded political activity that was not reported to the FEC.¹⁵¹ Even if the organizations receiving RJC’s donations did report to the FEC, though, the daisy chain effect would come into play, and the original donor to the RJC would be able to avoid disclosing. Other social welfare organizations have also reported incongruent amounts of political spending to the IRS and the FEC, indicating a significant disconnect between the regulatory requirements and policies of the two Agencies.¹⁵²

Arguably at the center of this controversy is Crossroads Grassroots Policy Strategies (Crossroads GPS), which operates as a § 501(c)(4) organization affiliated with the § 527 group American

145. Hasen, *Progressive Approaches*, *supra* note 69, at 21.

146. Barker, *supra* note 4. In a survey of § 501(c)(4) filings, nearly half of the groups listed no intent to impact elections on the initial application but later reported political spending on tax returns. *Id.*

147. *Id.*

148. *Id.*

149. *Id.*

150. *Id.*

151. *Id.*

152. *Id.* For example, in its FEC filing, the § 501(c)(4) Center for Individual Freedom reported spending \$2.5 million on advertisements for the 2010 election, but on its tax return, the group reported only issue-based educational and legislative activities. *Id.*

Crossroads. For the 2012 presidential race, the groups announced that *together* they would spend \$200 million to support the election of Mitt Romney.¹⁵³ This is problematic because the groups are supposed to serve two distinct tax-exempt purposes—political activity and social welfare activity—and thus maintain two distinct financial tallies of those activities. The announcement suggests that once Crossroads GPS reached its political activity limit (however that is defined), American Crossroads could step in to finish the job. So even when they remain independent from candidates, campaigns, and parties, social welfare groups can flout the spirit of the tax restrictions and engage in inventive accounting to keep their expenditures in check. More disconcerting, though, is evidence of so-called independent groups tracking and supporting candidate and party strategies.

3. *The Coordination Problem*

By striking the corporate expenditure ban, the Court has greatly expanded the range of activities in which § 501(c)(4) organizations can engage without expanding the ability of the government to track such activities. These groups can now basically operate as PACs, at least for 49.9 percent of the time, and work together to hide their donors by utilizing the daisy chain effect. This expansion also presents the problem of coordination, defined for election purposes as “cooperation, consultation, or concert with, or at the request or suggestion of, a candidate, a candidate’s authorized committee or their agencies, or a political party committee or its agents.”¹⁵⁴ Despite this seemingly all-encompassing description, “the legal definition of

153. *Id.* Actual reported expenses for the two groups came to just under \$175 million, though unreported “issue” advertisements might increase the total. See Ctr. for Responsive Politics, *American Crossroads: Independent Expenditures, Communication Costs and Coordinated Expenses, Election Cycle 2012*, OPENSECRETS, <https://www.opensecrets.org/pacs/indexpend.php?cmte=C00487363&cycle=2012> [<http://perma.cc/LK3F-7GRE>]; Ctr. for Responsive Politics, *Crossroads GPS: Independent Expenditures, Communication Costs and Coordinated Expenses, Election Cycle 2012*, OPENSECRETS, <https://www.opensecrets.org/pacs/indexpend.php?cmte=C90011719&cycle=2012> [<http://perma.cc/ZMD5-Q7RZ>].

154. *Coordinated Communications and Independent Expenditures*, FEC, <http://www.fec.gov/pages/brochures/indexp.shtml> [<http://perma.cc/W5GL-45JR>] (last updated Jan. 2015).

prohibited coordination is narrower than the commonsense meaning of the term,”¹⁵⁵ which “allows a great deal of, well, coordination.”¹⁵⁶

Unfortunately, in a deficiency this Note hopes to correct, “the FEC’s enforcement of coordination has made [the definition even] narrower in practice.”¹⁵⁷ The FEC addresses coordination only in the context of political communications, not overall activities. The Agency employs a three-part test, which considers: the Payment Prong, whether the candidate/campaign or an independent source, in whole or in part, provided the funds; the Content Prong, whether the advertisement is expressly tied to a candidate or features campaign-prepared material; and the Conduct Prong, whether the outside group and the campaign engaged in particular kinds of interactions like requesting, suggesting, or discussing the advertisement.¹⁵⁸ Each prong must be satisfied for the government to be successful in showing unlawful coordination occurred.¹⁵⁹

Campaigns and independent groups are predictably careful about not crossing this line. But because they are “frustrat[ed] at *not* being able to coordinate,” they often skillfully test the borders and reveal “just how narrow [the] line is.”¹⁶⁰ Even campaign insiders express skepticism at the idea that coordination does not occur and consider the whole system “kind of a farce.”¹⁶¹ The groups sometimes share office space or staff members, and leadership for “independent” social welfare groups in recent years looks more and more like a list of yesterday’s campaign directors, a “revolving door”¹⁶² that results in a “rat’s nest” of political connections.¹⁶³ According to former Senator Kent Conrad, a fifteen-year congressional veteran, “[i]f you look at who makes up these organizations, on all sides, they’re loaded with political operatives.... So they don’t need to talk to anybody in the campaign in order to know what to do.”¹⁶⁴ Even so,

155. TOKAJI & STRAUSE, *supra* note 109, at 22.

156. Gerken, *supra* note 69, at 916.

157. TOKAJI & STRAUSE, *supra* note 109, at 22.

158. *See* FEC, *supra* note 154; *see also* TOKAJI & STRAUSE, *supra* note 109, at 21-22.

159. *See* FEC, *supra* note 154.

160. TOKAJI & STRAUSE, *supra* note 109, at 64-65.

161. *Id.* at 65.

162. Chris Moody, *How the GOP Used Twitter to Stretch Election Laws*, CNN (Nov. 17, 2014, 10:55 AM), <http://www.cnn.com/2014/11/17/politics/twitter-republicans-outside-groups/index.html> [<http://perma.cc/2XE4-SZJ8>].

163. Gerken, *supra* note 69, at 916-17; *see also* Barker, *supra* note 4.

164. TOKAJI & STRAUSE, *supra* note 109, at 65.

staffers of independent groups have been “conditioned” to check campaign websites, where they can access b-roll (recordings of candidate messaging), photographs, and talking points through hidden links.¹⁶⁵

Social media has also begun to play a role. Just two weeks after the 2014 midterm election, CNN revealed that the National Republican Congressional Committee used anonymous Twitter accounts to communicate polling data, an important strategic measure, with conservative “independent” groups.¹⁶⁶ The individual tweets were deleted every few months, and the accounts were deactivated the day before the election.¹⁶⁷ Outside groups have previously incorporated information shared via Twitter in their advertisements.¹⁶⁸ But the sharing of polling data for particular districts is unprecedented.¹⁶⁹

Although it is unclear whether the FEC would consider such behavior illegal under the current enforcement regime,¹⁷⁰ this conduct is part of the growing body of evidence that independent groups—social welfare organizations in particular—do indeed operate as shadow parties, complete with party elite leadership. These groups direct party priorities and reflect candidate and campaign messages, rather than advocate for specific policy issues.¹⁷¹ The emergence of shadow parties signifies a dangerous institutional shift in power and political energy.¹⁷² As Professor Heather Gerken explains:

Once you understand the hydraulics of party power, once you recognize that party elites will shape-shift in response to changes in the regulatory environment, you can see that it’s quite easy to imagine the rise of shadow parties in the wake of *Citizens United*. In fact, we *already* see party elites exercising a great deal of control over independent-spending organizations. Despite the formal prohibitions on coordination, the independent Super

165. *Id.* at 66-67.

166. *See* Moody, *supra* note 162. Online anonymity is difficult, as this news report reveals, but the groups used account names like @TruthTrain14 and @brunogianelli44, appropriating a character from the popular television series *The West Wing*.

167. *Id.*

168. *Id.*

169. *See id.*

170. *See id.*; *see also supra* notes 157-59 and accompanying text.

171. *See* Gerken, *supra* note 69, at 915-17; Gold, *supra* note 114.

172. *See* Gerken, *supra* note 69, at 912, 919.

PACs and 501(c)(4)s are intimately interconnected with the real parties.¹⁷³

In the past, parties have been able to temper interest groups in favor of streamlined political goals, acting as the fora where interest groups could negotiate practical solutions and “reach deals that allow for governance.”¹⁷⁴ Partisan (that is, private-interest) independent groups will probably not be capable of following the same course on their own.

The IRS and the FEC have clearly lost the regulatory game¹⁷⁵ when organizations designed for discrete purposes can blur the lines and operate so closely with one another and with candidates, parties, and campaigns.¹⁷⁶ This is not to say that all § 501(c)(4) entities are falsely created; many legitimate social welfare groups exist and engage in actual, valuable issue advocacy. But there must be a way to distinguish the two. Only if the IRS and the FEC work together will they be able to provide the stricter enforcement necessary to fix this problem.

C. Deregulation’s Impact on Values that Support Campaign Finance Restrictions

Recall the four rationales that underlie campaign finance restrictions: the anti-corruption, equality, participation, and information interests.¹⁷⁷ Although the Roberts Court has recognized only quid pro quo corruption as a sufficient government interest to restrict political speech,¹⁷⁸ the changed landscape in political spending may require revisiting this judgment. The increase in independent spending on political advertisements cuts across the values that motivate campaign finance regulation, the most important of which is the anti-corruption interest.

Independent spending does not corrupt in the same way as direct contributions to a candidate, but as Professor Hasen has explained,

173. *Id.* at 915.

174. *Id.* at 919.

175. *See infra* note 200.

176. *See Gerken, supra* note 69, at 906, 910-13; *Torres-Spelliscy, supra* note 37, at 62.

177. *See supra* Part I.B.1.

178. *See generally* *Citizens United v. FEC*, 558 U.S. 310 (2010).

“\$20 million in a Super PAC supporting Member of Congress X is less bad (but still bad) than \$20 million in Member X’s campaign account [from that Super PAC].”¹⁷⁹ Candidates do not live in a vacuum and are aware when support from outside groups, § 501(c)(4)s or otherwise, assists their political success (or defeat).¹⁸⁰ At least one state supreme court has accepted a systemic-level anti-corruption principle,¹⁸¹ and Judge Calabresi of the Second Circuit recently recognized the same.¹⁸² As we return to a time of unregulated political spending, the reemergence of these values is likely to continue.¹⁸³

As Super PACs grow larger and continue coordinating strategy between social welfare groups and wealthy donors,¹⁸⁴ the equality interest has also become more important. The donor class for the 2012 election was a “select group. The top 100 individual Super PAC donors ma[d]e up just 3.7% of those who [] contributed ... but account[ed] for more than 80% of the total money raised.”¹⁸⁵ The donors represented a homogenous, business-focused group, many of whom personally gave more than \$1 million.¹⁸⁶ Indeed, some candidates in the 2012 presidential primaries owed their competitiveness to individual donors and outside groups.¹⁸⁷ Similarly, an increase in funds for judicial elections has seen money shift from candidates to independent groups, which may later impact judicial decision making.¹⁸⁸

Increased independent spending also impacts the participation and information interests. Because social welfare organizations are

179. Hasen, *Progressive Approaches*, *supra* note 69, at 33.

180. *See id.*

181. *See* Benson, *supra* note 49, at 742 (citing *Grady v. City of Livingston*, 141 P.2d 346 (Mont. 1943)).

182. *See* Ognibene v. Parkes, 671 F.3d 174, 197-99 (2d Cir. 2012) (Calabresi, J., concurring) (“[T]he antidistortion interest promotes [free speech rights] in two important ways.”).

183. *See* Benson, *supra* note 49, at 741-42.

184. For a stunning but helpful illustration of the Koch brothers’ political network, see Ctr. for Responsive Politics, *Koch Network*, OPEN SECRETS, <https://www.opensecrets.org/news/wp-content/uploads/2014/05/kochnet.jpg> [<http://perma.cc/4K85-27SS>].

185. Charles Riley, *Can 46 Rich Dudes Buy an Election?*, CNN MONEY (Mar. 26, 2012, 8:50 AM), <http://money.cnn.com/2012/03/26/news/economy/super-pac-donors> [<http://perma.cc/LK82-4ZY4>].

186. *See id.*

187. *See id.*

188. For a full discussion of the impact of *Citizens United* on judicial elections, see Erenberg & Berg, *supra* note 70, at 502.

not held accountable to the public, they tend to release many more negative advertisements compared to campaigns or leadership PACs.¹⁸⁹ This can decrease confidence and participation in elections¹⁹⁰ and distort the information the public has about a candidate's message.¹⁹¹ Noting declining voter confidence in his *Wisconsin Right to Life* dissent, Justice Souter recognized participation as an important government interest—an appropriate justification, then, for the BCRA provisions.¹⁹² Justice Stevens later echoed this sentiment in his *Citizens United* concurrence.¹⁹³

The information interest is most affected by the ambiguous names § 501(c)(4) groups often choose for themselves.¹⁹⁴ For example, in a Colorado ballot measure, a group called “Littleton Neighbors Voting No” reported spending \$170,000 against a zoning restriction that would have prevented construction of a new Wal-Mart store.¹⁹⁵ It was later revealed that Wal-Mart itself fully funded the “Neighbors” coalition.¹⁹⁶ This anonymity is quite beneficial—even when a negative advertisement airs, voters tend to be more receptive and agreeable if the source is an unknown group, or if donors are not listed.¹⁹⁷ Voters rely on cognitive shortcuts, like which organizations support a candidate, when deciding for whom

189. See Benson, *supra* note 49, at 741.

190. A 2012 survey conducted by the Brennan Center for Justice reveals this crisis of confidence: more than 80 percent of those surveyed believed money spent in the 2012 election, compared with past elections, would lead to more corruption; nearly two-thirds trusted government less because of the extra money in politics; and more than 25 percent were less likely to vote because of big-donor influence. BRENNAN CTR. FOR JUST., NATIONAL SURVEY: SUPER PACS, CORRUPTION, AND DEMOCRACY 1-3 (2012), <http://www.brennancenter.org/analysis/national-survey-super-pacs-corruption-and-democracy> [<http://perma.cc/XU87-MRW3>].

191. See Benson, *supra* note 49, at 741; see also Gora, *supra* note 11, at 772; *supra* notes 7-9 and accompanying text. This Note operates within the current Supreme Court rejection of the anti-distortion rationale first recognized in *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990), but given the changed landscape in just five years after *Citizens United*, now is an appropriate time for a renewed call for its recognition as a compelling interest and sufficient justification for regulation.

192. See *WRTL*, 551 U.S. 449, 507 (2007) (Souter, J., dissenting) (“Hence, the second important consequence of the demand for big money to finance publicity: pervasive public cynicism.”).

193. See *Citizens United v. FEC*, 558 U.S. 310, 447-50 (2010) (Stevens, J., concurring).

194. See Torres-Spelliscy, *supra* note 37, at 64.

195. *Id.* at 88.

196. *Id.*

197. Dowling & Wichowsky, *supra* note 111.

to cast a ballot.¹⁹⁸ But there is a documented impact on voter behavior once voters are fully informed about who is behind a political message, so the importance of rigorously enforcing disclosure requirements should not be understated.¹⁹⁹

All four principles underlying campaign finance regulations are affected when non-disclosing tax-exempt groups engage in significant political activities. The administrative solution proposed in this Note aims to honor and preserve these values.

III. PROPOSAL: FEC-IRS HYBRID ENFORCEMENT, ENHANCED BY INTERNAL AGENCY REFORMS

As detailed in Part II, money in politics continues to find new avenues, leaving regulators to play a game of catch-up.²⁰⁰ The Court perhaps best described the problem in *McConnell v. FEC*: “Money, like water, will always find an outlet.”²⁰¹ This comparison holds true more than ever now that § 501(c)(4)s are primed to be some of the biggest spenders in elections across the nation. Reformers have typically offered legislative solutions, hoping for a comprehensive overhaul of the campaign finance system. Even if these revisions are successful against procedural and judicial hurdles, though, it will be difficult to create a new statutory scheme that does not open itself to loopholes and abuse by expedient political actors. Further, while the statutory debates persist, social welfare organizations continue to engage in unchecked and sophisticated political operations capable of evading tax and election laws. Arranging rigorous enforcement through administrative tweaks and interagency cooperation is thus critical to fostering robust *and* transparent election dialogue. Working together, each Agency will be emboldened to fulfill its respective mission and to prevent corruption and exploitation of the electoral and tax systems.

198. Torres-Spelliscy, *supra* note 37, at 62-63.

199. *See id.*

200. *See* Gerken, *supra* note 69, at 906-11 (“[Political groups] inevitably [find] loopholes ... As a result, the entire reform game has been focused on closing those loopholes, engaging in the regulatory equivalent of whack-a-mole.”).

201. 540 U.S. 93, 224 (2003).

A. Internal Agency Reforms

Although this Note proposes a nuanced fix in the form of inter-agency regulation of social welfare groups' political speech, there is still great need for intra-agency reforms. Regulation of political activity can improve with precise definitions, influenced by broad statutory interpretation, and with stricter filing and reporting procedures. These internal changes, which fall within the regular scope of agency enforcement, are detailed below.

1. Filing Requirements

To have a worthwhile chance of regulating political spending by social welfare organizations, the IRS must strengthen applicable filing requirements, bringing them more in line with those laid out in § 527. No application is currently required to operate as a § 501(c)(4) organization,²⁰² meaning groups may pop up during election season and dissolve with no liability. According to Melanie Sloan, former executive director at Citizens for Responsibility and Ethics in Washington, this is one of the many problems regulators face with § 501(c)(4) political activity: "You can go into business and violate the law and then go out of business And what's ever going to happen about that? There's no consequence."²⁰³

The IRS has an easy fix: require an application from any § 501(c)(4) group that wishes to engage in political activity. For the groups that do not submit applications or indicate they will not conduct partisan activities but later do (evidenced by FEC filings), the IRS should impose sanctions to enforce the application requirement, including reclassification as a § 527 organization or revocation of exempt status. The current application form is sufficient, and administering such a requirement should not be particularly onerous because the IRS already accepts and reviews applications for tax exemption. The purpose of this change is simply to bring § 501(c)(4) political activity under the same regulatory scheme as § 527 political activity. Additionally, if the IRS discovers that a politically active group has formed and then disbanded during an election

202. See *supra* Part I.A.

203. Barker, *supra* note 4.

cycle, an inquiry is warranted to determine whether the organization's actual purpose was campaign intervention rather than social welfare. If so, an enforcement action would be appropriate.²⁰⁴

Similar reforms would ensure that the IRS receives more timely reports about political activity. Even if the IRS required public disclosures of donors, the current regulations would allow groups to file such information more than twenty-two months after Election Day.²⁰⁵ This could be the IRS's first notice of the existence of a politically active social welfare organization. The IRS should thus create rules that require strict and timely reporting like the FEC: within twenty-four hours of an exempt group's political expenditure, the group should notify the IRS. Such notification would close the timing gap and help the IRS tally political activity by social welfare organizations as they inch toward the threshold ("primary" or otherwise) and risk losing § 501(c)(4) status.

2. Earmarked Funds

Unlike the IRS's facts-and-circumstances methodology used to determine whether activity is "political,"²⁰⁶ the FEC's guidelines on what constitutes political involvement are more sharply drawn. Any entity that qualifies as a political committee—in the words of the Court, any group whose "major purpose ... is the nomination or election of a candidate" and whose activity is "by definition, campaign related"²⁰⁷—must register with the FEC and report contributions and expenditures over \$1000.²⁰⁸ This bright-line rule, however, is not without fault. As a preliminary matter, any social welfare organization that registers under this scheme risks a hefty tax bill because admitting it has the *major* purpose of impacting an election, such as when its activity very closely resembles that of traditional

204. Of course, the IRS must require more than evidence of mere coincidental timing. In addition to the length of time between creation and dissolution, and how that timing compares to the election cycle (perhaps defined by candidate activity), regulators should consider analysis of reported spending, number and identity of donors, and engagement in nonpartisan activity. These suggestions are not exhaustive and other factors will likely be relevant, but developing a comprehensive list is beyond the scope of this Note.

205. See Tobin, *supra* note 28.

206. See *supra* Part II.A.2.

207. Buckley v. Valeo, 424 U.S. 1, 79 (1976).

208. See 11 C.F.R. § 100.5(a) (2012).

political actors, likely means conceding that social welfare activities are not its *primary* purpose.

Further, for each electioneering communication and independent expenditure, regardless of whether the spender (in other words, the speaker) is a registered organization, the FEC requires disclosures only for earmarked donations—those given *for the purpose* of the communication or expenditure.²⁰⁹ It is easy for organizations to avoid disclosure, then, even with this seemingly well-delineated rule. First, many donors to social welfare groups give unrestricted amounts—funds for the organization’s general budget rather than earmarked for a specific purpose.²¹⁰ Second, independent expenditures are still subject to the strict “magic words” test (“vote for [X]”),²¹¹ and political advertisements are considered electioneering communications only in limited circumstances.²¹²

BCRA makes no mention of earmarked funds, so the FEC rules represent a very narrow reading of the statute.²¹³ The FEC should thus broaden its administrative understanding of the statute to cover more funds—those actually used for political involvement, rather than only those intended for such activity. This wider perspective would trigger more complete reporting for all politically active organizations, regardless of tax status.²¹⁴

The IRS should also independently address this problem by taking the opposite approach and imposing an earmark rule. By requiring social welfare organizations to pay for political activity with funds specifically earmarked for such a purpose, the IRS can help prevent circumvention of FEC requirements (should they stay the same) and align tax-exempt activities and reporting with congressional intent. With this rule, if an organization were not able to raise designated funds, it could not legally engage in any political activity. This stricter accounting would facilitate more accurate FEC disclosures and assist the IRS in determining whether the group is “primarily” organized for social welfare.

209. See Torres-Spelliscy, *supra* note 37, at 63, 71, 73 n.68, 75.

210. See *id.* at 73.

211. See *Buckley*, 424 U.S. at 44 n.52; 11 C.F.R. § 100.16(a).

212. See 11 C.F.R. § 100.29(a); see also Torres-Spelliscy, *supra* note 37, at 63.

213. See Torres-Spelliscy, *supra* note 37, at 73.

214. See *id.*

3. *Combating the Daisy Chain Effect*

Even when the disclosures they receive are consistent, the IRS and FEC should remain watchful in order to combat obscured disclosures made possible by the daisy chain effect. A classic example of the daisy chain effect in action is the Center to Protect Patient Rights, which spent 75 percent of its budget (more than \$44 million) on contributions to other politically active tax-exempt groups.²¹⁵ When organizations act as conduits, tracking donations becomes much more difficult. Under the current regime, social welfare organizations can report donations from similar groups without mention of the original donor.²¹⁶ If a § 527 or § 501(c)(4) organization reports contributions from other social welfare groups, the IRS should require the reporting organization—the last in the chain—to disclose donation history so that the money is traceable to the original source. This process adds some procedural burdens (for exempt entities rather than the IRS), but it is not too severe a requirement for § 501(c)(4) organizations that engage in political activity. Such an obligation mirrors the strict accounting expected of § 527 groups for their political activity and serves the same functions,²¹⁷ bringing into agreement how political activity is treated across exempt organizations. This area of regulation in particular also lends itself well to interagency regulation—that is, cooperation between the FEC and the IRS.

B. Cooperative Regulation: Pooling Together Tax & Election Enforcement Powers

The internal changes discussed above are important steps in improving enforcement of the laws relating to politically active social welfare organizations. Perhaps more important, though, is for the Agencies to provide a unified front against entities that do not follow the restrictions of their exempt, politically active status. The FEC oversees the financing of elections,²¹⁸ and the IRS, the effective

215. See Barker, *supra* note 4.

216. See *supra* note 99 and accompanying text.

217. See *supra* Part I.A.2.

218. See *supra* note 3.

administration of the tax code.²¹⁹ These seemingly distinct areas overlap when tax-exempt organizations engage in political activity, and this intersection necessitates something more complex than independent regulation. The Agencies thus must work together, combining their respective powers to accomplish their separate but interrelated missions.

Professor Daphna Renan's recent work is particularly informative as to how this regulation can legally and functionally take shape. As she explains, "pooling" is the process of two or more agencies working together, which is neither required nor prohibited by statute, nor limited to instances of designated overlap.²²⁰ The purpose of pooling is to take advantage of agencies' diverse specialized expertise, authorization, or abilities in certain areas and "create regulatory power that would not otherwise exist."²²¹ Though pooling is not limitless—statutory, political, and institutional constraints still apply—agencies may undertake pooling on their own.²²² As policy priorities evolve, and regulatory challenges become more interconnected, pooling has become a desirable solution.²²³ Prompt administrative action, particularly in the form of pooling, is more responsive than legislative solutions to the flexibility this and other areas of regulation demand.²²⁴

Pooling is perhaps most common when one agency has the resources and institutional knowledge, but not the legal authority, to address a particular issue, and another agency, lacking in expertise, has the legal grant of power.²²⁵ The D.C. Circuit has ratified such arrangements, where the agencies "have complementary roles" and the statute does not forbid coordination.²²⁶ Such is the situation here, where the IRS has the statutory grant to regulate tax-exempt entities but lacks exact knowledge of the electoral system. The FEC,

219. *The Agency, Its Mission and Statutory Authority*, IRS, <http://www.irs.gov/uac/The-Agency-its-Mission-and-Statutory-Authority> [<http://perma.cc/T7ZR-5SRN>] (last updated Jan. 23, 2015).

220. See Daphna Renan, *Pooling Powers*, 115 COLUM. L. REV. 211, 214, 216, 219 (2015).

221. *Id.* at 217.

222. See *id.* at 218.

223. See *id.* at 234-35.

224. See *supra* Parts II.A-B.

225. See Renan, *supra* note 220, at 223.

226. *Id.* at 270-71 (citing *Nat'l Mining Ass'n v. McCarthy*, 758 F.3d 243, 247, 249 (D.C. Cir. 2014)).

on the other hand, possesses institutional expertise and the grant to regulate political behavior, but cannot competently regulate issues of tax exemption. The IRS and the FEC thus will be most adept at regulating political speech by social welfare organizations only by engaging in pooling.

As the agency tasked with managing and administering the nation's elections, the FEC is perhaps the obvious regulatory entity of choice—the problems presented in this Note, after all, center on political involvement. But because social welfare organizations can avoid FEC reporting requirements, and simultaneously shirk tax responsibility, the Agency has “only part of the equation”²²⁷ needed to solve the crisis. IRS participation in this regulation is also appropriate—and virtually unavoidable—because tax-exempt status dictates at what level, if at all, a group can participate in political activity.²²⁸ Congress understands this to be true: thirteen senators have urged the IRS to adopt stricter limits on outside spending from social welfare groups, finding that the current “primary” purpose rule diverges from the language of the statute, which would demand an “insubstantial” amount of political activity.²²⁹ Ultimately, robust enforcement in this area will require a cooperative approach.

These Agencies are institutionally and structurally incapable of regulating this behavior on their own. The FEC suffers from perpetual structural gridlock.²³⁰ Functionally flawed at its core—six commissioners, three from each of the two major parties—it is beyond difficult to get the four votes needed for an administrative ruling.²³¹

227. Palmer Gibbs, *Transparency Advocates Look at “The Price We Pay for Money’s Influence on Politics” During Sunlight-Hosted Event*, SUNLIGHT FOUND. BLOG (Sept. 17, 2014, 10:45 AM), <http://sunlightfoundation.com/blog/2014/09/17/transparency-advocates-look-at-the-price-we-pay-for-moneys-influence-on-politics-during-sunlight-hosted-event> [http://perma.cc/ERW6-5WU8].

228. See *The Restriction of Political Campaign Intervention by Section 501(c)(3) Tax-Exempt Organizations*, IRS, [http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/The-Restriction-of-Political-Campaign-Intervention-by-Section-501\(c\)\(3\)-Tax-Exempt-Organizations](http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/The-Restriction-of-Political-Campaign-Intervention-by-Section-501(c)(3)-Tax-Exempt-Organizations) [http://perma.cc/4QM2-PGVW] (last updated Jan. 6, 2015).

229. See Paul Blumenthal, *Democrats Push IRS to Limit Dark Money’s Political Power with Strict New Rules*, HUFFINGTON POST (Feb. 27, 2014, 1:59 PM), http://www.huffingtonpost.com/2014/02/27/dark-money-rules_n_4867534.html [http://perma.cc/2LBG-FKTU]. Under that standard, Rosenberg’s Rules, *supra* note 83, indicate that 5 to 15 percent of an organization’s activity would be an acceptable threshold, rather than nearly 50 percent.

230. See Goodman, *supra* note 62.

231. See *id.*

Even Justices typically in favor of loose campaign restrictions have recognized the imperative need for, and constitutionality of, vigorous disclosure.²³² Yet the FEC ended in a 3-3 standstill in a recent request to shield a donor list from disclosure, failing to provide any clear guidance to the requestor.²³³ This fundamental disagreement plagues the FEC, consistently reducing its productivity.²³⁴ Even Congress, not exactly known for its efficiency,²³⁵ has lost respect for the FEC—despite the FEC’s countless demands for electronic filing, something on which both major parties can agree, the Senate refuses to amend internal rules that would allow it to comply with this request.²³⁶

The IRS has faced similar challenges. In 2013, it became embroiled in a scandal when evidence surfaced that it had directed extra attention toward social welfare organizations associated with the Tea Party movement.²³⁷ Sources revealed that the IRS had denied exempt status to certain groups that applied under § 501(c)(4), and conducted rigorous audits of existing groups, usually hand-picked by name (when indicating Tea Party affiliation).²³⁸ The IRS has since exhibited a general unwillingness to bring enforcement actions against tax-exempt groups for their political activities, engaging in an unofficial avoidance policy. Treasury oversight was pronounced “at best overzealous, at worst partisan,” only deepening

232. See, e.g., *Citizens United v. FEC*, 558 U.S. 310, 366 (2010) (“Disclaimer and disclosure requirements may burden the ability to speak, but they impose no ceiling on campaign-related activities, and do not prevent anyone from speaking.”); *id.* at 369 (“[T]he public has an interest in knowing who is speaking about a candidate shortly before an election.”); *Doe v. Reed*, 561 U.S. 186, 228 (2010) (Scalia, J., concurring) (“Requiring people to stand up in public for their political acts fosters civic courage, without which democracy is doomed.”).

233. See Peter Overby, *FEC: Tea Party May Not Shield Donors*, NPR (Nov. 22, 2013, 4:33 AM), <http://www.npr.org/2013/11/22/246665788/fec-tea-party-cant-shield-donors> [<http://perma.cc/YX76-JA5H>].

234. See *id.* Consider, in the mid-2000s, before *Wisconsin Right to Life* and *Citizens United*, the FEC voted on more than 1000 enforcement matters each year. Goodman, *supra* note 62. Since 2010, that has decreased to fewer than 200 per year. *Id.*

235. See David Sherfinski, *113th Congress Narrowly Avoids “Least Productive” Status: Report*, WASH. TIMES (Dec. 29, 2014), <http://www.washingtontimes.com/news/2014/dec/29/pew-113th-congress-narrowly-avoids-least-productiv/> [<http://perma.cc/3BHE-GWYR>].

236. See Overby, *supra* note 233.

237. See Goodman, *supra* note 62.

238. See *id.*; Andy Kroll, *The IRS Tea Party Scandal, Explained*, MOTHER JONES (Nov. 21, 2013, 1:19 PM), <http://www.motherjones.com/politics/2013/05/irs-tea-party-scandal-congress-nonprofit-obama> [<http://perma.cc/99H7-V5LF>].

this reluctance.²³⁹ The IRS now rarely initiates enforcement actions, even against exempt groups that clearly violate their tax-exempt status,²⁴⁰ and moots any litigation resulting from its action by refunding all levied fines or reinstating revoked exempt status.²⁴¹ Given its essential purpose of revenue collection, the IRS likely will not, on its own, make this regulation a priority, because it involves complicated enforcement of nonprofit groups (from which little revenue is collected).²⁴²

Though some may still feel the fallout from the scandal, the record-high independent spending in the 2014 midterms²⁴³ and the nearly 100 candidate-related outside groups already formed for the 2016 presidential election²⁴⁴ signify that it is time for the IRS to come forward and enforce its existing regulations. Timidity is arguably what led to the situation surrounding the scandal and made the IRS vulnerable to attack.²⁴⁵ In the wake of *Citizens United*, the IRS should have established useful precedent by issuing guidance about acceptable activities and reclassifying *all* delinquent organizations.²⁴⁶ It can follow this path now by pooling its resources and relevant expertise with the FEC's to create an appropriately forceful regulatory environment.

The Agencies are functioning poorly without support from one another, but the powers they do have complement each other well in this area. As discussed in Part II.B, the figures reported in FEC and IRS filings often conflict. The inconsistency lies largely at the center of the definitional problem created by the deficient guidance

239. Goodman, *supra* note 62.

240. Some have suggested the IRS could employ the private benefit doctrine to bring enforcement actions against § 501(c)(4) groups that are organized for the special interests of a few wealthy donors, rather than for "social welfare" purposes. *See, e.g.*, Dougherty, *supra* note 78, at 1342; Hasen, *Danger*, *supra* note 69.

241. *See, e.g.*, *Christian Coal. of Fla., Inc. v. United States*, 662 F.3d 1182, 1185 (11th Cir. 2011) (dismissing for mootness).

242. *See* Colinvaux, *supra* note 74, at 46.

243. *See* Derek Willis, *Outside Groups Set Spending Record in Midterms*, N.Y. TIMES, Dec. 11, 2014, at A3; *supra* Part II.B.1.

244. *See* Ctr. for Responsive Politics, *2016 Presidential Race, Behind the Candidates: Campaign Committees and Outside Groups*, OPENSECRETS, <http://www.opensecrets.org/pres16/outside-groups.php> [<http://perma.cc/6L3E-US2K>] (last updated Oct. 5, 2015, 7:00 PM) (indicating the formation of ninety-six outside groups supporting declared presidential candidates, including six § 501(c)(4) organizations).

245. *See* Colinvaux, *supra* note 74, at 46.

246. *See id.*

found in the IRS Revenue Rulings and by its case-by-case approach, as well as the FEC's constricted interpretation of BCRA's reporting requirements.²⁴⁷ Without well-defined guidelines, § 501(c)(4) groups can frame communications as issue advocacy—rather than express advocacy—and therefore avoid the IRS political activity threshold and the FEC disclosure requirements.²⁴⁸ Because the FEC regulations are clearer, groups often report higher political spending figures to the FEC than they do to the IRS.²⁴⁹ The 2013 IRS-proposed rules represent one step forward toward an improved enforcement regime, but the proposal lacks meaningful changes and thus remains inadequate.²⁵⁰ Election activities are not always easily distinguishable from actual issue-based actions,²⁵¹ but by creating more clearly defined standards, the IRS will be able to protect itself and social welfare groups that wish to engage in legitimate issue advocacy. The FEC's expertise in crafting rules about political activity should contribute to this venture significantly. Pooling their respective skills to craft a unified definition of political activity will also help ensure the Agencies receive accurate and consistent reports.²⁵²

Both the IRS and FEC reporting schemes incentivize social welfare organizations to minimize (that is, incorrectly categorize) political activities, so the Agencies must be guarded when evaluating reports of political spending. Unlike § 527 groups, the tax-exempt status of social welfare organizations hinges on a threshold determination—that their “primary” activity supports the social

247. See Galston, *supra* note 12, at 890; see also *supra* Parts II.A, II.B.2.

248. This is a legitimate concern given how imprecise the Rulings are regarding what is issue advocacy versus political activity. See *supra* notes 85-91 and accompanying text.

249. See, e.g., Robert Maguire & Viveca Novak, *Shadow Money Magic: Five Easy Steps that Let You Play Big in Politics, Hide Your Donors and Game the IRS—Step 2*, OPENSECRETS (Apr. 16, 2013), <http://www.opensecrets.org/news/2013/04/shadow-money-magic-five-easy-steps-1/> [<http://perma.cc/5WH7-G8UF>].

250. See *supra* note 84 and accompanying text.

251. In the ninety-day comment period, the IRS received over 140,000 comments, most of them negative. Gerken, Gibson, & Lyons, *supra* note 97.

252. The IRS was scheduled to release the revised version of its disastrous 2013 rule earlier this year. Pooling would strengthen this effort, but the Agency has at least suggested it is considering uniform application of the “political activity” definition to all politically active exempt entities. See Flynn & Bade, *supra* note 25.

welfare.²⁵³ The FEC collects information crucial to this determination—information about independent political expenditures, including what the money was spent on, where, and by whom.²⁵⁴ The IRS should regularly consult FEC filings to determine whether exempt organizations are adequately conforming to their prescribed purpose. This will no doubt impose some institutional burden on the IRS, but since these reports are readily available online to members of the public, ensuring accurate filings does not even require formal agency coordination. More importantly, though, this measure greatly furthers the IRS’s successful enforcement of the tax code, a task it is commanded to undertake.

By adopting clearer and more streamlined definitions, the FEC and the IRS will be able to ensure political expenditures are brought in to the regulatory scheme designed to capture them. Developing a precise definition of what constitutes political activity will be essential to this cooperative effort. Even with a narrow definition, though, the Agencies should work together to determine which groups are engaging in what type of political activity (and how much), and whether those organizations have satisfactorily reported those activities.

CONCLUSION

This Note aims to provide an alternative solution to issues in the current campaign finance landscape regarding the increased involvement of social welfare organizations. Comprehensive legislative reform may at some point be necessary to fixing the campaign finance challenges highlighted herein, but much can be done in the regulatory space. Improving the reticent climate of agency avoidance and empowering the IRS and the FEC to create valuable, effective, and constitutional²⁵⁵ enforcement mechanisms is an equally beneficial, if not preferable, response to the rise in independent spending and of § 501(c)(4) political involvement.

253. See I.R.C. § 501(c)(4) (2014). As a general matter, FEC registration categorically excludes social welfare organizations because a § 501(c)(4) group’s “primary” purpose cannot be election intervention. See Tobin, *supra* note 28.

254. See Barker, *supra* note 4.

255. See *supra* note 12 and accompanying text.

Many scholars expect no meaningful reform will come until a scandal emerges.²⁵⁶ However, instituting the proposed internal reforms and engaging in cooperative action now provides a powerful, and likely more expedient, resolution. Most importantly, following such a path establishes a blueprint for stringent enforcement, ensuring that any later legislative reforms are operable and that regulators are not again trapped playing a game of catch-up. There is great danger in waiting for scandal, as non-enforcement leaves open the possibility of tax code and election law abuses, and allows more undisclosed money in politics. As Paul S. Ryan, senior counsel for the Campaign Legal Center, has explained, without rigorous enforcement, “[t]he political players who are soliciting these funds and are benefiting from ... these funds will know where the money came from. The only ones in the dark will be American voters.”²⁵⁷

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256. See, e.g., Hasen, *Progressive Approaches*, *supra* note 69, at 31; Gibbs, *supra* note 227; Overby, *supra* note 233. The sweeping restrictions of FECA did, after all, pass in the wake of the Watergate scandal. See Gora, *supra* note 11, at 768 (regarding FECA as a classic example of the establishment protecting itself against challenging voices).

257. Barker, *supra* note 4.

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