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CURRENT ISSUES IN CAMPAIGN FINANCE LAW ENFORCEMENT

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BEFORE THE

SUBCOMMITTEE ON CRIME AND TERRORISM

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

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CURRENT ISSUES IN CAMPAIGN FINANCE LAW ENFORCEMENT

TUESDAY, APRIL 9, 2013

U.S. SENATE,
SUBCOMMITTEE ON CRIME AND TERRORISM,
COMMITTEE ON THE JUDICIARY,
Washington, DC

The Subcommittee met, pursuant to notice, at 10:02 a.m., in Room SD–226, Dirksen Senate Office Building, Hon. Sheldon Whitehouse, Chairman of the Subcommittee, presiding.

Present: Senators Whitehouse, Feinstein, Schumer, Durbin, Klobuchar, Graham, Cruz, Sessions, and Lee.

OPENING STATEMENT OF HON. SHELDON WHITEHOUSE, A U.S. SENATOR FROM THE STATE OF RHODE ISLAND

Chairman WHITEHOUSE. Good morning. The hearing will come to order. I appreciate the witnesses being here, and the order of proceeding will be that any Senators who are present before the testimony will be invited to make any opening statement that they care to make. We will take the testimony from these witnesses and then have a question-and-answer session, and I think we will start with seven-minute rounds. It does not appear, given everything that is going on in the Senate today, that we are going to have a great number of Senators here, so I think we can go with seven-minute rounds. And we will switch then to the other panel and continue the same way, and we have to be done at noon. So I appreciate the witnesses who are here, and I will lead with my opening statement.

In a country of laws, when the laws are made a mockery, it is a serious matter. This hearing will explore the mockery our campaign finance laws have become, with particular emphasis on what appears to be flagrantly false statements made with impunity in official documents.

We note Section 1001 of the U.S. Criminal Code, which makes it a criminal offense to make "any materially false, fictitious, or fraudulent statement or representation" in official business with the government, and Section 7206 of the Internal Revenue Code, which makes it a crime to willfully make a false material statement on a tax document filed under penalty of perjury.

The false statements we look at relate, among other things, to Section 501(c)(4) of the Tax Code, which gives nonprofit status to entities that are "operated exclusively to promote social welfare." This promotion of social welfare is specifically forbidden to include direct or indirect participation or intervention in political cam-

paigns on behalf of or in opposition to any candidate for public office. It seems clear enough.

But after the Supreme Court opened the floodgates to big money in elections in its disgraceful *Citizens United* decision, big donors like to use these nonprofit entities to launder campaign spending and hide their identities. As the head of one such nonprofit admitted, for big donors "the anonymity was appealing."

So the tax filings then begin to get creative. There are several areas of mischief: discrepancies in reporting to the IRS and to the FEC; discrepancies between reported and actual political activity; characterizing political TV ads as "educational activities" or "legislative activities"; characterizing as "nonpolitical" donations made to other groups that then spend it on political advertising; and disbanding and reforming under other names before the reporting is due for the disbanded organization.

The responsible federal agencies, primarily the IRS and DOJ, appear somewhat complicit in the mockery that is made of these tax laws. The DOJ maintains a policy of deference to the IRS and does not investigate or prosecute false statements in campaign finance tax reporting without a case having been brought to it by the IRS. As we will hear from some of the witnesses, this creates problems. DOJ maintains this policy despite 18 U.S.C. 1001, the well-known law against false statements that spans all federal agencies in addition to the false statements law specific to tax filings.

The IRS on its part is an organization as to which, according to press reports quoting its own previous Director of Nonprofit Organizations, and I quote here, "Chasing political nonprofits isn't the organization's primary function, nor one for which it is staffed." Thus, from a systems point of view, we have DOJ deferring for enforcement to an effectively toothless organization, with the predictable result that zero cases appear to have been brought. Indeed, as far as I know, not one person has been put before an investigative grand jury.

To make matters worse, the IRS has taken one of the clearer statutes passed by Congress and through its regulations has so defanged and confused the law as to make it virtually unenforceable by the agency. The IRS did this by saying that "exclusively"—the word in the statute—meant "primarily" by then accepting that "primarily" meant 51 percent, and further by pursuing a policy of conspicuous nonenforcement even of that watered-down standard.

If the IRS has affirmatively wished to defeat this law and permit rampant false statements to go unpunished, it could hardly have done a better job. As a Notre Dame law professor who specializes in this area has said, "the IRS seems to blink if you push them." And yet DOJ defers to the IRS.

The result is that statements that are plainly false by any common lay definition of the term "go unpunished." A clear congressional statute goes unenforced. An industry that launders immense amounts of anonymous money into our elections grows like a weed. And in politics, only the big donors and the candidates and their intermediaries know who is beholden to whom and for how much.

As Senator McCain and I pointed out in a brief to the Supreme Court recently, this latter condition is a prescription for corruption. As even the Supreme Court pointed out in *Citizens United*, it is

disclosure of donors' identities that allows "citizens to hold corporations and elected officials accountable for their positions and supporters" so that citizens can "see whether elected officials are in the pocket of so-called monied interests."

And, of course, under this regime, nothing prevents foreign interests from influencing American elections if there is no investigation and no enforcement of whose money is really hiding behind the nondisclosure provisions that gives Section 501(c)(4) its appeal to big donors.

The relevant federal IRS form includes Question 15, which asks, under penalty of perjury, "Has the organization spent or does it plan to spend any money attempting to influence the selection, nomination, election, or appointment of any person to any Federal, State, or local public office or to an office in any political organization?" In one investigation, ProPublica found 32 organizations that answered no to this question and then went out and spent money on political races. And that was out of 72 IRS filings they reviewed. Nearly half appear to be false. Some organizations had ads running on the day they mailed their filings in. Some had run them before. Many spent millions on political ads.

Looked at the other way, in the ProPublica investigation they found 104 organizations that told State or federal elections officials they had spent money on candidates' specific political ads, what the FEC called "electioneering communications." Thirty-two of those 104 had told the IRS they had spent no money to influence elections.

Even when information is provided, it may be false. One organization said it would spend 50 percent of its effort on a Web site and 30 percent on conferences. Investigations showed its Web site consistent of one photograph and one paragraph, and no sign of any conferences. The same group declared it would take contributions from individuals only and then took $2 million from PhRMA, the pharmaceutical lobby.

Another declared to the IRS that it spent $5 million on political activities, but told the FEC it has spent $19 million on political ads. Another pledged its political spending would be limited in amount and will not constitute the organizations primary purpose, and then went out and spent $70 million on ads and robo-calls in one election season.

And some never even apply. They just start spending and file a tax return after the fact, potentially as their last act before they disband so they are gone before the mail brings their filing to the IRS.

One never filed at all, even after the fact. No enforcement action has been taken as far as I know.

As Melanie Sloan, executive director of CREW, has said, "You can go into business and violate the law and then go out of business. And what is ever going to happen about that? There is no consequence."

Let me close on this issue by reading from an article describing the reaction of a State election official: "When ProPublica read the group's description of its activities on its IRS application to Ann Ravel, the chairwoman of the California Fair Elections Commis-

sion, she laughed. 'Wow,' she said, upon hearing that the group said it would not try to influence elections. 'That is simply false.'"

So this hearing is directed to the mechanisms and machinations by which such false statements are allowed to go unpunished. During this hearing we will also examine enforcement issues pertaining to coordination between candidates and outside groups where the FEC has so weakened the limitations as to make so-called independent expenditures functionally equivalent to campaign contributions, also the use of shell corporations to hide donor identities, and the risk of foreign money influencing our elections that comes with secret fundraising and spending by 501(c)(4)s and other groups.

I look forward to hearing from the witnesses on these and other issues. I see that Senator Cruz has joined us, and I invite him to make any opening statement he cares to make at this time.

Senator CRUZ. I am happy at this point just to hear from the witnesses.

Chairman WHITEHOUSE. Very good. Let me introduce both witnesses.

Mythili Raman is Acting Assistant Attorney General for the Criminal Division of the Department of Justice. In this role, Ms. Raman oversees nearly 600 attorneys who prosecute federal criminal cases across the country. Previously, Ms. Raman was the Principal Deputy Assistant Attorney General for the Criminal Division. Ms. Raman has been with the Department since 1996 and previously served as an Assistant United States Attorney in the U.S. Attorney's Office for the District of Maryland.

Patricia J. Haynes is the IRS Deputy Chief of Criminal Investigation. In this role, Ms. Haynes directs worldwide programs for investigating potential criminal violations of the Internal Revenue Code and related financial crimes. Previously, Ms. Haynes was the Executive Director of Investigative and Enforcement Operations, and before that Director of Field Operations for the Southeast Area. She began her career as a special agent in Virginia in 1983.

If I could ask the two witnesses to stand and be sworn, we will begin the hearing. Do you affirm that the testimony you are about to give before the Committee will be the truth, the whole truth, and nothing but the truth, so help you God?

Ms. RAMAN. I do.

Ms. HAYNES. I do.

Chairman WHITEHOUSE. Thank you very much.

Ms. Raman, welcome. We will begin with you. Thank you very much for being here on the part of the Department of Justice.

STATEMENT OF MYTHILI RAMAN, ACTING ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE, WASHINGTON, DC

Ms. RAMAN. Chairman Whitehouse and distinguished Members of the Subcommittee, thank you for——

Chairman WHITEHOUSE. Is your microphone on?

Ms. RAMAN. Let me start again.

Chairman WHITEHOUSE. Before you start again, let me just make clear that for those who have prepared testimony, your entire testimony will be included in the record. We do call on our witnesses

to restrict their presentations in terms of time here, but the full statement becomes a part of the record of the proceeding.

Again, Ms. Raman, thank you.

Ms. RAMAN. Thank you very much. Thank you, Chairman Whitehouse and distinguished Members of the Subcommittee. Thank you for inviting me here today to share the views of the Department of Justice on challenges to the criminal enforcement of our campaign finance laws posed by the growing activity of super PACs and certain 501(c) organizations. I am honored to represent the Department at this hearing and to have the opportunity to oversee the important work of the Criminal Division.

Protecting the integrity of our elections is one of the Department's most important tasks, and enforcement of our campaign finance laws is a top priority. There is no question that private contributions to political campaigns are a fundamental part of the electoral process and that, under the Constitution, the ability to make political contributions is a protected component of our citizens' political speech. At the same time, Congress and the federal courts have long recognized the importance of transparency and fairness in campaign finance to avoid any individual or entity exercising undue influence over our elections or over our elected officials.

The Justice Department is fully committed to investigating and prosecuting those who willfully violate the disclosure requirements and the contribution limits established by our campaign finance laws. Indeed, since 2010, we have successfully prosecuted more than a dozen cases involving campaign finance violations.

In the time since the Supreme Court's decision in *Citizens United* v. *FEC*, however, the manner in which individuals and entities raise and spend money in our elections has changed dramatically and continues to change. The two most important developments affecting our ability to enforce the campaign finance laws are the rise of super PACs and the growing political activity of certain types of organizations created under 501(c) of the Internal Revenue Code, such as 501(c)(4) social welfare groups.

We face certain investigative and prosecutorial challenges as a result of this new landscape. With regard to super PACs, the primary challenge we face is establishing illegal coordination between a super PAC and a campaign. As described more fully in my written testimony, as a result of certain FEC advisory opinions, regulations, and matters under review, we believe it will be exceedingly difficult for prosecutors to prove beyond a reasonable doubt whether and when super PACs and campaigns willfully engage in illegal coordination.

With regard to designated classes of 501(c) organizations, we are hampered by the fact that, unlike PACs, super PACs, and other political organizations, these 501(c)s are not required to publicly disclose their donors to the FEC even though those donors' contributions may be used as expenditures to seek to influence federal elections. Instead, 501(c) organization donors are disclosed only to the IRS as part of their tax returns, which can be filed a year or more after an election and are subject to the traditional restrictions on public disclosure imposed by our tax laws.

Thus, for example, a donor seeking to bribe a corrupt official could potentially use a 501(c) organization to hide his identity, and we would be unlikely to ever receive the warning signals we would need to investigate further.

Vigorous enforcement of our campaign finance laws is essential to preserving both the integrity of our elections and the public's confidence in these elections. The Justice Department's prosecutors and federal law enforcement agents work tirelessly to uncover, investigate, and prosecute campaign finance offenses. But the recent changes in our campaign finance laws have made it easier for individuals and entities to buy influence over elections and conceal their conduct. And our ability to successfully combat these threats is hindered by the current law regarding what constitutes coordination between super PACs and candidates and by the loss of transparency arising from the use of designated 501(c) organizations in connection with elections.

Despite these challenges, we are committed to vigorously rooting out corruption and ensuring the fairness of our elections through the robust enforcement of our campaign finance laws.

Thank you for the opportunity to appear before you, and I am pleased to answer any questions you may have.

[The prepared statement of Ms. Raman appears as a submission for the record.]

Chairman WHITEHOUSE. Thank you very much.

Ms. Haynes, welcome, and thank you for being here.

STATEMENT OF PATRICIA HAYNES, DEPUTY CHIEF, CRIMINAL INVESTIGATION, INTERNAL REVENUE SERVICE, WASHINGTON, DC

Ms. HAYNES. Thank you, Chairman Whitehouse and Members of the Subcommittee. My name is Patricia Haynes, and I am the Deputy Chief of IRS Criminal Investigation. Thank you for the opportunity to testify at this hearing on the criminal enforcement of our campaign finance laws.

My purpose here today is not to discuss the campaign finance laws themselves or how violations of those laws are prosecuted, which is not my area of expertise. Rather, I am here to explain how IRS Criminal Investigation helps to enforce the tax laws of the United States and specifically Internal Revenue Code Section 7206.

The mission of Criminal Investigation is to foster compliance in our tax system and compliance with the tax laws by investigating potential criminal violations of the Internal Revenue Code and related financial crimes. Criminal Investigation consists of approximately 2,400 special agents worldwide who investigate violations of the Tax Code as well as statutes related to money laundering and the Bank Secrecy Act. Criminal Investigation works closely with the Department of Justice and the United States Attorneys' Offices around the country to bring criminal offenders to justice. The work being done by our special agents is a critical component of the IRS' overall effort to encourage voluntary tax compliance.

Criminal tax enforcement is a crucial component of the IRS's overall effort to encourage voluntary compliance. Under IRS Code Section 7206, it is a felony to make false or fraudulent statements to the IRS or to file false or fraudulent returns or other documents

with the IRS. The most common prosecutions under this code section involve the underreporting of income or the fraudulent inflation of deductions on federal tax returns. But violations of 7206 may also be charged in cases involving other types of false statements made to the IRS on an array of IRS forms, applications, and schedules.

The government must prove four key elements in order for a return or statement to be deemed in violation of Section 7206: that the defendant making the statement declared it to be true; that the statement was materially false; that the defendant signed the statement willfully and with the knowledge that it was false; and that the statement was accompanied by a written declaration that it was made under the penalty of perjury.

Let me turn now to an explanation of how Criminal Investigation investigates potential tax law violations. In general, Criminal Investigation conducts two types of investigations. The first type, known as an administrative investigation, is worked outside of the grand jury process. An administrative investigation can be initiated when Criminal Investigation receives or develops information indicating possible violations of laws related to tax, money laundering, or bank secrecy. If a special agent determines that the information supports the potential for criminal prosecution, the special agent will launch an investigation to gather evidence, with the special agent involved using the broad spectrum of techniques available to him or her.

The second type of investigation arises when Criminal Investigation submits a request to the Justice Department to initiate a grand jury investigation either before, during, or after an administrative investigation. This type of investigation is initiated when the use of a grand jury would be more efficient or would strengthen the potential for prosecution.

At the conclusion of an administrative or grand jury investigation, IRS criminal tax counsel evaluates the evidence gathered and provides advice on whether to recommend prosecution by the Department of Justice.

Criminal Investigation also works with other law enforcement agencies that investigate campaign finance-related offenses. In the past, such cases have involved allegations of public corruption, improper use of campaign contributions, and the concealment of conduit or straw contributions.

Mr. Chairman, that concludes my testimony. Thank you again for the opportunity to appear before the Subcommittee and describe the role that IRS Criminal Investigation plays in helping enforce tax laws and campaign finance laws. I would be happy to answer any questions.

[The prepared statement of Ms. Haynes appears as a submission for the record.]

Chairman WHITEHOUSE. Thank you very much.

Let me begin first by thanking Ms. Raman and highlighting the point that she makes in her testimony that the current state of affairs impedes investigation into political corruption. That is a point that the Supreme Court has simply failed to address, both in *Citizens United* and in cases that followed. And it is a point that Senator McCain and I made in our brief to the U.S. Supreme Court,

and it is an area where I think they need to provide some attention.

But what I would like to focus on in my questions are some very specific acts that appear to be happening fairly frequently and that appear to be happening with impunity. The first is a violation of the false statements laws and specifically in response to this question on the IRS form: Has the organization spent or does it plan to spend any money attempting to influence the selection, nomination, election, or appointment of any person to any federal, State, or local public office? So that is one sort of fact pattern that I think is quite clear and relatively simple. We have numerous instances where the answer to that question was a plain no, and then very significant political activity was then accomplished by the entity that said that it would not do that. So that is one.

The second is the—I will just describe it. A super PAC has no ability to shield the identity of its donors. In fact, disclosure is part of the reason that there is a super PAC. And yet we often see—here we go—individuals or corporations, some anonymous entity, making a donation to what appears to be a completely shell corporation designed just for the purpose of laundering money into a super PAC and violating the law that would require disclosure of the true identity, which would seem to be a pretty clear 441(f) violation, making a contribution in the name of another. And I am wondering why it is that the Justice Department does not appear to bring any of those cases, and I think the immediate answer to that question—you can correct me if I am wrong—but I think the immediate answer to that question is that it is because you defer to the IRS to bring those cases to the Department, because they come out of the tax world, and I do not know why particularly the false statements—let me focus on that because that comes off the IRS report.

I can see why the Department of Justice would want to defer to the IRS on criminal prosecutions involving complex tax matters. Making a false statement is something the Department prosecutes all the time. It does not take particular tax expertise to recognize a false statement when you see one or to prosecute one when you see one. What are the inhibiting factors that prevent DOJ from going forward? Are you rethinking deferring so much to the IRS in these matters where it is not a tax-specific underlying issue and is something as simple as making a false statement? And are you satisfied with the state of play right now with the lack of prosecution in this area?

Ms. RAMAN. Thank you, Senator Whitehouse, for asking those questions. I should start by saying 18 U.S.C. 1001 is a bread-and-butter statute that we use in our corruption cases and our fraud cases. It is an important statute. It is one of the best ways for us to get to the heart of cases involving people who are trying to defraud the United States or lie to an agency of the United States. So we fully embrace and understand the importance of robust enforcement of 1001 in appropriate circumstances.

Chairman WHITEHOUSE. But I am correct that no 1001 cases have been brought about Question 15 and the answers to it that appear to be false?

Ms. RAMAN. And you have highlighted, I think, some of the problems that we have encountered, particularly in the last several years, regarding how to get to the bottom of some of the activities in the flow of money that goes through 501(c)(4)s and super PACs.

One of your charts described a scenario in which an anonymous donor provides money to a shell company and then contributes to a super PAC. That is, in fact, something we could and would prosecute under 441(f).

Chairman WHITEHOUSE. But have not.

Ms. RAMAN. Not yet. Without discussing ongoing investigations, we can assure you that we are incredibly vigilant about the use of these organizations as an end run around contribution limits.

Chairman WHITEHOUSE. Well, I fully respect the constraints, particularly if a grand jury will succeed, that you cannot discuss ongoing investigations and you cannot discuss matters that are before a grand jury. But I believe it is perfectly legitimate to say whether a category of offense is being prosecuted or not anywhere in the Department and whether or not the Department has grand jury investigations addressing a category of offense underway without going into the details of who or where. And as I understand it, there is no activity at this point within the Department of Justice either on false statements made in response to Question 15 or under 441(f) for the shell identity laundering into a super PAC.

Ms. RAMAN. Well, I actually cannot comment on any ongoing grand jury matters, but setting that aside, I do want to assure you, Senator Whitehouse, that——

Chairman WHITEHOUSE. Can I infer from that that there actually is a grand jury matter that might be going on? Or can you not even say that?

Ms. RAMAN. I would not want to tell you that.

Chairman WHITEHOUSE. OK. So as far as I can know, there is zero activity.

Ms. RAMAN. And I do want to assure you, Senator Whitehouse, that our Public Integrity Section within the Criminal Division and the 94 U.S. Attorneys' Offices are focused on these kinds of activities.

441(f) is a statute that our Public Integrity Section has used repeatedly over the last several years. We used it prior to *Citizens United*, 441(f), in the context of conduit contributions where essentially people were using shell donors or straw donors to funnel money to candidates. Post-*Citizens United*, those people do not need to use those kinds of conduit schemes anymore. They simply donate directly to a super PAC because there are no limits on independent expenditures. So——

Chairman WHITEHOUSE. Unless they want to hide their identity, and then they do the shell corporation thing. And if that is a 441(f) case, I would think that that is something that could be brought. There is nothing that would legally inhibit bringing a 441(f) prosecution in a fact pattern in which a donor creates a shell corporation exclusively for the purpose of hiding their identity and then has the shell corporation, which they control and which is for the exclusive purpose of hiding their identity, make their contribution in its name to a super PAC. Correct?

Ms. RAMAN. I absolutely agree.

Chairman WHITEHOUSE. Okay. Senator Cruz.

Senator CRUZ. Thank you, Mr. Chairman. I want to thank both of the witnesses for joining us this morning.

In my view, whenever Congress acts in the area of political speech, the touchstone for everything we do should be the First Amendment to the Constitution. And I think that the public should be particularly skeptical when you have elected politicians of either party enacting rules limiting the ability of public citizens to criticize the behavior of their elected officials.

In my view, the First Amendment was created precisely to ensure that the citizens could speak without the men and women who sit in this body restricting what they say. And I think there are few areas that are more dangerous to have the government engaged in prior restraint or punishment after the fact for private citizens who would choose to speak out on politics.

Indeed, of all the areas of speech—we have long lines of cases extending free speech protections to all sorts of questionable activities, including things like nude dancing—and that is a well-established line of cases from the Supreme Court. But of every possible area of speech, I think there is none more central to the core purposes of the First Amendment than political speech, than the ability of every American to speak up and express his or her views on the direction of this country.

And I would point out that in saying this, I am not unfamiliar with the downsides. In Texas, I just came through a campaign where I was on the receiving end of $35 million in attack ads and was outspent 3:1. And let me say those who chose to put resources into launching attacks against me had a First Amendment right to do so, and God bless them for speaking out and being involved in politics. And I think we should all be concerned about those who are elected to office and immediately want to prevent anyone from speaking and being engaged in the political process or saying something they do not like.

Now, Ms. Raman, I would like to ask you a few questions about your testimony. The first thing I would like to ask is: In the Department of Justice's opinion, what is the government interest in regulating the independent expenditures of private citizens?

Ms. RAMAN. Well, we obviously understand——

Chairman WHITEHOUSE. I think your microphone need to come on.

Ms. RAMAN. I am sorry. We understand fully the holdings of the Supreme Court in this area, and we are not suggesting regulation of independent expenditures. Our challenge as corruption prosecutors is something altogether different. Our challenge as corruption prosecutors is to be able to understand when those independent expenditures really are not independent, where there is the kind of illegal coordination such that the expenditures become contributions and become an end run around the contribution limits that have long been recognized by both Congress and courts around the country. And that is our concern. We want to be able to have the tools that we have always had to be able to follow the trail of money, to be able to follow the paper trail, to be able to determine whether there are bad actors who are illegally trying to influence our elected officials by providing donations to the PACs that are il-

legally coordinating with the campaign. And that is our challenge now. It is simply a different challenge post-*Citizens United*.

Senator CRUZ. Ms. Raman, I want to make sure I understand your answer. If I understood you correctly, you said that the government interest was in investigating and/or prosecuting expenditures that were not independent, that were coordinated directly with a candidate or a campaign. Is it fair, then, to infer that the answer to the question I asked about does the Justice Department—is there a government interest in regulating independent expenditures, in other words, those expenditures that are not coordinated, is it fair to infer that your statement is there is not a government interest? Or is there a government interest? I do not want to put words in your mouth, so I would like to know what the Department's view is.

Ms. RAMAN. Well, I am not going to speak holistically for every circumstance in which there may be some law or regulation passed that may be viewed as affecting independent expenditures. But I am here to tell you that our primary purpose is to ensure that our campaign contribution limits are robustly enforced, and we are hampered from doing that now given that we simply do not have the tools that we used to have to determine whether or not super PACs are illegally coordinating with campaigns.

Senator CRUZ. But today the Justice Department is not articulating any government interest in regulating independent expenditures of private citizens. Is that correct?

Ms. RAMAN. Today I am here to tell you that our interest is twofold: One, we want clear and common-sense understanding of what coordination is so that we can do our job as robustly as we have been able to; and, number two, we need transparency in the way our campaign finance system works, so that if a donor is, in fact, using an organization like a 501(c)(4) to hide his identity, that we somehow be able to get that information.

Senator CRUZ. Let me focus on the second part of your answer there. You said that the Department has an interest in transparency. Does the Department have a view on whether the First Amendment protects a right to anonymous speech?

Ms. RAMAN. Again, I cannot get into every hypothetical in which we might have some interest in talking about anonymous speech. And I am certainly not here to suggest that our goal is to impede a lawful ability of individuals to speak on behalf of——

Senator CRUZ. Ms. Raman, I am asking what I think should be a fairly straightforward question. The Department is testifying today in support of legislation forcing disclosure of political speech, and my question is: Does the Department believe the First Amendment protects a right to anonymous speech? That is a question that goes right to the heart of your testimony.

Ms. RAMAN. I think, Senator Cruz, more important than what the Justice Department thinks, *Citizens United*, the Supreme Court upheld a disclosure regime and found it fully consistent with the First Amendment. And we believe that the kind of disclosure regime that the Supreme Court upheld in *Citizens United* is critical to our ability to continue to understand——

Senator CRUZ. Does the Department think it would be permissible under the Constitution for the Federal Government to require the NAACP to disclose a list of all of its members?

Ms. RAMAN. I am certainly not here to suggest that that is what we are asking for.

Senator CRUZ. I mean, as you know, the Supreme Court held that cannot be required.

Ms. RAMAN. And, Senator Cruz, I am certainly not here to suggest otherwise. What I am suggesting is that there is a risk that we have seen of bad actors using the anonymity that is given to them when they donate to 501(c)(4)s to hide the true purpose of their donation. And we need to be vigilant about that. We need to be able to determine when those donors are acting with bad intent and, frankly, when a campaign or an elected official may be knowingly allowing that kind of donation to occur intending to be influenced in some corrupt way. That is our job. We need to ensure that we are robustly and vigorously enforcing Title 2, the campaign finance laws, but also that we vigorously enforce our corruption laws. And it is not—it has certainly been the case that we have had several cases in which campaign contributions are, in fact, part of the quid pro quo that goes to the heart of a bribery case.

Senator CRUZ. Okay. Thank you very much. I appreciate your being here this morning.

Ms. RAMAN. Thank you.

Chairman WHITEHOUSE. Well, first, let me thank my friend Senator Cruz for bringing new dancing into what was a very dry and technical hearing.

[Laughter.]

Chairman WHITEHOUSE. That is going to raise the profile of this hearing quite a lot.

I wanted to just follow up. There is nothing in the First Amendment that would protect threatening or corrupt speech, even if it is anonymous.

Ms. RAMAN. That is right.

Chairman WHITEHOUSE. And there is nothing in the First Amendment that protects false statements and the prosecution of false statements when provided under penalty of perjury.

Ms. RAMAN. Of course not.

Chairman WHITEHOUSE. And there is nothing in the First Amendment that protects anybody's right to violate disclosure laws through a shell corporation.

Ms. RAMAN. No.

Chairman WHITEHOUSE. And that so far has been the focus. Let me ask Ms. Haynes a question. This is an issue where there is obviously often partisan disagreement, but we have some interesting partisan agreement among the witnesses who will follow, which is that, as professional as your organization is, you are not well suited to doing this particular work. Mr. Noble says it does not appear there is any effort to target donors to super PACs who use front organizations; there appears to be little effort being given to making sure politically active groups claiming 501(c)(4) status are complying with the law; it appears that the agency rarely challenges a group's 501(c)(4) designation based on political activity; and ultimately it does not appear that the law is being enforced.

Mr. Smith says that this is a mission for which the IRS lacks knowledge and expertise and which is tangential to its core responsibilities, the Service has long been particularly prickly about being dragged into political wars, and the agency, "is not equipped or structured to do the job it was asked to do."

Let me ask both of you: Does it make sense to have the IRS right now get from the Department of Justice the deference that it does with respect to those two narrow particular kinds of cases—the false statement case under Question 15, or the 441(f) case in which you have a clear shell corporation manufactured for the purpose of violating a disclosure law? I do not believe—I asked Ms. Raman this question—that the Department of Justice has ever made a case or is even investigating any case in either of those areas. I do not know if the IRS is either. If you are not, is that a signal that maybe DOJ's policy of deference to the IRS in this particular set of areas, which are not tax-law specific, have nothing to do with understanding the Tax Code, and are all about false statement and shell corporation behavior, which is, as Ms. Raman pointed out, frequent in many areas of criminal behavior, whether that should be rethought and whether you are confident that the IRS is doing a good enough job on its own and making adequate referrals?

Ms. HAYNES. Well, Senator, I can say that the IRS Criminal Investigation has been involved in violations of campaign finance laws using the statutes that we have. In fact, one of the cases that we were involved in was mentioned in Ms. Raman's written testimony out of New Jersey.

Chairman WHITEHOUSE. A straw donor case.

Ms. HAYNES. Pardon me?

Chairman WHITEHOUSE. A straw donor case.

Ms. HAYNES. Yes. Yes, it was.

Chairman WHITEHOUSE. But not one of these shell corporation to super PAC cases. There has never been one of those done.

Ms. HAYNES. I do not have any information that I can share on any case like that.

Chairman WHITEHOUSE. Nor a false statement in answer to the no on Question 15 and then subsequent immense political activity.

Ms. HAYNES. I do not have any information I can share on a 501(c)(4)-related false statement case, you are correct. But IRS is still engaged in these types of investigations.

In the course of a criminal investigation, the special agents gather all the facts and circumstances and make a recommendation based on what they feel has the strongest likelihood of prosecution, whether that is a 7206 charge or a 7212(a) charge, as was in the prior case that I mentioned. That recommendation is reviewed by our criminal tax counsel and then ultimately when it is referred to the Department of Justice, the discretion lies with the prosecutor on what violations to charge.

So IRS is involved in these types of cases. It is just that we have not had one that I can speak of with that particular charge.

Chairman WHITEHOUSE. Well, I guess under the circumstance of the testimony that we have from the subsequent panel on what we have today, I would urge that the Department and the Service get together and rethink whether in these two specific areas, which I think bear little resemblance to traditional tax violations and are,

in fact, very, as I think you used the words, "plain vanilla" criminal cases, whether or not that deference to the IRS is actually serving the public interest at this point, or whether the Department could not proceed to investigate, empanel grand juries, bring people before them, generate evidence, and put together a criminal case showing a fairly straightforward false statement or a fairly straightforward shell corporation disclosure violation. And I do not need you to answer that right now because I know that question is going to be answered, if it is answered at all, by people above you in both organizations. But I would ask you to take that away from this hearing.

Ms. HAYNES. Sure, Senator.

Chairman WHITEHOUSE. I had another round. Senator Cruz, you are welcome to another round.

Senator CRUZ. Thank you, Mr. Chairman.

Ms. Haynes, does the IRS have any position on whether additional campaign finance legislation should be passed by Congress?

Ms. HAYNES. Senator, I do not have an official position on that matter. I leave those decisions up to our criminal tax counsel or our tax counsel in the Department of Treasury to establish those types of regulations or improvements.

Senator CRUZ. Thank you.

Ms. Raman, I would like to go back to the conversation we were having a few minutes ago and understand, as best I can, the Department's position with regard to the constitutional protections on independent expenditures by private citizens.

As I understood our discussion, the principal basis you were pointing to additional disclosure requirements on private political activity is that that transparency would aid in discovering if there is corruption or bribery. Am I understanding you correctly?

Ms. RAMAN. Corruption and bribery, and if there are other violations of our campaign contribution limits.

Senator CRUZ. Now, you would certainly agree that there are limits—and I would think significant limits—to the theory that additional government information would be helpful for discovering crime, that that is a theory that has the potential to require government disclosure of virtually everything. And I am sure you would agree there are limits to that theory.

Ms. RAMAN. Of course, and we obviously just want a reasonable disclosure regime that balances the need for people to speak freely and have their voices heard in the political arena while still assuring us that we are able to combat both corruption and the appearance of corruption.

Senator CRUZ. Now, when I asked about a constitutional right to anonymous speech, you made reference to Supreme Court decisions. Does the Department of Justice maintain that the Supreme Court has been wrong in concluding that there is a First Amendment right to anonymous speech?

Ms. RAMAN. It is not the government's position to second-guess the Supreme Court. I am here, however, to clearly describe what some of our challenges are in light of *Citizens United*. Obviously, the government took a particular position before the Supreme Court in *Citizens United*, but now we have a law, and we intend to follow it.

That having been said, there are real challenges. There are real challenges to our ability to enforce the campaign contribution laws, and there are real challenges to our ability to determine when and whether there is the type of corruption that is rooted in campaign contributions in exchange for official acts.

Senator CRUZ. Well, and I think everyone on both sides of the aisle would agree that preventing corruption and preventing bribery is an important governmental interest and deserves serious focus. You mentioned, though, in your prepared testimony that you were concerned also not just about corruption and bribery but what you characterized as "undue influence." And I guess I have a little bit of difficulty understanding what "undue influence" means, because if it is not corruption or bribery, which is a very different thing, it strikes me that the citizens are due all the influence they can get in a democratic process.

So I am curious what you mean by "undue influence," if it is any different from corruption or bribery.

Ms. RAMAN. I do not think I intend to suggest that it is something different from illegal acts such as corruption or bribery or extortion by officials. What it does—what it is that—I am focusing, however, on the fact that undue influence often translates into those kinds of activities. I think it is axiomatic that contributions lead to influence, and the larger the contribution, the larger the influence. And we have seen in certain of our corruption cases that public officials succumb to that influence and agree to take official acts in exchange for campaign contributions. And we just want to be vigilant about ensuring that we can get to the heart of those kinds of cases when and if we encounter them.

Senator CRUZ. Well, but the Supreme Court has certainly recognized a distinction between contributions and independent expenditures, and there are a great many organizations on the left and on the right that devote real resources to try to convince their fellow citizens that they are right on particular issues of public importance.

I assume it is not, for example, the Department of Justice's position that a group like the Sierra Club exercises undue influence. Am I right in that?

Ms. RAMAN. And, again, Senator Cruz, I want to be absolutely clear. My concern is not about any one particular group or about undue influence in and of itself. What I am concerned about is that, given the rise of super PACs, our ability to understand when there is the type of coordination that causes an expenditure to become a contribution and that contribution is over the contribution limits that have long been established by Congress, that we want to be able to get to that, get to the bottom of that.

Senator CRUZ. So is it right, then, that to get to the bottom of it the Department would like to know every political contribution made to every private group? Again, I do not want to put words in your mouth, so I am trying to understand what your testimony is.

Ms. RAMAN. There are two things that would aid us as prosecutors: greater transparency in general, and we are happy to work with Congress or your staffs to talk further about the particulars; number two, a more common-sense understanding and definition

about what constitutes coordination. And those two things would assist us as prosecutors in being able to continue to do the jobs that we have always done in terms of rooting out corruption.

Senator CRUZ. You know, we have seen in recent news reports instances of bribery and corruption of public officials receiving bribes. I think one, it was alleged, received a bribe in a box of Cheerios. Another public official recently was alleged to have kept a bribe in his freezer. So corruption is a real problem. But I think it is qualitatively different from regulating the efforts of private citizens to speak out in the political process. And I will make clear at least my views. I asked about the Sierra Club, and I can happily say, no, I do not think they exercise undue influence. I do not think Planned Parenthood exercises undue influence. I do not think the unions exercise undue influence. I do not think the NRA exercises undue influence. I think every one of them has a constitutional right to speak out in a democracy. I think their members care passionately about the values they are espousing, and that is the way our system is supposed to work. And I think we should be very cautious about the Federal Government restricting the ability of private citizens to express their views on the direction of our country.

Thank you.

Chairman WHITEHOUSE. If I might add, because I think Senator Cruz makes a very good point, and I would want the record of the hearing to reflect that I think we have agreement amongst everyone that it is never the government's position or proper role to determine based on the amount of influence that a political group or interest or individual has that they have too much. That is a role, I think, for the voters to determine. And in that regard, I think it is important that the record of the hearing reflect that it is not just corruption and bribery that are of concern in this area, but as the Supreme Court has clearly established, making sure that citizens are informed is an important public goal, as the Supreme Court said, to hold corporations and elected officials accountable for their positions and supporters so citizens can see whether elected officials are "in the pocket of so-called monied interests." And to the extent that there are laws that provide that disclosure, I think the government then does have an interest, if it not to be made a mockery, in enforcing the laws that we have created for that disclosure. And clearly there are appropriate limits on that, but I think that disclosure is an important element in this discussion.

And, with that, I will release these two witnesses. Let me thank you both for the work you do on behalf of the people of the United States. I spent four years as a United States Attorney and had great pride and satisfaction in working with people at the Department of Justice and Main Justice and with the IRS criminal investigative agents. You do great work, and I am glad you came here today, and I thank you.

Ms. RAMAN. Thank you.

Ms. HAYNES. Thank you.

Chairman WHITEHOUSE. We will take about a two- or three-minute break while the room gets reset for the second panel of witnesses and come back into session in just a moment.

[Pause.]

Chairman WHITEHOUSE. If the witnesses are present, can I ask them to take their seats and we can proceed with the remainder of the hearing?

Well, we are awaiting the arrival of Mr. Colvin, who I understand has been seen and must be nearby, so we will have him here in a moment. Indeed, here comes somebody with a determined approach to the chair. There we go. Thank you very much.

Let me introduce the witnesses and then have them sworn and then ask you each to make your statements.

First, on our left, on the witnesses' right, is Lawrence M. Noble. He is the president and CEO of Americans for Campaign Reform, which is a nonpartisan organization supporting public funding for federal election. He is also an adjunct professor at the George Washington University Law School, where he teaches campaign finance law. Previously, Mr. Noble served for 13 years as the general counsel for the Federal Election Commission.

Our second witness, front and center, is Gregory L. Colvin. He is chairman of the board of Adler & Colvin, a San Francisco law firm that specializes in representing nonprofit organizations and their donors. Mr. Colvin has written widely on the political activities of tax-exempt organizations. From 1991 to 2009, he served as co-chair of the Subcommittee on Political and Lobbying Organizations and Activities of the Exempt Organizations Committee of the ABA Tax Section.

And furthest to my right is Bradley A. Smith, a professor of law at Capital University Law School in Columbus, Ohio, and founder and chairman of the Center for Competitive Politics. Mr. Smith served as a Commissioner on the Federal Election Commission from 2000 to 2005, including service as its Chairman in 2004.

I welcome all the witnesses and ask if you would please stand and be sworn. Do you affirm that the testimony you are about to give before the Committee will be the truth, the whole truth, and nothing but the truth, so help you God?

Mr. NOBLE. I do.

Mr. COLVIN. I do.

Mr. SMITH. I do.

Chairman WHITEHOUSE. Thank you very much, and please be seated.

Mr. Noble, we begin with you. Thank you very much for being here.

STATEMENT OF LAWRENCE M. NOBLE, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AMERICANS FOR CAMPAIGN REFORM, WASHINGTON, DC

Mr. NOBLE. Thank you. Chairman Whitehouse, Senator Cruz, I want to thank you for inviting me to testify at this Committee on this very important issue of the enforcement of the campaign finance laws.

It is estimated that over $6 billion, well over $6 billion, was spent on the last elections, with so-called independent groups—that is the super PACs, the 501(c)(4) organizations, and the others—spending somewhere around $1 billion, or at least that was what was reported. We also know that a tremendous amount of the money was not reported.

So we have a situation here now where our elections are being funded by these independent groups, which is constitutional, but there are also laws surrounding how those groups should operate, and those are not being followed.

Many point to the Supreme Court's decision in *Citizens United* and other decisions as saying it has hampered the ability of the Department of Justice, the Federal Election Commission, and the IRS to enforce the laws. And that is true. In some ways it has. The Supreme Court has recognized the constitutional right to make independent expenditures by individuals and corporations.

But that overstates the case, because those who say that often say that, well, there is no point in trying to do anything, there is no point trying to do any reform because the power of corporations, unions, wealthy individuals cannot be effective under what the Supreme Court has said.

But the reality is that the FEC—the Federal Election Commission—the IRS, and the Department of Justice are not enforcing the laws on the books. And if they would enforce the laws on the books, a number of the issues that we have would go away or at least would be more manageable.

First of all, super PACs are required to report their donors, as has been discussed. They are political action committees. It seems logical that if they are required to report their donors, they should actually report the person who really gives to them. And, therefore, you should have a law, it would seem, that would prevent somebody from giving through a straw donor to a super PAC to hide their identity. That is logic. And, fortunately, there is such a law, and that is 2 U.S.C. Section 441(f), which allows the government to prosecute the giver, the intermediary organization, and the super PAC if they knowingly give money. Through that intermediary organization, the super PAC knows about it for the purpose of hiding the identity of the donor. That is illegal right now. That is not being prosecuted.

Even beyond super PACs, 501(c)(4) organizations do not have to report their donors. That is absolutely true. But if they make independent expenditures, they do have to report. And they have to report anybody who gives over $200 for the purpose of furthering an independent expenditure. That would sound like if I gave to a 501(c)(4) organization and said, "Here is money to make independent expenditures," my name would be reported. It is not happening. Why? Because FEC Commissioners have determined or some have determined that unless you give for a specific ad, you do not have to be disclosed. It is very difficult to prove anybody has given for a specific ad.

Beyond that, any organization, whether it is a 501(c)(4) or a 501(c)(3), any organization or any group of persons that makes expenditures over $1,000 and has as its major purpose political activity, federal election activity, has to report as a political committee, report all of its donors. That is the current law.

Given the statements made by many of the 501(c)(4) organizations, given what we know about their funding, it is hard to see how there is at least not an investigation as into why some of these are not political committees. But the Federal Election Commission has basically given up on trying to define what is a political com-

mittee because of a dispute on the Commission or enforcing any group to report as a political committee if it decides not to.

As to the coordination issue, this is an area where reality and the law have separated. Under the law, these expenditures are allowed because they are independent. The Supreme Court said very explicitly, the constitutional right for an independent expenditure comes from the fact that, because it is independent, it could hurt the candidate as well as help the candidate, and there is virtually no chance of a quid pro quo or any potential corruption because of that separation.

Put that statement up against what we saw in the last election, where candidates have their own super PACs, raise funds for their own super PACs, call them their super PACs. Their staff, their former staff go to work on those super PACs, and it is not surprising that neither the candidates, the public, or anybody else seems to think that these are truly independent organizations. So they are not independent organizations.

Why is this happening? Because the FEC, the Federal Election Commission, is not enforcing the law on the books; the Department of Justice is not independently enforcing the law on the books; and as was discussed in the previous panel, the IRS is not taking a serious look at what these 501(c)(4) organizations are doing.

Thank you.

[The prepared statement of Mr. Noble appears as a submission for the record.]

Chairman WHITEHOUSE. Thank you very much, Mr. Noble.

Mr. Colvin, welcome. Please proceed. You need to turn on your microphone, sir.

STATEMENT OF GREGORY L. COLVIN, PRINCIPAL, ADLER & COLVIN, SAN FRANCISCO, CALIFORNIA

Mr. COLVIN. Good morning, Senators. I appreciate the chance to come before you and address the question why we have seen so little enforcement—civil or criminal—of the federal tax laws that apply to political activities of 501(c)(4) organizations.

My law firm represents a broad range of nonprofits and their donors. For 35 years, I have formed tax-exempt organizations, including (c)(4)s, and advised them on their political activities.

Why is the IRS in the business of enforcing political rules? You see, every person, every entity, in the country has a federal tax life. It must pay tax on its income unless it is exempt by statute. The only entity allowed to have a primary political purpose is a 527 organization; it has a partial tax exemption and must disclose its donors over $200. All other tax-exempts must have a primary purpose that does not include politics. Therefore, the IRS cannot avoid the law enforcement duty to, one, qualitatively define political activity and, two, quantitatively determine what is too much to keep your exemption.

The annual Form 990 has a question under penalty of perjury: "Did the organization engage in direct or indirect political campaign activities on behalf of or in opposition to candidates for public office?" If you answer yes, you must report the amount spent, the number of volunteer hours, and describe what you did.

There is, though, a fundamental problem affecting enforcement on 501(c)(4) nonprofits. The tax rules are vague, unpredictable, and unevenly applied. Only the most flagrant violations could be knowing, willful, or deliberate and subject to criminal prosecution.

What is political intervention? The IRS interpretation must be gleaned from a few old cases and rulings, internal training materials, and a few bursts of guidance from the last decade. The IRS insists on using an open-ended "facts and circumstances" approach rather than drawing bright lines. Political intervention under tax law is more than express advocacy under election law, we are told, but what is it? Reasonable minds could differ, and they do.

How much political intervention is too much for a tax-exempt (c)(4)? Its primary operations must promote social welfare—"the common good" of the community. The IRS, therefore, deduces that non-qualifying activities must be "less than primary."

While the Service has never pinned this down to an annual level of expenditures, it has tacitly accepted 49 percent as a defensible figure. Yet because of the IRS "facts and circumstances" approach, we can never be sure. So,the speech of some (c)(4) groups is chilled. They avoid the risk and stay far below the 49 percent level, while their adversaries may go right up to the edge.

Two things I want to say about the focus of this hearing on (c)(4)s: First of all, there are well over 100,000 registered with the IRS. They include well-known organizations such as Rotary, Kiwanis, and the Disabled American Veterans, as well as Sierra Club and the NRA. Most are highly reputable and do very little or no political activity. They do not present a law enforcement problem.

Second, enforcing these tax laws is not limited to the (c)(4) class. The vagueness of these rules affects (c)(3) charities, (c)(5) unions, and (c)(6) trade associations that have the same primary purpose rule.

Here is the most difficult political tax law enforcement problem: What is the difference between a political campaign ad and an issue ad that names a candidate, says something good or bad about them, and tells the viewer to contact the candidate about the issue?

BCRA in 2002 required disclosure to the FEC of spending on "electioneering communications," defined basically as paid advertising that names a candidate and is broadcast within 30 or 60 days before an election. The IRS went in a different direction. It issued Revenue Ruling 2004–6, listing a series of six bad factors and five good factors by which to judge "advocacy communications." Then three years later, it issued Ruling 2007–41, with a seven-factor test on issue advocacy. The two multifactor tests are not the same. Neither of them applies directly to the key question in this hearing: What political speech by a (c)(4) would count against its exemption?

So how can a lawyer advise his or her client, how can a prosecutor evaluate a case, in which a (c)(4) denies it will engage in candidate politics on its federal tax form, and on the same day in March it broadcasts a TV ad praising a Senator who is up for reelection in November?

Under the seven-factor IRS test, three factors look bad: It names a candidate, expresses approval, and is not connected to an event

such as a vote on legislation. But three factors look good: The election is still eight months away, the ad makes no reference to the election or voting, and it mentions no "wedge" issues separating the candidates. What if the ad is targeted to a battleground State? Targeting is a factor in one ruling but not the other.

With this kind of vague, uncertain, multifactor approach, the (c)(4) can find a reputable lawyer to advise that the ad is not political intervention under the IRS tests. Therefore, an officer of the (c)(4) entity can sign a tax return believing that it is true and correct.

I want to conclude by suggesting that the IRS itself can solve both the qualitative and quantitative problems.

The IRS and Treasury could establish a regulatory project to define bright lines for political intervention. I chair a drafting committee of the Bright Lines Project, sponsored by Public Citizen, which is attempting to do exactly that.

Finally, the IRS could reconsider its position on the "less than primary" ceiling for (c)(4)s, (5)s, and (6)s. It could establish a percentage, at 10 percent, as an insubstantial level of political activity.

These reforms would go a long way toward restoring public confidence in the tax-exempt universe.

Thank you.

[The prepared statement of Mr. Colvin appears as a submission for the record.]

Chairman WHITEHOUSE. Thank you, Mr. Colvin.

And now we—I do not know if it is appropriate to call you "Commissioner Smith" still? Does the title stick with you after you are gone. "Mr. Smith," in any event. We will go that way. Mr. Smith, welcome.

STATEMENT OF BRADLEY A. SMITH, CHAIRMAN, CENTER FOR COMPETITIVE POLITICS, JOSIAH H. BLACKMORE II/SHIRLEY M. NAULT PROFESSOR OF LAW, CAPITAL UNIVERSITY LAW SCHOOL, COLUMBUS, OHIO

Mr. SMITH. Thank you, Chairman Whitehouse and Senator Cruz. Thank you for inviting me to testify today.

I want to actually be the one who challenges some of the assumptions that have underlaid this hearing. For example, it was said at the beginning that there are massive amounts of money flooding into the system because of *Citizens United*. It is true, for example, that spending in 2012 was up about 37, 35 percent from 2008. But between 2008 and 2004, spending rose by about 30 percent. Spending has gone up in every Presidential election in my lifetime, usually by a substantial amount. And to suggest that this is the consequence of one decision I think is incorrect.

In fact, when we look at the numbers, it appears that at an absolute maximum, about five percent of the spending came from corporations, for-profit corporations, and we get there only by suggesting that everything nonprofits spent, (c)(4)s spent, was from corporations. And we know that that is not true. We know that much of that came from unions, and much of it came from other individuals and so on.

Second, I do not agree that there is a huge crisis of enforcement here. For example, we talk about the disclosure aspect. That has

gotten a lot of attention today. In fact, it appears that about five percent of political spending in the last election went "undisclosed." Okay? Now, $380 million sounds like a lot; five percent does not sound like maybe it is such a dominant problem in American politics. And even that overstates it. Much of that spending was, in fact, done directly by groups that are well known to the public. If we are trying to inform the public, I think most people know what the agenda of the Chamber of Commerce is, or most people know what the agenda of most of the types of groups that were giving happen to be.

We have talked some about shell corporations. You know, people go over these super PAC contribution lists and in great detail. That is what CREW exists to do and so do some of these other groups. And to my knowledge—I may have missed one or two, but to my knowledge there have been two recorded episodes of "shell corporations." In both cases, it was revealed within a matter of hours, if not days at the most, who was the spender behind those shell corporations. And as has been pointed out, that activity is probably already illegal, although the people did not seem to recognize it because so many people have been going around suggesting that, in fact, you could use shell corporations in this way.

Next I want to address the issue of shifting enforcement to other agencies than the FEC, which has been the big creature here in the room. It kind of surprised me to hear all this talk about should the IRS be enforcing campaign finance laws and so on. Much of what is talked about and complained about with the FEC is not a bug. It truly is a feature. People complain all the time: "Well, the FEC is prone to gridlock. It is 3–3." Actually, it does not deadlock very much 3–3. When it does, that usually decides the issue. But beyond that, it is designed that way intentionally so that one party cannot take over the political system and ram things through on a 3–2 vote of Commissioners. That is precisely what Congress said we were not going to have, and I do not think there is any Member of this chamber who would be willing to stand on the floor and say, "I am willing to give the opposition party the ability to decide who speaks when on politics without input from my party." I do not think any Member of this chamber would do that.

We need to recognize as well, for example, on coordination, the rules are complex and it is hard to prove coordination. But that is as well a design, because coordination investigations are extremely sensitive. I can guarantee—well, I cannot guarantee, but I am pretty sure—that at some point in the next 30 days, you know, all the Senators here are likely to meet with somebody who is from a super PAC, an interest group, a union, a trade association, right? At this point, if it is a coordination investigation, we should then be able to investigate that meeting. Who knows what they talked about? Maybe if that trade association or union did any election expenditures, maybe it was coordinated. And this is what we find with these coordinated hearings. They are extremely intrusive into political strategy, into political tactics, and into the ongoing goals and efforts that folks made.

So I want to conclude by suggesting that we need to be very careful about trying to get aggressive enforcement out of Justice. We have seen that in the past. We have seen that at the IRS in the

past. The IRS for many years, under pretty much every President up through Richard Nixon, of both parties, was used for political purposes. And for that reason it has sought hard to stay out of politics, and now Congress is trying to drag it back in as a campaign enforcement mechanism because it is unhappy with the fact that the FEC is set up to guarantee a bipartisan regime.

I am going to suggest here that if you really want to shatter confidence in government, if you really want to build this trust, if you want to create the appearance of corruption, then what you ought to do is use a straight party-line political vote, either in this Congress or at the administrative agencies that have party-line majorities, and use that vote to attack the other side politically with no bipartisan support. I can think of nothing more that would shatter public confidence in government and the impartiality of the government agencies, including Justice and the IRS, than taking that approach.

Thank you very much.

[The prepared statement of Mr. Smith appears as a submission for the record.]

Chairman WHITEHOUSE. Would that apply to the Supreme Court and the 5–4 decision with the Republican judges all holding with no support from the minority?

Mr. SMITH. I am not sure how that actually relates to the question, but I guess I would say that, no, I do not think that holds there at all. I do not think the judges are sitting in partisan roles, and they are not running for election, and they are not worried about who is going to be the next Speaker.

Chairman WHITEHOUSE. Well, they are not running for election, anyway.

Mr. Noble, I wanted to ask you, I am one who believes that the FEC is logjammed. I am one who believes it is deliberately logjammed by outside forces that have come to bear on the Commission itself to stop actions that interfere with practices that are useful in the political world but may actually be unlawful if the FEC would act. And in that regard, we spend, I do not know, close to $70 million on this Commission. Would it be useful to and will you recommend establishing a private right of action for a candidate or campaign that believes it has had the law violated against it, cannot get an answer from the FEC, and now has the right to go to the traditional constitutional locus for adjudication in the American system of government, which is a jury, and have that heard? And perhaps if there was that alternative, then the satisfaction of blockading the FEC would dissipate, and it would become more of an active and responsive body again.

Mr. NOBLE. I think a private right of action is important. There is one right now in the FEC. There are cases certain complainants can bring if the FEC does not act. Now, there are a lot of hoops you have to go through, but——

Chairman WHITEHOUSE. It is very rarely done, is it?

Mr. NOBLE. It is very rarely done, and there are constitutional reasons, including standing concerns about whether people can actually sue another party.

While I think it is an important factor, I would hate to rely on it too much because that is only available to major players, the peo-

ple who can afford lawyers. The party committees can. It is not available to the average citizen who cannot afford to sue the agency.

And I agree with Commissioner Smith on something which is very important, that I think the Department of Justice needs to do much more, but I do agree that a locus should be at the FEC. I think the problem is the FEC is not enforcing the law, and it is deteriorated tremendously since Commissioner Smith was there. And there have been always been differences on the Commission, but right now what you see are true ideological differences, where you have three Commissioners who just do not believe much of the law.

And I appreciate Commissioner Smith saying that these are not bugs, these are features. I do think it is a bug that, as of the end of this April, all six seats on the Commission will have expired, and no appointments have been made to the Commission. I do think that is a bug. I think it is a bug that since 2010, when *Citizens United* came out, the FEC has been trying—actually, it has given up—to come up with regulations to explain how *Citizens United* affects the law. It has been unable to do that.

It is kind of like saying when I had a sports car that ran half the time that that was actually a feature stopping me from using gas. No, it was a bug, and it is not acceptable.

The FEC is broken. It does not work, and something has to be done about that. And I agree with Commissioner Smith you have to be concerned about the political ramifications. But I think that if you had an effective FEC, a lot of these issues would go away. Obviously, there would always be issues that exist, but I do think a private action is part of it, but you have to address the FEC.

Chairman WHITEHOUSE. Mr. Colvin, in your testimony you addressed the Vision Service Plan case and the insubstantiality standard. Could you elaborate a little bit further on the insubstantial standard as it came through Vision Service and how that conforms or does not conform with the political activity standard, and whether that should conform? I think you reached the conclusion that it should conform. Could you explain your argument there and describe Vision Service Plan a little bit more?

Mr. COLVIN. Certainly. The Vision Service Plan did not involve political activity. It involved a health insurance plan that had, in the IRS' view, too much private benefit to certain members of the plan. The test that it used to determine what was too much was an insubstantial test. "Insubstantial" does not have a precise——

Chairman WHITEHOUSE. "Insubstantial," in quotes.

Mr. COLVIN. That is right.

Chairman WHITEHOUSE. Yes.

Mr. COLVIN. It does not have a precise percentage to it, but there have been cases in other areas of tax law affecting both political and lobbying activity that have said somewhere around five or 10 percent would be considered insubstantial.

The legal precedent for this is that when the IRS interprets words like "exclusively" and "primarily," it means all but insubstantial.

So the presence of one activity or one purpose, if it is substantial, destroys the tax exemption. However, the IRS has not taken that

stance clearly in the case of political activity and, instead, in Revenue Ruling 81–95, provided that a 501(c)(4) organization can engage in political activity, so long as it is less than primary. And in the absence of any percentage, many have interpreted that to be 49 percent.

So, really, the IRS, for that matter, if it were to pursue a case of political activity under 501(c)(4), (c)(5), or (c)(6), and the Department of Justice got hold of that case, could very well determine that the same standard ought to apply as in the Vision Service Plan, private benefit, insubstantial, 5–10 percent, and no more.

Chairman WHITEHOUSE. And they are both articulating the statutory requirement of 501(c)(4) that these entities be operated exclusively to promote social welfare. So in the case of Vision Service Plan, they said it was not exclusively to promote social welfare because there was a more than insubstantial amount of private benefit being taken out of the organization, and your hypothesis is that you could take that same standard that you used for private benefit and apply it to the political side, the political benefit, and apply the insubstantial standard.

Mr. COLVIN. Absolutely. That is correct. And Miriam Galston is here, who has written an article arguing exactly that point, and I agree with it.

Chairman WHITEHOUSE. Great.

Let me ask Mr. Smith a question. I think we have agreement so far in this hearing that with respect to the First Amendment, which clearly is a significant consideration in all of this discussion, that—two things. One, false statements under oath do not enjoy First Amendment protection. And, second, where there is a constitutional requirement, not a requirement in the Constitution but one that meets constitutional muster, by law that fraudulent use of a shell corporation to defeat that law is also not protected by the First Amendment.

Would you agree with both of those hypotheses?

Mr. SMITH. Certainly I would agree with the first. The second I'm not quite sure what you are talking about. If you are saying is it illegal to make a contribution in the name of another, you know, yes, I think that can withstand——

Chairman WHITEHOUSE. And despite the fact that making a contribution is political speech that is protected by the First Amendment, making it in the name of another is not protected by the First Amendment and can be prosecuted properly?

Mr. SMITH. I think the Court would uphold that. But it is important for us to recognize that generally, as I have heard the discussion about disclosure in this case, people kind of say, well, the Court has endorsed disclosure in *Citizens United*. It did, but remember, the Court has not endorsed anything called "disclosure." It has, in fact, placed huge limits on disclosure. Even in *Buckley* v. *Valeo*, it struck down more of the Federal Election Campaign Act's disclosure regime than it upheld. And there is a long line of cases suggesting that you have to be very sensitive in that area.

So you have raised what, again, I think is a very minor problem. We do not really see many examples of it. People are combing these things——

Chairman WHITEHOUSE. But you do not have——

Mr. SMITH. I think it is fine——

Chairman WHITEHOUSE [CONTINUING]. Any dispute that a contribution in the name of another that is fraudulently done, not innocently——

Mr. SMITH. Well, you know, if you put the circumstance that you have, which is that it is in the name of another and it is fraudulently done—and those are the questions that will often come up in investigations.

Chairman WHITEHOUSE. Yes, and ditto, false statements under oath enjoy no First Amendment protection.

Mr. SMITH. Well, I do not think they do. I tell you, under the *Stolen Valor* case, maybe even there they might have some. But I think the "under oath" would probably take that away.

Chairman WHITEHOUSE. Yes, it would seem that way. It would be a novel theory if it were not.

Senator Cruz.

Senator CRUZ. Thank you, Mr. Chairman, and I would like to thank all three witnesses for being here today.

Commissioner Smith, I would like to ask several questions. As we sit here today, Organizing for America, which is President Obama's 501(c)(4)—indeed, their Web site is barackobama.com. They are currently today running online ads criticizing me.

Now, Commissioner Smith, would you agree that that is their First Amendment right to do so that should be entirely protected under the Bill of Rights?

Mr. SMITH. I think it is a terrible thing to run ads criticizing you, Senator Cruz.

[Laughter.]

Mr. SMITH. But I probably would agree that it is protected by the First Amendment.

Senator CRUZ. And that standard should obviously apply across the board, regardless of the partisan affiliation of the speaker or the person being praised or criticized.

Mr. SMITH. I would apply that to criticism of Chairman Whitehouse as well, yes.

Senator CRUZ. Very good.

One of the things, Commissioner Smith, you talked about was the structure of the Federal Election Commission, in particular that you have got three Democrat Commissioners, three Republican Commissioners, and the role that plays as a check on partisan excesses. And you mentioned that there has been a long history when campaign activities have been located purely in the executive branch, located in, say, the IRS. There has been a long history of abuse, and abuse on both sides of the aisle. There were allegations of abuse under President Nixon. There were allegations of abuse under President Johnson.

Can you share your views on the importance of the structural check of the FEC's organization to limit either party abusing the executive branch to punish their political enemies?

Mr. SMITH. Well, I think obviously it is very, very important, you know, and the history, I have outlined some of it in my prepared remarks. We see cases like the very first prosecution brought under the Federal Election Campaign Act was brought against a group of people, ordinary citizens, basically, kind of upper-middle class folks

who had a little bit of money to pool, some professors and so on, who ran an ad in the *New York Times* criticizing Richard Nixon and calling for him to be impeached. This was before Watergate. And the Nixon folks said, well, if somebody is convinced we ought to be impeached, maybe they will be convinced not to vote for me, we ought to be able to go after these folks.

And so I really know that it is very important—you know, long history under both parties, that that is why Congress set up a bipartisan agency—not bipartisan like many agencies, 3–2 majority or something, but a true 3–3.

The Commission has historically deadlocked, as people say, gone 3–3 on about one to four percent of its votes. In recent years, that has spiked up to about 10 percent of its votes. One thing I'd point out is that typically resolves the issue, and it is important to note that that spike may be precisely due to the fact that over the last couple years we have seen, I think, strong attempts by partisans to use disclosure in the campaign finance rules in that way.

You know, Media Matters, a very liberal group, has, for example, said that its goal is to attack corporations that might make political contributions of any kind, which would include contributions to a trade association that makes political expenditures. And then use its allies to then attack that same corporation for the damage done to its reputation, which is created by Media Matters itself.

Candace Nichols, an opponent of Proposition 8 out in California, made the comment afterwards that they were blacklisting and boycotting a number of folks, and she said, "Years ago"—they used the campaign finance regulations disclosure to get that. She said, "Years ago, we would have never been able to get a blacklist out that fast and quickly." Apparently this is considered progress since the McCarthy era. We are now much more efficient at creating blacklists.

There is a group called Accountable America that sent letters to thousands of conservative donors threatening to dig through their lives if they continued to do that. As the *New York Times* reported, it was "hoping to create a chilling effect that will dry up contribution."

There are groups such as Huffington Post and eight maps that put maps to donors' homes right on the Web. What is the purpose of that?

I am straying a bit from your question, but what I am saying is when you are in this kind of environment, it is really important that you have some degree of bipartisan support before acting.

Senator CRUZ. Well, and I think the examples you gave about the potential for partisan retribution are particularly chilling. And they are most dangerous, it seems to me, for those who would have the temerity to criticize those in power; that a system that requires full disclosure of any citizen's activity in the political sphere enables those in power to very directly exact punishment for any who dare criticize them.

Mr. SMITH. Well, the purpose of disclosure laws, as I have always seen them, is to inform citizens about their government, but not to inform the government about their citizens.

Now, those are often two sides of the same coin, so it is hard to tease them apart. But I do think when we look at, you know, orga-

nizations that are not working with candidates, for example, that we need to start thinking about being careful about what it is that we are doing. When we are talking about direct contributions to candidates or parties, that is historically where we have allowed more disclosure, and that is where the Supreme Court upheld it in *Buckley*. Remember, in *Buckley*, the Supreme Court struck down most of the disclosure regime that otherwise existed. It was a very broad disclosure regime that would have taken in almost anybody who spoke about politics at all, whether they were giving to a candidate or not. And the Court struck most of that down.

Senator CRUZ. And I guess the threat of retribution for political speech, as you just described, is not hypothetical. We have seen it for donors who supported Proposition 8 in California and lost their job because they engaged in political speech.

I guess we recently saw with respect to another constitutional right in New York a number of gun owners being publicly identified in the newspaper and potentially subject to retribution for exercising their Second Amendment right to keep and bear arms.

Would you agree that part of the reason the First Amendment protects the right to anonymous speech is precisely to prevent retribution for citizens engaging in speech? And, indeed, that was much of the reason why perhaps the most famous example of anonymous political speech in history was the Federalist Papers, published under the pseudonym Publius.

Mr. SMITH. Right. Well, as the Supreme Court said in the *NAACP* case that you mentioned earlier, Senator, "It is hardly a novel perception that compelled disclosure of affiliation with groups engaged in advocacy may constitute . . . effective . . . restraint on freedom of association . . . ." I think it is very definitely something—I have said sometimes imagine if the government said we are going to make sure that terrorists are not infiltrating our government or foreigners are not infiltrating our government, we are going to require you to report your political activity to the government, and they are going to keep it in a big data base, and it will be made available to creditors, mortgage lenders, potential employers, your nosy neighbor, Halliburton, whoever wants it, right? Most people I know get very, very upset. And then I point out to them that that is exactly what the Federal Election Campaign Act does, and we are talking about doing more of it.

And I want to emphasize that we already have broader disclosure in America now than we have had any time in our Nation's history. We are in the greatest disclosure age of our history. And I think when we look, we do not see that it is really achieving its goals, and I wonder if the real solution is to say we have got to have more and crack down more if it is really to change the idea and try to create different incentives for people to participate.

Senator CRUZ. Thank you very much, Commissioner, and thank you to all of you.

Chairman WHITEHOUSE. Let me ask one additional question, and that is, your opinion—let me start with you, Mr. Noble. You have made the observation that there is conspicuous non-enforcement of a variety of laws in situations in which the enforcement of the law actually would be reasonably straightforward. A false statement case is not a complicated thing to make, and the 441(f) shell cor-

poration, you know, use of shell corporations to violate the law occurs in all sorts of areas of the law. So why the non-enforcement?

And let me add an asterisk to that. I know that DOJ will say, "Well, why the non-enforcement is because we have not been referred cases by the IRS." But that really begs the question, because the Attorney General and the Secretary of the Treasury and the Commissioner of the Internal Revenue Service all work for the same person, and the Attorney General could perfectly well say to his colleague, "Look, these are laws that I am supposed to enforce. We prosecute false statements all across the board. Why aren't you referring these to us? What is going on with your regulations that makes this difficult?" And you might then see some of the progress that Mr. Colvin has suggested toward the IRS redoing the regulations, to the extent that that is described as the problem.

So that is really, I think—when that is the answer to the question, that is really just another way of asking the question. So I wanted to make sure that you looked at it that way. Why the non-enforcement? And if the reason is because the IRS does not make referrals and has adopted confusing and different regulations, why are they satisfied with that as the status quo?

Mr. COLVIN. I think there are several reasons, and I have to say up front, I have tremendous respect for the staff of federal agencies, of the IRS and the Department of Justice. I think they try very hard to do what the right thing is.

I think there is a certain amount of fear. There is a fear of getting involved in politics. There is a fear of being accused of being partisan when you are not being partisan, when you are calling it as you see it, but people are going to say, "You did that just for partisan reasons."

I think as you move up the chain, I think then you get into a power issue. Frankly, the current system helps those in power. The current system, the lack of enforcement, favors those who are writing the laws right now, who are enforcing the laws right now. It favors this administration to keep a system by which they won in place. They do not want, frankly, any more disclosure. They are not calling—this is a great disappointment, but this administration right now is not calling to redo the FEC, not calling for much stricter enforcement of these laws, not calling for a crackdown on OFA, Organizing for America. They are not doing that either. Why? Because I think the problem we face is that we are fundamentally dealing about a power issue here and about the right of voters.

There is a very critical First Amendment issue, no doubt about that. It is paramount in this area, and everything we do in this area involves the First Amendment. But there is also an issue about democracy, about our right to know what the government is doing, about our right to know where Members of Congress or Senators are getting their funding, who they may be beholden to. And these are the issues the Supreme Court has upheld. These are the things the Supreme Court has said the government has a compelling interest in. And when it says "the government," it means the people have a compelling interest in knowing who are funding the campaigns.

And when the Supreme Court says these expenditures have to be independent or that 501(c)(4) organizations that do not get involved

in political activity do not have to disclose, there are caveats that go along with that. That means that they are not involved in political activity. And we are not talking about every issue. We are not talking about arguing about gun control. There are very specific—the Court is limited to very specific types of ads: express advocacy ads, electioneering communication ads, or things that are done in coordination with a candidate. These are very, very specific issues, very specific areas where the public has a right to know; the public has the right to have the law enforced as it is; and, yes, the public has a right to be protected.

But just to quote the First Amendment and say that that bar is doing anything, I think, is really to present the public with a false option. You can have the strongest First Amendment and a very strong representative democracy that actually is responsible to the people, and the people understand and make the decisions about what they feel about where the contributions are going or who is supporting whom.

So I think it is fear, and I think it is politics and power.

Chairman WHITEHOUSE. Senator Cruz.

[No response.]

Chairman WHITEHOUSE. All right. Let me thank the witnesses for coming. I really appreciate the effort that went into the testimony. I think that each one of you provided very thoughtful and extensive testimony. Mr. Smith, I thought some of the historical examples that you brought out were particularly instructive and helpful. And I am delighted that you all shared your time with us. I know you are very busy people.

Senator Leahy has a statement for the record, our Chairman, that, without objection, I will add to the record of these proceedings.

[The prepared statement of Chairman Leahy appears as a submission for the record.]

Chairman WHITEHOUSE. And I want to thank Senator Cruz for attending. He brings a very valuable and well-honed perspective. But I do think that there has emerged an area of agreement that really translates across all of the participants in this hearing, and that is that a traditional prosecutable false statement under oath is not protected by the First Amendment, and that the use of shell corporations fraudulently to violate the law is not protected by the First Amendment. And yet those specific things within the much larger context of campaign finance reform, those specific things seem to be happening a lot, and that neither the Department of Justice nor the Internal Revenue Service could identify a single case they had ever made either in the circumstance of a false statement made to the famous Question 15 or in the case of a shell corporation used to obscure the origin, unlawfully, of a contribution to a super PAC that would otherwise have to be disclosed. Those seem like very straightforward cases.

And it appears—I will now venture into my own personal opinion at this point. It appears to me that the deference of the Department of Justice to the tax authorities with respect to those specific matters is not merited. They are not the kind of case that a prosecutor looks at and says, "Oh, my gosh, I better bring the tax guys in on this one. This is a complicated question of tax law." No. A

false statement is a false statement, and if you take people into a grand jury, you can pretty well find out very quickly what the intent was and prove the materiality and move on.

So it appears to me that if there is at least one flaw in what we are doing right now, it is, with respect to those matters, the willingness of the Department of Justice to allow itself to be constrained by this policy of deference, which is its own policy, to the Internal Revenue Service, which I think all of the witnesses—many of the witnesses, at least—agree is not particularly well suited, is not particularly well staffed, and is not particularly well disposed toward this sort of a matter.

So I will close the hearing with my personal commentary and look forward to continuing to work on this issue with all of the witnesses and all of the Members of the Subcommittee. Again, my gratitude to Senator Cruz for his helpful participation in this hearing.

Thank you, and we are—the record will be open for one week for any additional matter anybody wants to add to the hearing, and with that, we are adjourned.

[Whereupon, at 11:43 a.m., the Subcommittee was adjourned.]

[Questions and answers and submissions for the record follow.]

[Additional material is being retained in the Committee Files; see Contents.]

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Witness List

Hearing before the
Senate Committee on the Judiciary
Subcommittee on Crime and Terrorism

On

"Current Issues in Campaign Finance Law Enforcement"

Tuesday, April 9, 2013
Dirksen Senate Office Building, Room 226
10:00 a.m.

Panel I

Mythili Raman
Acting Assistant Attorney General
Criminal Division, United States Department of Justice
Washington, DC

Patricia Haynes
Deputy Chief, Criminal Investigation
Internal Revenue Service
Washington, DC

Panel II

Lawrence M. Noble
President
Americans for Campaign Reform
Washington, DC

Gregory L. Colvin
Principal
Adler & Colvin
San Francisco, CA

Bradley A. Smith
Chairman
Center for Competitive Politics
Josiah H. Blackmore II/Shirley M. Nault Professor of Law
Capital University Law School
Columbus, OH

PREPARED STATEMENT OF CHAIRMAN PATRICK LEAHY

STATEMENT OF SENATOR PATRICK LEAHY (D-VT.)
CHAIRMAN, SENATE JUDICIARY COMMITTEE
HEARING ON "CURRENT ISSUES IN CAMPAIGN FINANCE LAW ENFORCEMENT"
APRIL 9, 2013

More than three years ago, with the stroke of a pen, a narrow, conservative, and activist majority of the Supreme Court overturned a century of law designed to protect our elections from unfettered corporate spending. In *Citizens United*, the Court struck down key provisions of our bipartisan campaign finance laws, and ruled that corporations are no longer prohibited from direct spending in political campaigns. As we have seen in recent elections, the decision has resulted in billions of dollars of advertising by secret, unaccountable sources flooding our airwaves. While money has always played a significant role in politics, the sheer amount of secret money that is now used to finance our elections undermines our democracy, which is rooted in transparency and accountability. *Citizens United* has made our democracy less transparent and less accountable. It turned on its head the idea of government of, by and for the people. Few Supreme Court decisions in American history have had such a negative impact on our political process. It is an issue that should concern both Democrats and Republicans.

Last June, those same five justices doubled down on *Citizens United* when they summarily struck down a 100-year-old Montana state law barring corporate contributions. In doing so, they again ignored the mountain of evidence establishing the corrupting influence of unaccountable corporate money on our political process.

These Supreme Court decisions not only go against longstanding laws and legal precedents, but also against commonsense. Corporations, quite simply, are not people. Corporations do not have the same rights, the same morals or the same interests. Corporations cannot vote in our democracy. They are artificial legal constructs meant to facilitate business. The Founders understood this. Vermonters and Americans across the country have long understood this. A narrow majority on the Supreme Court apparently does not.

Because so much of our campaign finance laws has been gutted by *Citizens United*, our Nation must find new ways to protect our democracy and to ensure that our elections remain free and fair. In the past, I have cosponsored various versions of the DISCLOSE Act, which attempted to restore transparency in our campaign finance laws after *Citizens United* and to curtail some of the worst abuses caused by that decision. Regrettably, Senate Republicans filibustered the bill in 2010, and again, in 2012. Despite a majority of support for this common sense legislation, Republicans refuse to even proceed to debate the bill in the Senate. Our efforts to ensure that our democracy would not be undermined by the harmful effects of unfettered political spending have fallen on deaf ears.

Today, Chairman Whitehouse holds this important hearing on "Current Issues in Campaign Finance Law Enforcement," and will raise public awareness as to how we can best protect our elections from undue corporate influence by prosecuting those who flagrantly violate our campaign finance laws. I thank and commend him for holding this hearing. I believe it is critical that we engage those in law enforcement to ensure that they have the necessary tools to prosecute those who are undermining our democracy by skirting what remain of our campaign

finance laws after *Citizens United*. Our goal, of course, is to do everything in our power to re-establish public safeguards to prevent corporate megaphones from drowning out the voices of American voters. I am hopeful that this hearing will be a positive step in that direction.

This issue is one that is especially important to me because it strikes at the core of our democracy. I know that the people of Vermont, like all Americans, take seriously their civic duty to choose wisely on Election Day. Like all Vermonters, I cherish the voters' role in the democratic process and am a staunch believer in the First Amendment. The rights of Vermonters and all Americans to speak to each other and to be heard should not be undercut by corporate spending. More importantly, they should not be undercut by unaccountable Super PACs and independent, outside organizations whose identities remain hidden from the public.

When a person knowingly and willfully violates our criminal laws, they are prosecuted. So should individuals who knowingly and willfully violate prohibitions on coordination between independent organizations and candidates or parties. So, too, should individuals who knowingly and willfully violate disclosure rules – including those who illegally transfer money through a conduit. And so, too, should individuals who knowingly and willfully make false and deceptive statements to evade our campaign finance laws.

Vermonters and all Americans should not be subject to deceptive campaign advertisements created by those who abuse our campaign finance laws by funneling money into shell corporations and political action committees that misrepresent who they are. Our democracy is at its best when there is accountability and transparency. We must ensure that our law enforcement officials can uncover deception in our electoral process to make it better. Let us continue today to re-establish the accountability and transparency that have been stripped away after *Citizens United*.

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PREPARED STATEMENT OF SENATOR JOHN CORNYN

Statement of Senator Cornyn

Senate Judiciary Subcommittee on Crime and Terrorism Hearing "*Current Issues in Campaign Finance Law Enforcement*" (April 9, 2013)

In theory, today's hearing examines the enforcement of existing campaign finance laws. In fact, it lays the groundwork for yet another attempt to undermine the Constitution's guarantees of free speech and assembly and limit involvement in the political process.

The Justice Department insists that "recent changes in our campaign finance laws have made it more difficult for us to combat the ability of individuals and entities to 'buy influence' over elections and conceal their conduct."[1] It offers no evidence of newfound illegality, merely insinuation; and it condemns conduct that is, right now, completely legal. The Department then advocates for authority to prosecute that legal conduct, which happens to involve the exercise of political speech and assembly rights. There is perhaps nothing more frightening in a democratic society than the government identifying legal political activity that it does not like and seeking to make it illegal.

The Democratic Party is trying once again to build support for the DISCLOSE Act – and this hearing is part of that effort. Transparency and the disclosure are laudable goals, but advocates of the DISCLOSE Act seek a legal regime that will undermine the First Amendment, chilling speech and association. The bill would gerrymander election law to favor the majority party and put the Administration in a position to identify – and silence – those with which it disagrees. That is not good government, the point of most transparency efforts. And it will not help democracy. Prior attempts at campaign finance reform have led to unintended consequences and, sadly, our government has a bad history of abusing its authority to silence opposition.

Proponents of DISCLOSE claim that new restrictions on political speech and association are necessary because *Citizens United* and other court decisions led to a flood of "secret" money into elections. While no one disputes that increasing amounts of money are being spent on elections, the amount of money given by "secret" people or groups is a tiny fraction. And the increase is not the result of *Citizens United* or any other case. Their premises are false.

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[1] *Current Issues in Campaign Finance Law Enforcement: Hearing Before the Subcomm. on Crime and Terrorism of the S. Comm. on the Judiciary*, 113th Cong., (statement of Mythili Raman, Acting Ass't. Att'y Gen., Criminal Div., Dep't of Justice, at 4).

PREPARED STATEMENT OF MYTHILI RAMAN, ASSISTANT ATTORNEY GENERAL, U.S. DEPARTMENT OF JUSTICE

Department of Justice

STATEMENT

OF

MYTHILI RAMAN
ACTING ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION

BEFORE THE

SUBCOMMITTEE ON CRIME AND TERRORISM
COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

AT A HEARING ENTITLED

"CURRENT ISSUES IN CAMPAIGN FINANCE LAW ENFORCEMENT"

PRESENTED

APRIL 9, 2013

Mythili Raman
Acting Assistant Attorney General
Criminal Division
U.S. Department of Justice

Subcommittee on Crime and Terrorism
Committee on the Judiciary
United States Senate

"Current Issues in Campaign Finance Law Enforcement"
April 9, 2013

Chairman Whitehouse, Ranking Member Graham, and distinguished Members of the Subcommittee: Thank you for inviting me to share the views of the Justice Department on challenges to the criminal enforcement of our campaign finance laws posed by the growing activity of Super PACs and certain 501(c) organizations. I am honored to represent the Department at this hearing and to have the opportunity to oversee the important work of the Criminal Division.

Protecting the integrity of our elections is one of the Department's most important tasks, and enforcement of our campaign finance laws is a top priority. There is no question that private contributions to political campaigns are a fundamental part of the electoral process, and that, under the Constitution, the ability to make political contributions is a protected component of our citizens' political speech. At the same time, Congress and the federal courts have long recognized the importance of transparency and fairness in campaign finance, to avoid any individual or entity exercising undue influence over our elections or elected officials.

The Department of Justice, through the Criminal Division's Public Integrity Section and the 93 United States Attorneys' Offices, is committed to investigating and prosecuting those who willfully violate the disclosure requirements and contribution limits established by our campaign finance laws. We are greatly assisted in this mission by the comprehensive disclosure system administered by the Federal Election Commission (FEC). When the public and law enforcement can see who is making contributions, the Department can better detect, investigate, and prosecute contributions exceeding statutory limits, contributions from banned sources, and bribes.

RECENT CAMPAIGN FINANCE PROSECUTIONS

Since 2010, the Department has successfully prosecuted more than a dozen cases involving campaign finance violations. For example, in February of this year, the Criminal Division's Public Integrity Section and the U.S. Attorney's Office for the Eastern District of Virginia secured guilty pleas from Virginia businessman William Danielczyk and one of his employees, Eugene Biagi, in connection with a scheme in which Danielczyk contributed over $180,000 to a federal candidate in excess of the limits imposed by law. Danielczyk and Biagi used employees and others to make conduit contributions to the campaign, and reimbursed the straw contributors in part using corporate funds. In that case, the district court initially dismissed

two significant charges, relying on the U.S. Supreme Court's 2010 decision in *Citizens United v. FEC* to find unconstitutional the ban on corporate contributions to candidates. The Department appealed that decision and prevailed in the U.S. Court of Appeals for the Fourth Circuit.

Also in February of this year, the Public Integrity Section and the U.S. Attorney's Office for the Northern District of Florida obtained a guilty plea from Florida real estate developer Jay Odom, who admitted to making $23,000 in conduit contributions to a presidential campaign in 2007. Odom pleaded guilty to causing a false statement to be made by the campaign to the FEC concerning these unlawful contributions.

Last year, the U.S. Attorney's Office for the District of New Jersey secured a guilty plea from Joseph Bigica, who contributed almost $100,000 to a federal candidate's campaign committee in the form of conduit contributions made through family, friends, and employees. Also last year, the Public Integrity Section and the U.S. Attorney's Office for the Middle District of Florida secured guilty pleas from a real estate developer, Timothy Mobley, and his accountant, Timothy Hohl, for their roles in funneling corporate contributions and contributions in excess of the legal limits to a state political party and to the campaign of a Member of Congress. The unlawful contributions were made through straw contributors whom Mobley and Hohl reimbursed.

In 2010, the Public Integrity Section and the U.S. Attorney's Office for the Eastern District of Virginia secured a guilty plea from lobbyist Paul Magliocchetti in one of the largest conduit contribution schemes in U.S. history. Magliocchetti made hundreds of thousands of dollars of contributions in excess of legal limits and funneled corporate funds to federal candidates for elected office by having his family, friends, and employees make reimbursed conduit contributions. Magliocchetti also pleaded guilty to causing various federal candidate campaign committees to unwittingly make false statements to the FEC in regard to these unlawful contributions.

CURRENT CHALLENGES IN CAMPAIGN FINANCE ENFORCEMENT

Under current law, candidate committees, party committees, and political action committees (PACs) are required to register with the FEC and to disclose contributions and expenditures. Until recently, almost all political spending occurred through these organizations, and we were able to detect and prosecute violations of the campaign finance laws, often by using campaign and committee disclosures available to federal agents and prosecutors through the FEC's comprehensive, searchable website.

Following the Supreme Court's decision in *Citizens United*, the manner in which individuals and entities raise and spend money in our elections changed dramatically, and continues to change. These developments are having a profound effect on our ability effectively to enforce the campaign finance laws. The two most important developments are the rise of Super PACs and the growing political activity of certain types of 501(c) organizations, such as 501(c)(4) entities.

Super PACs came into being following *Citizens United*, in which the Supreme Court held that corporations have a First Amendment right to spend money to seek to influence elections, invalidating a statute that prohibited independent expenditures by labor organizations and banks. In light of *Citizens United*, corporate and other entities, like individuals, can make independent expenditures – that is, expenditures expressly advocating the election or defeat of a clearly identified candidate – so long as the expenditures are not coordinated with candidate committees or organizations that contribute directly to candidates. In other words, as long as a corporation or other entity spends money for political speech that is truly independent of the candidate or campaign that it supports, it may spend as much money as it wishes.

Soon after the *Citizens United* decision, the U.S. Court of Appeals for the D.C. Circuit held in *SpeechNow.org v. FEC* that it is unconstitutional to limit the amount of money that is given to independent expenditure-only PACs, now commonly known as Super PACs. Through advisory opinions issued after *SpeechNow*, the FEC clarified that Super PACs can accept unlimited contributions from individuals, corporations, unions, or other entities.

Similarly, as a result of *Citizens United* and related decisions, organizations described in certain provisions of Section 501(c) of the Internal Revenue Code – 501(c)(4) social welfare organizations, 501(c)(5) labor organizations, and 501(c)(6) trade associations – that spend money on campaign activity can now likewise accept unlimited contributions from individuals and entities alike under the campaign finance laws. These types of 501(c) organizations are permitted to make independent expenditures to seek to influence elections, and can meet the requirements imposed by Section 501(c) provided they otherwise satisfy the requirements for tax-exempt status, which, in the case of 501(c)(4) social welfare organizations, requires only that the organization's primary activity be the promotion of social welfare rather than political activity. Unlike PACs, Super PACs and other political organizations, these classes of 501(c) organizations are not required to publicly disclose their donors to the FEC under the campaign finance laws, even though those donors' contributions may be used as expenditures to seek to influence elections. Instead, their donors are disclosed only to the Internal Revenue Service (IRS), only as part of their tax returns, and are specifically protected from public disclosure under the tax laws. Disclosure to the IRS occurs well after the spending occurs, and only through tax returns that are not available to the Department absent a referral from the IRS or a court order based on independent information. Thus, it is possible for such a 501(c) organization – one that is created during an election year and spends millions of dollars engaging in campaign activities – to ultimately disclose its donors and activities to the IRS for the first time only a year or more after the election.

The increasing use of Super PACs and the types of 501(c) organizations described above impacts transparency and changes the kinds of criminal cases the Department can bring under our campaign finance laws. We anticipate seeing fewer cases of conduit contributions directly to campaign committees or parties, because individuals or corporations who wish to influence elections or officials will no longer need to attempt to do so through conduit contribution schemes that can be criminally prosecuted. Instead, they are likely to simply make unlimited contributions to Super PACs or 501(c)s.

As to Super PACs, there are significant challenges in seeking to establish, in a criminal case, improper coordination between a Super PAC and a campaign or official. The FEC, through its advisory opinions, regulations, and matters under review, has been unable to reach agreement or declined to take administrative action in each of the following instances of possible coordination: a candidate's mother running a Super PAC expressly supporting the candidacy; sharing of office facilities by political committees and firms providing services to candidates; candidates themselves soliciting contributions to the supposedly independent committees; former campaign employees working for independent committees; sharing common vendors; and the solicitation of contributions to federal candidates by email and on the website of an independent committee. As a result, it will be rare that the evidence could give rise to proof beyond a reasonable doubt of a criminal intent to illegally coordinate through contribution to, or expenditures by, a Super PAC.

The kinds of 501(c)s described above raise other challenges to effective prosecution. An individual or entity seeking to skirt existing legal limitations under the campaign finance laws through contributions to a 501(c) may do so free from public disclosure of donors to the FEC, with a lack of any required disclosure to the IRS coincident with the contribution, and with restrictions on prosecutors' access to any eventual IRS disclosures. Thus, for example, a donor seeking to bribe a corrupt official could potentially use a 501(c) organization to hide his or her identity, and we would be unlikely to receive the warning signals we would need to investigate further. Additionally, the increasing use of 501(c)s, and the lack of disclosure of 501(c) contributor information, may make it more difficult to detect the use of foreign funds to influence elections. While proven instances of foreign financial influence are rare, detecting such improper contributions, should they occur, will be very difficult indeed given the lack of 501(c) disclosure requirements.

CONCLUSION

Vigorous enforcement of our campaign finance laws is essential to preserving both the integrity of our elections and the public's confidence in those elections. The Justice Department's prosecutors and federal law enforcement agents work hard to uncover, investigate, and prosecute campaign finance offenses. The recent changes in our campaign finance laws have made it more difficult for us to combat the ability of individuals and entities to buy influence over elections and conceal their conduct. But notwithstanding the added challenges, our commitment to enforcing the nation's campaign finance law remains as strong as ever.

PREPARED STATEMENT OF PATRICIA HAYNES, DEPUTY CHIEF, INTERNAL REVENUE SERVICE, CRIMINAL INVESTIGATION

Testimony of Patricia Haynes
Deputy Chief, Internal Revenue Service, Criminal Investigation
Before The
Senate Committee on the Judiciary
Subcommittee on Crime and Terrorism
Current Issues in Campaign Finance Law Enforcement
April 9, 2013

Chairman Whitehouse, Ranking Member Graham, and distinguished Members of the Subcommittee on Crime and Terrorism, thank you for the opportunity to appear before you this morning. My name is Patricia Haynes, and I am the Deputy Chief of the Internal Revenue Service ("IRS"), Criminal Investigation (CI).

At the request of the Subcommittee, today I will discuss IRS enforcement under Internal Revenue Code section 7206 as well as how the IRS-CI interacts with the Department of Justice and other law enforcement agencies. The IRS-CI has authority over potential criminal violations of the Internal Revenue Code.

I. Overview of IRS Criminal Investigation

The mission of the IRS-CI office is to serve the American public by investigating potential criminal violations of the Internal Revenue Code and related financial crimes in a manner that fosters confidence in the tax system and compliance with the law. IRS-CI consists of approximately 2,400 special agents worldwide who investigate criminal violations of the Internal Revenue Code and the money laundering and Bank Secrecy Act statutes. IRS-CI works closely with the Department of Justice and U.S. Attorneys' Offices around the country to bring criminal tax offenders to justice. Criminal tax enforcement is a crucial component of the IRS's overall effort to encourage voluntary compliance.

II. Title 26 U.S.C. § 7206(1)

Statutory Overview and IRS Investigative Procedures

A. Introduction

The making of false or fraudulent statements to the IRS may be prosecuted under 26 U.S.C. § 7206(1), which provides the following:

> § 7206. Fraud and false statements.
>
> Any person who--
>
> (1) Declaration under penalties of perjury.--Willfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter; [...]

> shall be guilty of a felony and, upon conviction thereof, shall be fined not more than $100,000 ($500,000 in the case of a corporation), or imprisoned not more than 3 years, or both, together with the costs of prosecution.[1]

Although the most common prosecutions under this provision involve the underreporting of income or the fraudulent inflation of deductions on federal income tax returns, § 7206(1) may also be charged in cases involving other types of false statements made on documents submitted to the IRS. *See, e.g., United States v. Mubayyid,* 658 F.3d 35 (1st Cir. 2011) (affirming § 7206(1) convictions based on defendant's false responses to Question 76 on IRS Forms 990, Return of Organization Exempt from Income Tax, which asked "Did the organization engage in any activity not previously reported to the IRS?").

B. Elements of the Offense

Courts have held that § 7206(1) has the following four elements:

(1) that the defendant made or caused to be made, a return, statement, or other document for the year in question which he verified to be true;

(2) that the return, statement, or other document was false as to a material matter;

(3) that the defendant signed the return, statement, or other document willfully and knowing it was false; and

(4) that the return, statement, or other document contained a written declaration that it was made under the penalty of perjury.

See, e.g., United States v. Griffin, 524 F.3d 71, 76 (1st Cir. 2008); *United States v. LaSpina*, 299 F.3d 165, 179 (2d Cir. 2002).

1. Materiality

The second element of § 7206(1), which requires the government to prove that the return, statement, or document in question was "false as to a material matter," has been subject to varying judicial interpretations.[2] The Circuit Courts of Appeal have applied

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[1] Pursuant to 18 U.S.C. § 3571, the maximum permissible fine has been increased to $250,000 for individuals and $500,000 for corporations.

[2] Under *United States v. Gaudin*, 515 U.S. 506 (1995), materiality is considered a mixed question of law and fact for the jury, not the court, to decide.

the following two tests to determine whether an item is material for purposes of § 7206(1):

> **i. Under the first test, any item required on a tax return necessary for a correct computation of tax is considered material.**

See, e.g., Neder v. United States, 527 U.S. 1, 16 (1999) (noting that several courts have determined that any failure to report income is material); *United States v. Scholl*, 166 F.3d 964, 979 (9th Cir.1999) ("'information is material if it is necessary to a determination of whether income tax is owed'") (*quoting United States v. Uchimura*, 125 F.3d 1282, 1285 (9th Cir. 1997)); *United States v. Clifton*, 127 F.3d 969, 970 (10th Cir. 1997) (a material statement is one that is "necessary in order that the taxpayer...compute his taxes correctly"); *United States v. Klausner*, 80 F.3d 55, 60 (2d Cir. 1996); *United States v. Taylor*, 574 F.2d 232, 235 & n.6 (5th Cir.1978) (recognizing and describing both tests); *United States v. Warden*, 545 F.2d 32, 37 (7th Cir. 1976).

> **ii. Under the second test, an item is material if it has a natural tendency to influence or impede the IRS in ascertaining the correctness of the tax declared, or in verifying or auditing the taxpayer's returns.**

See, e.g., Neder v. United States, 527 U.S.1, 16 (1999) ("In general, a false statement is material if it has a natural tendency to influence or [is] capable of influencing, the decision of the decisionmaking body to which it is addressed."); *United States v. Presbitero*, 569 F.3d 691, 700-701 (7th Cir. 2009); *United States v. Tarwater*, 308 F.3d 494, 505 (6th Cir. 2002); *United States v. DiRico*, 78 F.3d 732, 736 n.1 (1st Cir. 1994); *United States v. Greenberg*, 735 F.2d 29, 31 (2d Cir. 1984); *United States v. DiVarco*, 484 F.2d 670, 673 (7th Cir. 1973); *see also United States v. Fawaz*, 881 F.2d 259, 264 (6th Cir. 1989); *United States v. Taylor*, 574 F.2d 232, 235 & n.6 (5th Cir. 1978) (recognizing both *Warden* and *DiVarco*).

These two tests are arguably not in conflict, but are rather two "complimentary but separate tests, with one test embracing the other."[3] Nevertheless, when evaluating a

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[3] Department of Justice Criminal Tax Manual, § 12.10. The Seventh Circuit has explicitly endorsed both tests. *Compare United States v. Warden*, 545 F.2d 32, 37 (7th Cir. 1976), *with United States v. Presbitero*, 569 F.3d 691, 700-701 (7th Cir. 2009); *United States v. DiVarco*, 484 F.2d 670, 673 (7th Cir. 1973); *see also United States v. Boulerice*, 325 F.3d 75, 82 (1st Cir. 2003) ("A 'material' matter is one that is likely to affect the calculation of tax due and payable, or to affect or influence the IRS in carrying out the functions committed to it by law, such as monitoring and verifying tax liability.").

case for referral to the Department of Justice, it is important to consider the relevant Circuit precedent. In criminal investigations of tax-exempt entities, IRS-CI and Criminal Tax Counsel consult with experts in the Office of Division Counsel / Associate Chief Counsel (Tax Exempt and Government Entities) to assess the materiality of any allegedly false matter.

2. Willfulness

Section 7206(1) is a specific intent crime requiring a showing of willfulness. The Supreme Court has defined "willfulness" as "a voluntary, intentional violation of a known legal duty." *Cheek v. United States*, 498 U.S. 192, 200 (1991). In *United States v. Pomponio*, 429 U.S. 10 (1976), a § 7206(1) prosecution, the Supreme Court approved the following jury instruction on willfulness: "[t]o establish the specific intent the Government must prove that these defendants knowingly did the acts, that is, filing these returns, knowing that they were false, purposely intending to violate the law." 429 U.S. at 11 n.2.

C. IRS Investigative Procedures

The central mission of IRS-CI is to investigate potential criminal violations of the Internal Revenue Code, including potential violations of § 7206(1), and related financial crimes in a manner that fosters confidence in the tax system and compliance with the law.

1. Administrative Investigations

Investigations worked outside of the grand jury process are referred to as "administrative investigations." Most administrative investigations involve Title 26 and tax-related Title 18 violations and are generally initiated when a CI special agent anticipates working without the cooperation of other agencies. Administrative investigations may be initiated whenever information indicating possible violations of tax, money laundering, or bank secrecy laws is received or developed. CI also receives criminal fraud referrals from civil compliance employees via Form 2797, Referral Report of Potential Criminal Fraud Cases. Criminal fraud referrals consist of information acquired during a civil examination or a collection proceeding that is provided to CI by another IRS business operating division after affirmative acts (firm indications) of fraud are established and criminal criteria are met.

If information supports the potential for criminal prosecution, CI will determine whether to initiate a subject criminal investigation ("SCI"). The object of an SCI is to gather pertinent evidence to prove or disprove the existence of a violation of the laws enforced by the IRS. An SCI is considered a full-scale criminal investigation and, therefore, may include the broad spectrum of investigative techniques available to law enforcement officers.

2. Grand Jury Investigations

CI may submit a request to the Department of Justice to initiate a grand jury investigation either before, during, or after conducting an administrative investigation. A grand jury investigation may be requested when use of a grand jury would be more efficient; or when an investigation has proceeded as far as the administrative process allows, but prosecution potential would be strengthened by the grand jury process. In addition, an attorney for the government, such as an Assistant United States Attorney , may request CI's assistance in an ongoing or proposed grand jury investigation whenever the information available to the attorney indicates possible commission of crimes under the jurisdiction of the IRS.

C. Standards of Review

1. Evaluation of Administrative Cases for Prosecution

At the conclusion of an administrative investigation, CI forwards the Special Agent's Report and accompanying exhibits to Criminal Tax Counsel for review. Criminal Tax Counsel will evaluate the materials to determine whether the evidence relied upon to support CI's prosecution recommendation is sufficient to indicate guilt beyond a reasonable doubt and whether there is a reasonable probability of conviction. A Criminal Tax attorney prepares a criminal evaluation memorandum on the basis of this evaluation and transmits the memorandum to the IRS-CI Special Agent in Charge ("SAC"). The SAC is the referral authority for prosecution recommendation to the Department of Justice.

2. Review of Referrals for Grand Jury Investigation

If certain factors are present consideration may be given to referring the case for grand jury investigation. A referral for grand jury investigation is accomplished by the SAC, who refers CI's recommendation to the Department of Justice. Before this referral takes place, Criminal Tax Counsel reviews and evaluates the request and provides a legal analysis to the SAC. The review by Criminal Tax Counsel is to determine:

i. Whether there are articulable facts supporting a reasonable belief that a crime has been committed;

ii. Whether referral for grand jury investigation would be necessary and appropriate in the circumstances; and

iii. Whether there are legal impediments or other factors that substantially detract from or negate the prospect of ultimately developing admissible evidence necessary to establish guilt beyond a reasonable doubt and reasonable probability of conviction.

3. Evaluation of Grand Jury Cases for Prosecution

At the conclusion of a grand jury investigation, Criminal Tax Counsel will review and evaluate grand jury cases for legal sufficiency and will identify any legal or other impediments that detract from the prospects of successful prosecution. A grand jury criminal evaluation memorandum is prepared by a Criminal Tax attorney on the basis of this evaluation and is transmitted to the SAC.

Conclusion

Thank you for allowing me to discuss IRS enforcement under Internal Revenue Code section 7206 as well as how the IRS-CI, which has authority over potential criminal violations of the Internal Revenue Code, interacts with the Department of Justice and other law enforcement agencies. This concludes my testimony. I would be happy to answer any questions you may have.

PREPARED STATEMENT OF LAWRENCE M. NOBLE, PRESIDENT AND CEO, AMERICANS FOR CAMPAIGN REFORM

Americans for Campaign Reform

Statement
of
Lawrence M. Noble
President and C.E.O.
Americans for Campaign Reform

Before the
Subcommittee on Crime and Terrorism
Senate Committee on the Judiciary
"Current Issues in Campaign Finance Law Enforcement"

April 9, 2013

Statement
of
Lawrence M. Noble
President and C.E.O.
Americans for Campaign Reform

April 9, 2013

Chairman Whitehouse, Ranking Member Graham and distinguished Members of the Subcommittee, I am president and CEO of Americans for Campaign Reform (ACR), a non-partisan non-profit organization that advocates for small donor public funding of elections. I am also currently an Adjunct Professor at George Washington University Law School, where I teach campaign finance law. Prior to joining ACR, I served as general counsel of the Federal Election Commission (FEC) for 13 years, was executive director of the Center for Responsive Politics and was in private practice, where I advised corporate clients on compliance with federal and state campaign finance laws. I appreciate the opportunity to address the Subcommittee on issues with the enforcement of the campaign finance laws.

It is hard to look at the 2012 election and not conclude that there are very serious problems with our current campaign finance system. It is estimated that we spent over $6 billion dollars on the last election. According to the FEC, so-called "independent" SuperPACs reported spending over $600 million, while 501(c)(4) organizations reported spending over $250 million advocating the election of candidates through independent expenditures or electioneering communications. And, these figures only include what was reported to the FEC. They do not include all of the unreported money spent by various groups that were actively seeking the election or defeat of candidates, often working as surrogates for the campaigns and political parties while shielding their donors from public view.

Some argue that this spending reflects a spirited and healthy debate about the candidates and issues. It is true that there was a loud debate during the last election, but participation was largely limited to only those who could afford to buy expensive ads or donate large amounts of money to various groups. And, it was a debate where we often didn't know the real identity of those speaking.

Many, including some who agree that the current campaign finance system is broken and has resulted in the disenfranchisement of the average voter, point to Supreme Court decisions such as *Citizens United* as the reason it appears the current laws are no longer effective. In fact, some have concluded that the power that corporations, unions and wealthy individuals currently have over our elections is now a fact of life and that, short of a constitutional amendment, there is little Congress can be done to curb that power.

However, this analysis ignores how much of the problem has been caused by the failure of the FEC, Department of Justice (DOJ) and the Internal Revenue Service (IRS) to properly interpret and enforce the laws that do exist. While it is outside the power of the FEC and DOJ to prohibit corporations, unions and individuals from making independent expenditures in connection with federal elections, they do have the power and responsibility to make sure the sources of money spent on many of these expenditures are disclosed and that all of this unlimited spending is truly independent of the candidate. In fact, the laws requiring disclosure of the sources of this outside spending have been upheld by the Supreme Court. Equally significant is the fact that the Court presumed the rules prohibiting the spending of this money in coordination with candidates were being enforced when it determined there was insufficient justification to ban corporate independent expenditures.

I. Disclosure

The fact is that the Supreme Court has consistently held that disclosure serves a compelling governmental interest. In fact, four of the five justices who struck down the long-standing ban on corporate independent expenditures agreed with the four justices who would have upheld the ban that broad disclosure laws were justified when applied the same activity. However, the laws are currently being interpreted and enforced in such a way as to undermine core disclosure requirements as applied to both SuperPACs and 501(c)(4) organizations.

So-called SuperPACs are a product of the Supreme Court's decision in *Citizens United,* allowing corporations and unions to make unlimited independent expenditures, and the subsequent decision of the U.S. Court of Appeals for the D.C. Circuit, in *SpeechNow v. FEC,* allowing PACs that make only independent expenditures to accept unlimited corporate and union money. Nevertheless, SuperPACs must register with the FEC and publicly report the source of their funds. Therefore, the public should be able to learn who is funding the SuperPAC activity.

However, there have been instances where a SuperPAC has reported another corporation or organization as a donor, when in fact that entity was being used to shield the true individual donor of the funds. Disclosure can be easily circumvented if all you have to do is use an intermediary organization between the real donor and the SuperPAC. Fortunately, that is currently illegal under 2 U.S.C. §441f. Unfortunately, it does not appear that law is being enforced. Section 441f provides:

> No person shall make a contribution in the name of another person or knowingly permit his name to be used to effect such a contribution and no person shall knowingly accept a contribution made by one person in the name of another person.

Under the clear application of this law, providing a contribution to a SuperPAC through the use of a straw donor, and knowingly accepting such a contribution, is illegal. This means anyone who passes money through an organization for the purpose of making a contribution to a SuperPAC, the organization used as a pass-through, and the recipient SuperPAC who knows of the arrangement can all be prosecuted for violation of §441f. While the FEC and the Department of Justice have prosecuted cases where individuals and corporation have reimbursed donors to candidates, it does not appear there is any effort to target donors to SuperPACs who use front organizations to hide their contributions or the SuperPACs who knowingly accept such contributions.

Of course, many donors prefer to avoid the use of SuperPACs and work through organizations that do not report any of their donors. One of the most common ways to hide the source of funds used for independent expenditures is for the expenditures to be made by a group claiming status as a 501(c)(4) organization under the Internal Revenue Code. To be a 501(c)(4) organization a group must be engaged in social welfare activities and not have political activity as its primary activity. These groups are not required to publicly disclose their donors under the Internal Revenue Code. Under *Citizens United,* they may make independent expenditures.

Nevertheless, falsely declaring an organization to not have political activity as its primary purpose in an effort to obtain 501(c)(4) recognition could be treated as a criminal violation. However, given the number of 501(c)(4) organizations that appeared to spend most of their time on political activity during the last election, there appears to be little effort being given to making sure politically active groups claiming 501(c)(4) status are complying with the law. In fact, the IRS has never made clear when a group's purpose is "primary" or "political." And, while IRS proceedings are confidential, it appears that the agency rarely challenges a group's 501(c)(4) designation based on political activity.

Moreover, if such any group spends or receives more than $1,000 for an independent expenditure and its major purpose is election advocacy, it becomes a political committee under the Federal Election Campaign Act (FECA) and has to publicly report its contributors and expenditures, just like any other political committee. The FEC, however, no longer appears to be interested in determining whether any of these politically active groups should be reporting as political committees. In fact, the FEC Commissioners can no longer even agree on what activity will trigger political committee status for an organization.

Even if a group does not have to report as a political committee, it must report its independent expenditures. FECA provides that any person or organization that makes an independent expenditure in excess of $250 during a calendar year must disclose "each person who made a contribution in excess of $200 ...made for the purpose of furthering an independent expenditure." 2 U.S.C. §434(c).

Thus, when someone gives $25,000, $100,000 or $1 million or more to a 501(c)(4) organization with the knowledge or expectation that the money will be spent on election advocacy ads, it would seem that the law requires the identity of that donor be disclosed. Of course, we all know that is not being done. Why? Because certain members of the FEC have decided that the law only applies where the contributor gives for a specific advertisement, regardless of whether they gave with the knowledge that the organization was going to use his or her money for independent expenditures and with the intent that the organization do so. Utilizing this artificially narrow reading of the law, the FEC has failed to enforce the disclosure provisions as written by Congress.

To be clear, disclosure not only provides the public with information with which it can judge the message being funded, it also provides law enforcement with a necessary tool to prevent and prosecute other violations of the law. As Justice Louis Brandeis said, "Sunlight is said to be the best of disinfectants; electric light the most efficient policeman." The failure to enforce the disclosure laws means that we do not know the true source of funds being used to influence our elections. For example, it is still illegal for foreign nationals to make expenditures to influence any election in the United States, whether or not independent of a candidate. However, a system that provides easy ways to hide the true source of the funding of an independent expenditure allows those so inclined to evade that prohibition. While the Department of Justice has prosecuted cases where foreign nationals contributed directly to candidates, funding "independent" election advocacy through an organization that does not disclose its donors is way for to influence U.S. elections by hiding in plain site.

II. Coordination

Individuals have been allowed to spend unlimited amounts of their own money on "independent expenditures" since 1976 when, in *Buckley v. Valeo*, the Supreme Court first articulated what it saw as the important constitutional distinction between money spent independently of a candidate and money contributed to, or spent in coordination with, a candidate. "Independent expenditure" took on heightened significance after *Citizens United*, when the Court found that corporations and unions had the same constitutional right as individuals to make independent expenditures. While there is no doubt that both the *Buckley* and *Citizens United* decision opened the door to a new level spending in elections, what is often overlooked is that, as the word "independent" suggests, the key feature of such an expenditure is the absence of coordination with a candidate.

The Supreme Court has been very clear about why it is unconstitutional to limit independent expenditures. According to the Court, the lack of coordination with a candidate means the expenditure can hurt, as well as help the candidate, and eliminates the possibility of

any real or apparent corruption arising from the making of the independent expenditure. The presumed lack of connection between the candidate and spender means there is little chance for the candidate to feel beholden to the spender. At least that's the theory.

Congress carried this idea forward in FECA, where it defined an independent expenditure, in part, as an expenditure "that is not made in concert or cooperation with or at the request or suggestion of such candidate, the candidate's authorized political committee, or their agents, or a political party committee or its agents." 2 U.S.C. §431(17). At one time, the FEC applied the statute in a way that virtually prohibited any discussion about campaign strategy between the candidate and the independent spender. However, in what has become an all too common process, the FEC narrowed the coordination rules over time to the point where they were seen as totally ineffective.

Frustrated with the FEC, Congress enacted the Bipartisan Campaign Reform Act of 2002 (BCRA). One of the many reforms included in BCRA was the overturning of the then existing weak FEC coordination regulations and the direction to the FEC to draft new coordination rules. After a long drawn out process that involved a court sending the regulations back to the FEC more than once, in 2008 the FEC finally adopted a complex three part test with numerous subparts that runs well over 2,500 words. These new rules carve out major exemptions to the definition of coordination. But even these new weak rules have been too much for some FEC Commissioners and the FEC has deadlocked over any real attempts to enforce the coordination rules.

The result was an election where it was impossible to reconcile the normally understood concept of "independence" with the connections we routinely saw between the so-called independent spenders and the candidates and political parties. During the last election cycle, supposedly independent SuperPACs were publicly aligned with specific candidates and were established and staffed by former campaign officials, while the candidates raised funds for "their" SuperPACs and met with the SuperPACs supporters. There was no reason for these connections to be allowed to exist other than a lack of enforcement of the law. Given these connections, however, it is not surprising that no one, including the public and the candidates, seriously considered the SuperPACs independent of the candidates in any meaningful way.

III. The Role of The FEC, DOJ and IRS

There should be no doubt that a major portion of the responsibility for the lack of enforcement of the campaign finance laws lies with the FEC, which has primary jurisdiction over civil enforcement of FECA. It is the FEC which is responsible for administering and interpreting the law in the first instance. Nevertheless, the Department of Justice has independent authority to prosecute criminal violations and has made clear in the past that is not bound by the FEC's

inaction where it believes the law is clear. While one would hope the two agencies will work together, and they often do, the Department of Justice can prosecute a criminal violation of the law even where the FEC may not have the necessary votes to move forward. Unfortunately, the Justice Department seems to be willing to rely on the inaction of the FEC as justification for not moving forward on egregious cases involving SuperPACs and 501(c)(4) organizations.

While the IRS has no direct responsibility for enforcement of FECA, the Internal Revenue Code and FECA both deal with the regulation of political activity. The IRS cannot ignore its responsibility to ensure that organizations seeking to take advantage of being classified as a 501(c)(4) organization are complying with the Internal Revenue Code's restrictions on their political activity.

IV. Conclusion

It should be fundamental that, whether by action or inaction, an agency or law enforcement body cannot interpret or enforce a law in such a way as to make legal what Congress sough to prohibit. Yet, we seem to have tolerated just such a situation when it comes to our campaign finance laws. When the laws going unenforced regulate how we finance the elections of those who govern us, the public's trust in government is undermined.

I want to thank this Committee for exploring this problem and am hopeful that this is the beginning of an effort to bring about some fundamental changes to how the campaign finance laws are enforced.

PREPARED STATEMENT OF GREGORY L. COLVIN, PRINCIPAL, ADLER & COLVIN, SAN FRANCISCO, CALIFORNIA

Testimony to Senate Judiciary Subcommittee on Crime and Terrorism

April 9, 2013

Gregory L. Colvin, Adler & Colvin, San Francisco

Current Issues in Campaign Finance Law Enforcement

"Problems in IRS Enforcement of Political Rules for 501(c)4) Organizations; Reforms Needed"

Good morning, Senators. I appreciate the chance to come before you and address the question why we have seen so little enforcement--civil or criminal--of the federal tax laws that are supposed to regulate the political activities of 501(c)(4)[1] organizations.

My law firm represents a broad range of nonprofits and their donors. For 35 years, I have formed tax-exempt organizations, including (c)(4)s, and advised them on their political activities under Internal Revenue Service rules.

Why is the IRS in the business of enforcing political rules? Every person, every entity, in the country has a federal tax life. It must pay tax on its income unless it is exempt by statute.[2] The only entity allowed to have a primary political purpose is a 527 organization; it has a partial tax exemption and must disclose its donors over $200.[3] All other tax-exempts must have a primary purpose that does NOT include politics. Therefore, the IRS cannot avoid the law enforcement duty to (1) qualitatively, define political activity and (2) quantitatively, determine what is too much.

IRS Form 990 requires an answer under penalty of perjury: "Did the organization engage in direct or indirect political campaign activities on behalf of or in opposition to candidates for

public office?"[4] Those who answer "yes" must report the amount spent, the number of volunteer hours, and describe what they did.[5]

There is a fundamental problem affecting enforcement of the political tax rules on 501(c)(4) nonprofits. The tax rules are vague, unpredictable, and unevenly applied. Only the most flagrant violations could be knowing, willful, or deliberate and subject to criminal prosecution.

What is political intervention? The IRS interpretation must be gleaned from a few old cases and rulings,[6] internal training materials,[7] and a few bursts of guidance[8] from the last decade. The IRS insists on an open-ended "facts and circumstances" approach rather than drawing bright lines between partisan politics and truly nonpartisan voter education. Political intervention under tax law is more than express advocacy under election law, we are told, but what is it? Reasonable minds could differ on that judgment, dramatically so.

How much political intervention is too much for a tax-exempt 501(c)(4)? Its primary operations must promote social welfare—"the common good" of the community with no element of political intervention or private benefit. The IRS therefore deduces that non-qualifying activities must be "less than primary."[9]

While the Service has never pinned this down to an annual level of expenditures, it has tacitly accepted 49% as a defensible figure. Yet because of the IRS "facts and circumstances" approach, we can never be sure. So, the speech of some (c)(4) groups is chilled. They avoid the risk and stay far below the 49% level, while their adversaries may go right up to the edge.

Two things about the focus of this hearing on (c)(4)s:

First, there are well over 100,000 registered with the IRS. Most are highly reputable and do very little or no political activity. They do not present a law enforcement problem.

Second, enforcing these tax laws is not limited to the 501(c)(4) class. The vagueness of the IRS rules affects (c)(3) charities, banned from political intervention entirely. And (c)(5) unions and (c)(6) trade associations must obey the same primary purpose rule as (c)(4)s do.[10]

Here's the most difficult political tax law enforcement problem: what is the difference between political campaign advertising and so-called "issue ads" that name a candidate, say something good or bad about them, and tell the viewer to contact the candidate about the issue?

The Bipartisan Campaign Reform Act (McCain-Feingold) in 2002 required disclosure to the FEC of spending on "electioneering communications," defined basically as paid advertising that names a candidate and is broadcast within 30 or 60 days before an election.[11] The IRS went in a different direction. It issued Revenue Ruling 2004-6, listing a series of six bad factors and five good factors by which to judge "advocacy communications."[12] Three years later, it issued Ruling 2007-41, with a seven-factor test on "issue advocacy."[13]

The two multi-factor tests are not the same. Neither of them directly applies to the key question in this hearing: what political speech by a (c)(4) counts against its tax-exemption?

So, how can a lawyer advise his or her client, how can a prosecutor evaluate a case, in which a (c)(4) denies it will engage in candidate politics on its federal tax form, and on that same day in March it broadcasts a TV ad praising a Senator who is up for re-election in November?

Under the seven-factor IRS test, three factors look bad: it names a candidate, expresses approval of him, and is not connected to an event such as a scheduled vote on legislation. But three factors look good: the election is still eight months away, the ad makes no reference to the election or voting, and it mentions no "wedge" issues separating the candidates. The group can satisfy the seventh factor with an ongoing series of ads on the same issues.

What if the ad is targeted to a battleground state? Targeting is a factor in one IRS ruling but not the other.

With this kind of vague, uncertain, multi-factor approach, the (c)(4) can find a reputable lawyer to advise that the ad is NOT political intervention under the IRS tests. Therefore, an officer of the (c)(4) entity can sign a tax return believing that its denial is true and correct.

Let's turn to the quantitative side of the puzzle. Is the IRS properly interpreting its own precedents if it allows 49%? In recent litigation regarding *Vision Service Plan*,[14] which did not involve political activity, the IRS and the Department of Justice took the stance that ANY non-exempt activity, if substantial (that is, more than 5-15%), violates 501(c)(4). I have come to believe that the critics of 49% are right. The permitted level for political spending ought to be "insubstantial" as it is for private benefit.

A year ago, I proposed that Congress amend the Internal Revenue Code to set a 10% upper limit on political spending for all 501(c) groups, while keeping the 0% limit in place for 501(c)(3) charities.[15] This "silver bullet" would drive most of the undisclosed (c)(4) and (c)(6) money into 527 political committees, into the sunlight where it would be disclosed.

I want to conclude by suggesting that the Internal Revenue Service itself can solve both the qualitative and quantitative problems.

First, the IRS and Treasury can undertake an intensive regulatory project to establish bright lines defining political intervention—that wouldn't tolerate the disguise of targeted "issue ads" that refer to and reflect a view on candidates, and that would provide safe harbors for genuine lobbying and genuine voter education. I chair the drafting committee of the Bright Lines Project, sponsored by Public Citizen, which is developing just such a proposed regulation for IRS consideration.

Second, the Service can reconsider its position on the "less than primary" ceiling for (c)(4), (5) and (6) political spending. It can establish a percentage, at 10% (more or less), and/or a dollar level, as safely insubstantial.

These reforms would go a long way toward restoring public confidence in the tax-exempt universe, toward preventing the corruption of hidden financial leverage in our elections, and toward liberating the speech of citizen groups who have too long been intimidated by the fear of losing tax-exemption due to the unpredictable specter of IRS enforcement.

Thank you.

Questions

1. *Has anyone ever been convicted of a crime for failing to report political activity on a nonprofit tax return?*

I am aware of only one instance. During the Iran-Contra scandal in the 1980s, a man named Carl (Spitz) Channell, president of the National Endowment for the Preservation of Liberty, pled guilty to a felony conviction for conspiracy to defraud the government based on a number of violations of his organization's 501(c)(3) status, including political intervention.[16] He used tax-exempt funds to place TV ads aimed at defeating certain Congressmen who opposed aid to the contras in Nicaragua, and bragged about it to his co-conspirator Oliver North. Other than that, criminal prosecutions for conducting political activities in a tax-exempt organization, and failing to report that on an IRS tax filing, are truly rare.

2. *How does the filing of an exempt organization tax return relate to the criminal tax laws?*

The Internal Revenue Code does contain criminal laws to punish dishonest reporting. Section 7206 states: "Any person who willfully makes and subscribes any return, statement, or other document, which contains ... a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter ... shall be guilty of a felony...."

The annual Form 990 tax return filed by almost all tax-exempt organizations (except those with less than $50,000 of income and churches), must be signed by a corporate officer under penalty of perjury, declaring that "I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete."

3. *Do 501(c)(4) organizations have additional reporting requirements on Form 990, Schedule C?*

They do. They must also report:

* expenditures for activities defined (somewhat differently) as political under Section 527,
* filing of Form 1120-POL reporting tax paid on the lesser of investment income or political spending during the year,
* a list of ALL payments made to 527 political organizations, and
* a proxy tax report under Section 6033(e) to the extent that the organization gave insufficient notice of non-deductible political and lobbying expenses to its dues-paying members.

If your eyes are glazing over at this point, you can begin to see the problem. In my experience, many 501(c) organizations and their accountants get lost in the minute technicalities and fail to file complete information on the return.

4. *Is "political intervention" defined in the Treasury Regulations?*

The Internal Revenue Regulation (only 113 words) is of little help defining political "intervention," which is the term that appears throughout the Code.[17] The Regs tell us very little beyond what is in the statute, only that (a) intervention can be direct or indirect, (b) a candidate is an individual who offers himself or is proposed by others as a contestant for elective public office, (c) such office may be federal, state, or local, and (d) statements for or against a candidate may be oral or written.

5. *Can you give some examples of organizations in the 501(c)(4) category?*

You may hear about those very controversial (c)(4)s, connected to 527 SuperPACs and deeply involved in federal elections, such as Crossroads GPS and Priorities USA. There are also long-standing (c)(4)s with well-known policy agendas that do varying degrees of political activity, such as the National Rifle Association, the Christian Coalition, and the Sierra Club. But there are also brand-name (c)(4) organizations that stay completely away from political intervention, such as the AARP, Common Cause, the Disabled American Veterans, service clubs such as Rotary and Kiwanis, many health care service organizations, and committees such as in my state, California, that raise and spend fully-disclosed donations on ballot measures but stay out of candidate races.

6. *What has changed about the political spending of 501(c)(5) and (c)(6) organizations?*

After the *Citizens United* Supreme Court decision in 2010,[18] they are no longer required to limit their political spending to segregated PACs. Labor unions and chambers of commerce may spend unlimited amounts of general treasury funds on independent expenditures in politics under the election laws now, which makes it more likely that they will come closer to the edge and risk their tax-exempt status due to excessive political intervention in an election year.

7. *Is this a partisan issue?*

It is not. Our law office has represented both liberal and conservative 501(c) organizations and donors affected by this uncertain IRS enforcement, many referred by our Democratic and Republican colleagues in the California Political Attorneys Association.

8. *Has anyone questioned the disparity between the two IRS Rulings on issue advertisements?*

In May 2012, I wrote the IRS asking for a single, consolidated Ruling. No substantive response. In August I wrote again, asking four simple questions on how to reconcile the two Rulings. This January, after the election, the Service finally replied, admitting there was no "well established interpretation or principle of tax law" to answer my questions.[19] In other words, they just don't know.

9. *Can you give an example of the quantitative problem--how to determine whether a 501 (c)(4) should no longer be tax-exempt due to excessive political intervention?*

Assume that a (c)(4) spending $100 million on its programs during an election year spends $40 million on independent expenditures expressly advocating the election or defeat of candidates, admitted and described on Form 990 as political intervention. It spends another $40 million on broadcast "issue advocacy" ads that it believes pass the IRS multi-factor test and $20 million on grants to other (c)(4) organizations.

Is the organization safely qualified to be a (c)(4) organization based on spending 60%, a primary proportion, of its resources on social welfare? It depends partly on how the outgoing grants are treated. The IRS could treat the grants as a passive use of funds that is not the organization's own program activity, and shouldn't count as social welfare in the balance. If the grants do count, what does the organization need to do to make sure the money is not simply being passed off to other groups that will spend it on political intervention? It could stipulate that the grants are restricted solely to social welfare activity, but that could mean (money being fungible) that the grantee's other unrestricted funds may now be freed up to pay for more political advertising, while the grant itself could be used for more so-called "issue" ads. (Any (c)(4) grants made to 527 organizations, such as SuperPACs, are certain to be treated as political intervention.)

In this scenario, the $100 million (c)(4) organization is admitting that 40% of its spending was political. That's under 49% so it is "less than primary" and if the IRS doesn't challenge the social welfare character of its issue ads or its grants, it would remain tax-exempt.

10. *Has there been any attempt to quantify the "less than primary" test? What was the result?*

In 2004, I co-chaired a Task Force within the Exempt Organizations Committee of the ABA Tax Section that recommended to the IRS a safe harbor or a presumption of compliance at the level of 40% of annual program expenditures for 501(c)(4) organizations.[20] The Service

declined to do so. It seemed a modest proposal at the time, given the complete ban on corporate political spending that existed federally and in half of the states. Then, the Supreme Court decided in 2010 that the (c)(4) organization named Citizens United, and all other corporations and labor unions, could no longer be prohibited from making independent expenditures in elections, and (c)(4)s became the vehicle of choice for large, undisclosed donations to be spent on a combination of explicit political ads, issue ads, and other borderline election-year activities.

11. *Why do you say it is necessary to lower the amount that 501(c) organizations can spend on political intervention?*

So long as huge amounts and proportions of political campaign funds can flow through multi-purpose 501(c) entities, the task of achieving public disclosure will be almost impossible. It is very difficult to create rules that accurately trace political spending back to original sources in an organization with multiple programs. How far back do you go? Do you count the dollars first-in first-out or last-in first-out? Do you allocate the spending proportionately over all the donors? Do you let the organization say that the money came from investments, T-shirt sales, and small donors, and not from any big donors? Do you require donors to specify whether their money may or may not be used for politics?

Some of my colleagues worry that the "dark" money would go deeper underground to taxable vehicles with even less IRS regulation, but at least it would not have the halo and blessing of the federal tax-exempt system as it does now. I agree with my colleague Miriam Galston that 501(c) organizations should be whole-heartedly, not half-heartedly, devoted to their tax-exempt purposes.[21]

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[1] Internal Revenue Code (IRC) Section 501(c)(4) provides for the exemption from federal income tax of social welfare organizations. All references are to the Internal Revenue Code of 1986 as amended.

[2] IRC Section 162(e) prevents taxpayers from taking ordinary and necessary business tax deductions for political campaign expenditures.

[3] IRC Section 527 sets forth the tax-exemption and disclosure rules for political committees, parties, PACs, and other political organizations.

[4] IRS Form 990 (2012), Part IV, Line 3.

[5] Form 990, Schedule C, Part I.

[6] Revenue Ruling 78-248, 1978-1 Cum.Bull. 154; Revenue Ruling 80-282, 1980-2 Cum.Bull. 178; Revenue Ruling 86-95, 1986-2 Cum.Bull. 73; Association of the Bar of the City of New York v. Commissioner, 858 F.2d 876 (2d Cir. 1988), cert. denied, 490 U.S. 1030 (1989); Branch Ministries v. Rossotti, 211 F.3d 137 (D.C. Cir. 2000).

[7] Judith E. Kindell and John Francis Reilly, *Election Year Issues*, IRS Exempt Organizations Continuing Professional Education Technical Instruction Program for FY 2002, p. 335, www.irs.gov/pub/irs-tege/eotopici02.pdf.

[8] Revenue Ruling 2004-6, 2004-1 Cum.Bull. 328; Revenue Ruling 2007-41, 2007-1 Cum.Bull. 1421.

[9] Treas. Reg. § 1.501(c)(4)-1(a)(2)(ii); Revenue Ruling 81-95, 1981-1 Cum.Bull. 332.

[10] IRS Gen.Couns.Mem. 34233 (December 3, 1969).

[11] 2 U.S.C. 434(f)(3).

[12] Rev.Rul. 2004-6, 2004-1 Cum.Bull. 328, is limited to determining the 501(c) organization's liability for investment income tax under IRC Section 527(f).

[13] Rev.Rul 2007-41, 2007-1 Cum.Bull. 1421, is limited to 501(c)(3) charitable organizations.

[14] Vision Service Plan v. U.S., 96 A.F.T.R.2d 2005-7440, 2005-7443 (E.D. Cal. 2005), *affirmed* 2008 WL 268075, 1 (9th Cir. 2008).

[15] http://blog.ourfuture.org/20120411/A_Silver_Bullet_That_Would_End_Secret_Tax-Exempt_Money_in_Elections.

[16] 87 *Tax Notes Today* 83-3 (April 30, 1987).

[17] Treas. Reg. § 1.501(c)(3)-1(c)(3)(iii).

[18] Citizens United v. Federal Election Commission, 558 U.S. 310 (2010).

[19] IRS Correspondence to Gregory L. Colvin, January 14, 2013, attached.

[20] Comments of the Individual Members of the ABA Exempt Organizations Committee's Task Force on Section 501(c)(4) and Politics (May 25, 2004), www.abanet.org/tax/pubpolicy/2004/040525exo.pdf.

[21] Miriam Galston, *Vision Service Plan v. U.S.: Implications for Campaign Activities of 501(c)(4)'s*, 53 EXEMPT ORG. TAX REV. 165 (2006).

April 7, 2013 6 pm

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

JAN 14 2013

UIL: 501.38-00; 527.03-00

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(202) 283-8942

Dear Mr. Colvin:

This responds to your August 24, 2012, request for an information letter concerning Revenue Rulings 2004-6 and 2007-41. Your request is a follow-up to your letter dated May 7, 2012, in which you suggested that the IRS issue a single Revenue Ruling on issue advocacy communications that would apply to all tax-exempt organizations.

You request that the information letter answer the following questions:

1) "Would the application of [Rev. Rul. 2004-6] or [Rev. Rul. 2007-41] ever result in <u>different</u> judgments for the same communication, as to whether it was issue advocacy or political campaign intervention?"

2) "[Rev. Rul. 2004-6] includes, as a negative factor "target[ing] voters in a particular election." While not specifically mentioned in [Rev. Rul. 2007-41], is the presence of geographical targeting still a relevant factor?"

3) "Which [revenue] ruling applies to the primary purpose test for qualification as a tax-exempt non-charitable section 501(c) organization, such as a social welfare 501(c)(4) organization?"

4) "Why are [Rev. Rul. 2004-6] and [Rev. Rul. 2007-41] worded differently?"

Section 3.06 of Revenue Procedure 2013-4, 2013-1 IRB 126, provides that an "information letter" is a statement issued by the Director, Exempt Organizations Rulings and Agreements that "calls attention to a well established interpretation or principle of tax law ... without applying it to a specific set of facts." It also provides: "An information letter is advisory only and has no binding effect on the Service."

Rev. Rul. 2004-6, 2004-4 IRB 328 determines, in six situations, whether an organization described in section 501(c)(4), (5), or (6) that engages in public policy advocacy has expended funds for an "exempt function" as described in section 527(e)(2) and would

be subject to tax under section 527(f). Rev. Rul. 2007-41, 2007-25 IRB 1421, determines, in 21 examples, whether an organization described in section 501(c)(3) participated or intervened in any political campaign on behalf of or in opposition to any candidate for public office.

Rev. Rul. 2004-6 and Rev. Rul. 2007-41 make determinations under different sections of the Internal Revenue Code. There is not "a well established interpretation or principle of tax law" that responds to your specific questions. Therefore, pursuant to Rev. Proc. 2012-4, we decline to issue an information letter.

Notice 2012-25, 2012-15 I.R.B. 789, published on April 9, 2012, invites all taxpayers to submit recommendations for guidance for inclusion on the Guidance Priority List, which Treasury and the IRS use each year to identify and prioritize tax issues to be addressed through regulations, revenue rulings, revenue procedures, notices, and other published administrative guidance. The due date for recommendations was May 1, 2012, but the Treasury Department and the Service may consider recommendations subsequently submitted.

This letter will be made available for public inspection. The Internal Revenue Service will delete any name, address and other identifying information as appropriate under the Freedom of Information Act. See Announcement 2000-2, 2000-2 I.R.B. 295.

If you have questions, please contact Andrew Megosh at (202) 283-8942.

Sincerely,

David L. Fish
Manager, Exempt Organizations
Guidance

SUPPLEMENTAL PREPARED STATEMENT OF GREGORY L. COLVIN, ADLER & COLVIN, SAN FRANCISCO, CALIFORNIA

Testimony to Senate Judiciary Subcommittee on Crime and Terrorism

April 9, 2013

Gregory L. Colvin, Adler & Colvin, San Francisco

Current Issues in Campaign Finance Law Enforcement

"Problems in IRS Enforcement of Political Rules for 501(c)4) Organizations; Reforms Needed"

Supplemental Statement

12. *Isn't the IRS, as a tax collection agency, ill-suited to regulate political activities?*

I am more optimistic than others on this question. In my 35 years in this field, I have not seen the IRS deny or revoke the tax-exempt status of an organization for political activities without good justification. Yes, some IRS political activity audits have been protracted, mainly because of its approach that it must investigate "all the facts and circumstances." It has methodically handled cases involving high-profile individuals, including former House Speaker Newt Gingrich, NAACP Chairman Julian Bond, Jimmy Swaggart, and even President Obama, who spoke as a candidate in his own United Church of Christ. After many years, working with the Department of Justice, it settled the question of the Christian Coalition's 501(c)(4) exemption, including carefully-drawn procedures to ensure that its voter guides comparing candidates would be prepared in a nonpartisan fashion.[i]

The current director of the IRS Exempt Organizations Division had experience with the Federal Election Commission before she came to the Service. Senior IRS officials have deep experience evaluating political tax cases and have written long treatises on the subject. I believe that they are scrupulously fair and nonpartisan in these cases. Where they have made mistakes at lower levels, such as the sudden enforcement of gift tax on a few donors to (c)(4)s in 2011 or the recent improper release of confidential donor information, they have quickly corrected their procedures. The IRS is able to recognize political intervention in clear cases, such as express advocacy for or against candidates, outright political contributions, endorsements, and partisan candidate training programs, although the Service does not have a broad-scale program to detect and prosecute violations.

I have seen first-hand the IRS and Treasury produce bright line regulations in the political realm that have been well-crafted to guide tax-exempt organizations and achieve self-enforcement in the vast majority of situations. Between 1986 and 1990, with heavy input from the nonprofit sector, the Service developed lobbying regulations for public charities and private foundations with clear definitions and clear safe harbor exceptions. Working outside of government, groups like the Alliance for Justice have trained thousands of nonprofit executives on how to apply these rules,

and for the last 23 years there have been virtually no law enforcement problems in the lobbying area due to lack of clarity, no complaints of oppressive IRS prosecution.

The Service and Treasury could draw bright lines defining political intervention as well. They just need the institutional imperative to do so. In July, 2012, the director of the Exempt Organizations Division wrote to Democracy 21 and Campaign Legal Center, saying that the Service "will consider proposed changes" to regulations and other guidance in the area of 501(c)(4) political activity.[ii] But a few months later, the topic was completely absent from the IRS 2012-2013 Priority Guidance Plan. Recently, the IRS took the step of issuing a questionnaire to 1300 organizations that had declared themselves tax-exempt under 501(c)(4), (5), or (6), asking in detail about their activities, including media buys and political intervention during 2012.[iii] That's a start. The IRS should be mandated to launch a regulations project on tax-exempt political intervention, with public input, to be finished by January, 2016, before the next presidential election cycle.

To those who say the IRS should not be involved in political activity law enforcement I would reply: Congress set things up this way. The Internal Revenue Code denies a business tax deduction for political spending, charities are banned from political intervention, Sections 501(c) and 527 apply limits and taxes on political activity so that private political campaigning is not subsidized through the federal tax system. The only way to remove what Yale Professor John Simon calls political "border patrol" from IRS responsibility would be for Congress to repeal all those parts of the Code.

The IRS' jurisdiction over political activity reaches beyond federal elections to the state, county, and city levels. It is the only law enforcement system in a position to apply consistent rules on political spending by Americans and their organizations at every level of government. I believe that's actually a good thing.

13. *What's the difference between a 501(c)(4) organization and a 501(c)(3)?*

A 501(c)(4) social welfare organization is one step below a 501(c)(3) charity. They both must serve the public interest, and both are exempt from federal income tax on their annual net earnings. But the (c)(4) cannot receive tax-deductible charitable contributions and therefore the tax rules it must obey are more lenient. It is not subject to any public support testing, it can conduct unlimited lobbying on legislation, and it can engage in some degree of political campaign activity--what kind and how much is the critical question in this hearing.

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[i] Gregory L. Colvin, IRS Gives Christian Coalition Green Light for New Voter Guides, *Tax Notes* Vol.109/No. 8, Page 1093, November 21, 2005.

[ii] http://electionlawblog.org/?p=37338.

[iii] http://www.irs.gov/Charities-&-Non-Profits/Other-Non-Profits/Self-declarers-questionnaire-for-section-501-c-4-5-and-6-organizations.

PREPARED STATEMENT OF BRADLEY A. SMITH, CHAIRMAN, CENTER FOR COMPETITIVE POLITICS, JOSIAH H. BLACKMORE II/SHIRLEY M. NAULT, PROFESSOR OF LAW, CAPITAL UNIVERSITY LAW SCHOOL, COLUMBUS, OHIO

CENTER *for* COMPETITIVE POLITICS
Congress shall make no law...

Statement of Bradley A. Smith
Chairman, Center for Competitive Politics
Josiah H. Blackmore II/Shirley M. Nault Professor of Law
Capital University Law School

Before the Senate Judiciary Committee
Subcommittee on Crime and Terrorism
United States Senate
April 9, 2013

Chairman Whitehouse, Ranking Member Graham, and members of the Subcommittee, on behalf of the Center for Competitive Politics, thank you for inviting me to present our analysis of "Current Issues in Campaign Finance Law Enforcement."

The Center for Competitive Politics is a nonpartisan, non-profit 501(c)(3) organization focused on promoting and protecting the First Amendment political rights of speech, assembly, and petition. I founded the Center in 2005, after completing my term as Commissioner at the Federal Election Commission (FEC), because it had become clear to me, both as an academic and then in my time as a Commissioner, that the public is greatly misinformed about campaign finance laws and their enforcement. The Center has worked tirelessly to maintain an honest, nonpartisan approach to issues of campaign finance reform.

I. Introduction

For many reasons, enforcing campaign finance law is a highly complex issue. Most importantly, campaign finance law must be carefully crafted in order to avoid infringing on First Amendment rights. Unfortunately, too often these laws have not been carefully written, and when such laws are combined with criminal penalties, they provide a breathtakingly powerful tool for elected officials and government employees to use against political opponents.

Consider that the very first prosecution brought under the Federal Election Campaign Act of 1971 was against the National Committee for Impeachment, and that it was brought by the Justice Department under then-President Richard Nixon.

On May 31, 1972, a two-page ad appeared in the *New York Times* that featured the headline "A Resolution to Impeach Richard Nixon as President of the United States." The ad, which cost a total of $17,850, was paid for by a group consisting of several lawyers, at least one law professor, a former United States senator, and a number of other citizens of modest prominence, calling themselves the National Committee for Impeachment. In addition to criticizing President Richard Nixon, the ad recognized an "honor roll" of several congressmen who had introduced a resolution that called for the president's impeachment. In response, the United States Department of Justice moved swiftly, getting a federal district court to enjoin the National Committee for Impeachment and its officers from engaging in further political activity. The Committee, argued the government, was violating the Federal Election Campaign Act of

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1971 because its efforts had the potential to "affect" the 1972 presidential election, and the Committee had not properly registered with the government to engage in such political activity.

Ira Glasser, who was an Executive Director of the American Civil Liberties Union, noted that the government "wrote a letter to The Times threatening them with criminal prosecution if they published such an ad again.... Soon after, the ACLU itself sought to purchase space in The Times in order to publish an open letter to President Nixon, criticizing him for his position on school desegregation. The letter made no mention of the election and indeed the ACLU has never supported or opposed any candidate for elective office and is strictly nonpartisan. Fearful of government reprisal based on the government's threatening letter from the previous case, the Times refused to publish the ad."

Fortunately, in both cases, these groups' First Amendment rights were eventually vindicated. However, during the time it took to win these cases, much speech about elected officials was thwarted. Further, fighting the prosecutions came at great expense and much anxiety for those who simply sought to speak out about their government.

Indeed, the history of criminal and tax enforcement of campaign finance law is largely one of political prosecutions that should serve as a warning to this body. For example, the first case in which the U.S. Supreme Court clearly accepted the idea of regulation of political speech could be constitutional – which it did over the dissents of Justice William O. Douglas and Earl Warren – was *United States v. Auto Workers*, 352 U.S. 567 (1957). That case, as legal historian Allison Hayward has shown, was brought by the Eisenhower administration to seek to quash union political power after the merger of the AFL and the CIO. Fortunately, while the Supreme Court for the first time upheld such a prosecution against a constitutional challenge, the government was unable to get a conviction. *See* Allison R. Hayward, *Revisiting the Fable of Reform*, 45 Harv. J. Legis. 421 (2008).

The Eisenhower administration was merely following its predecessor, the Truman Administration, which had engaged in a series of political prosecutions aimed at auto dealers in Michigan in the late 1940s. In those cases, the U.S. Attorney prosecuted only reluctantly, viewing the violations as minor (in the case of some defendants) to non-existent (in the case of others), and as raising serious constitutional issues, but politicians in Washington insisted, apparently, like today, for political reasons, on "aggressive enforcement." Like today, the major columnists of the day, most notably Drew Pearson, were enlisted to whip up public fervor, with Pearson apparently benefiting from a stream of leaks from the Attorney General's office in Washington. Nevertheless – perhaps foreshadowing such prosecutions as that of John Edwards (see below), "once in court, prosecutors could not win a conviction, and jurors expressed distaste for enforcing this criminal statute against this kind of activity." And, indeed, the entire series of prosecutions was based on the belief of large scale violations "that, as it turned out, did not exist." But the prosecutions were directed from Washington because "chilling auto dealers and other corporate managers from making contributions to Republicans served the Administration's political agenda." *See* Allison R. Hayward, *The Michigan Auto Dealers Prosecution: Exploring The Department of Justice's Mid-Century Posture Toward Campaign Finance Violations*, 9 Election L. J. 177 (2010).

Today, once again, self-interested politicians are on the warpath, arguing with little evidence or on the basis of minor and exceptional incidents that massive violations are taking place that threaten our democracy, and that the problem could be resolved if only we had more "vigorous" enforcement. In particular, there has been a noted desire to police campaign finance law through regulatory bodies without expertise in campaign finance, including the IRS, the FCC, and the SEC, in addition to the Federal Election Commission. Much of this concern about enforcement stems from a desire to disclose donors to alleged "dark money" groups. Before explaining the numerous issues inherent in the IRS and other regulatory bodies enforcing campaign finance law, I think it is first necessary to consider the nature and extent of this much overblown and sensationalized theme of "dark money" in American politics.

II. The Nature and Extent of the Issue

The decisions of the United States Supreme Court in *Citizens United v. Federal Election Commission*, 558 U.S. 310 (2010) (allowing corporations and unions to make independent expenditures in political campaigns from general treasury funds) and of the United States Court of Appeals in *SpeechNow.org v. Federal Election Commission*, 599 F.3d 686 (en banc, 2010) (allowing independent expenditures to be made from pooled funds not subject to PAC contribution limits) have brought a renewed focus to the issue of disclosure of political spending. The claim has largely been that the public lacks information on the sources of vast amounts of political independent spending. This concern, while serious if true, has been artificially ramped up by many mistaken comments in the media about "secret" contributions to campaigns, as well as a widely held, but mistaken belief that under *Citizens United*, corporations and unions may now contribute directly to candidate campaigns. In any case, information amount political donors, it is believed, can help guard against officeholders becoming too compliant with the wishes of large spenders, and provide information that might be valuable to voters in deciding for whom to vote and how to evaluate political messages.

In particular, there have been concerns that non-profit organizations formed under Section 501(c)(4) of the Internal Revenue Code have been engaging in extensive political campaigns using "secret money." This issue, however, is not new. Express advocacy in favor of or against candidates was allowed for certain types of 501(c)(4) organizations even before *Citizens United*, as a result of the Supreme Court's ruling in *Federal Election Commission v. Massachusetts Citizens For Life* ("*MCFL*"), 479 U.S. 238 (1986). That decision allowed qualified non-profit corporations to conduct express advocacy through independent expenditures. These groups were significant and growing before the *Citizens United* decision and included groups such as the League of Conservation Voters and NARAL. In addition, even groups that did not qualify for the exemption pursuant to *MCFL* could and did run hard-hitting issue campaigns against candidates.

For example, in 2000, the NAACP Voter Action Fund, a non-profit social welfare group organized under Section 501(c)(4) of the tax code, ran the following ad:

> *Renee Mullins (voice over):* I'm Renee Mullins, James Byrd's daughter. On June 7, 1998 in Texas my father was killed. He was beaten, chained, and then dragged 3 miles to his death, all because he was black. So when Governor George W. Bush refused to support hate-crime legislation, it was like my father was killed all

> over again. Call Governor George W. Bush and tell him to support hate-crime legislation. We won't be dragged away from our future.

This thirty-second TV spot, featuring graphic reenactment footage, began running on October 25, 2000, just a few days before the 2000 presidential election. *See* Bradley A. Smith, *Disclosure in a Post*-Citizens United *Real World*, 6 St. Thomas J. L. & Pol'y __ (forthcoming 2013, available in draft at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2240048.)

This ad was perfectly legal to run at any time prior to 2003, with no donor disclosure, and remained legal to run under current disclosure laws more than 30 days before a primary or 60 days before a general election between 2003 and 2007. It probably also could have been run, with no donor disclosure, at any time after the Supreme Court's 2007 decision in *Wisconsin Right to Life v. Federal Election Commission*, 551 U.S. 449 (2007).

It should also be noted that neither the *Citizens United* nor *SpeechNow.org* decisions struck down any disclosure laws; nor has Congress or the FEC loosened any disclosure rules in place at the time those two decisions were issued in the spring of 2010. There has been no change in the laws governing disclosure of political spenders and contributors.

Despite heavy media focus in 2012 on "dark money," "secret money," and "undisclosed spending," in fact, the United States currently has more political disclosure than any time in its history. Candidates, political parties, PACs, and Super PACs disclose all of their donors beyond the most *de minimis* amounts. This disclosure includes the name of the group, individual, or other entity that is contributing, the date on which it occurred, and the amount given. *See* 2 U.S.C. §434(b) and (c). Indeed, these entities also report all of their expenditures.

Current law also requires reporting of all independent expenditures over $250, and of "electioneering communications" under 2 U.S.C. § 434(f). 501(c)(4) social welfare organizations, such as the National Rifle Association and the Sierra Club, must disclose donors who give money earmarked for political activity. All of this information is freely available on the FEC's website.

Furthermore, all broadcast political ads (like, in fact, all broadcast ads, political or not) must include, within the ad, the name of the person or organization paying for the ad. Thus, it is something of a misnomer to speak of "undisclosed spending." Rather, more precisely, some ads are run with less information about the spender, and contributors to the spender, than some might think desirable. This recognition is important to understanding the scope of the issue and the importance of particular measures that seek to require more disclosure.

According to the FEC, approximately $7.3 billion was spent on federal races in 2012. Approximately $2 billion, or less than 30 percent, was spent by "outside groups" (that is, citizens and organizations other than candidate campaign committees and national political parties). Jake Harper, *Total 2012 Election Spending: $7 Billion*, Jan. 31, 2013 (Sunlight Foundation); Jonathan Salant, *2012 Elections Cost Will Hit $7 Billion, FEC Chair Weintraub Says*, Jan. 31, 2013 (Bloomberg Media). According to figures from the Center for Responsive Politics, approximately $383 million was spent by organizations that did not disclose their donors. That is

just over *five percent* of the total. $383 million sounds like a lot – five percent doesn't sound like much of an issue at all.

Moreover, that five percent tends to overstate the issue because many of the largest 501(c) spenders are well-known public groups. Only 28 organizations that did not publicly disclose all donors spent more than $1 million on all independent expenditures in 2012. Most of these were well-known entities, including the U.S. Chamber of Commerce, the League of Conservation Voters, the National Rifle Association, Planned Parenthood, the National Association of Realtors, the National Federation of Independent Business, NARAL Pro-Choice America, and the Humane Society. Several of these groups also spent substantial funds on issue ads or express advocacy under the *MCFL* exemption, even before *Citizens United,* suggesting that the growth in "undisclosed" spending is even less than many believe.

Even many spenders that are not historically well-known organizations on the list are quite familiar to anyone who remotely follows the news, such as Crossroads GPS and Americans for Prosperity. Indeed, many of the funders are well-known, even as the organizations themselves do not formally disclose their names. Does anyone on this panel not know that David Koch provided substantial funding to Americans for Prosperity? If not, *see e.g.* Peter Overby, *Who's Raising Money for Tea Party Movement?* Feb. 19, 2010 (National Public Radio).

Furthermore, according to the Center for Responsive Politics, it appears that the percentage of independent spending by organizations that do not disclose their donors declined substantially (approximately 25 percent) in 2012 from 2010. This is not surprising. Because 501(c) organizations may not have political activity as their primary purpose, they must conduct their activities to stay within the IRS guidelines to maintain their exempt status. In effect, then, a donor whose main objective is political activity faces the effective equivalent of a over 50 percent tax on his or her political donations by giving to a 501(c) organization rather than to a "Super PAC," which fully discloses its donors. This is because the group must primarily spend its funds on programs other than political activity, as defined in Section 527 of the tax code. As a result of this inefficiency, it is doubtful that spending by 501(c) organizations will increase substantially as a percentage of independent or total spending. Furthermore, if the group does not conduct its activities in a manner consistent with IRS regulations, it could possibly be reclassified as a Section 527 organization by the agency and be forced to publically disclose its donors on nearly the same schedule as a political committee, except that the reports are on IRS Form 8872 and listed on the IRS website.

Lastly, it bears repeating that, contrary to claims by many, the Supreme Court's ruling in *Citizens United* did not change the prohibition on political activity by non-resident aliens and foreign corporations. Specifically, according to 2 U.S.C. § 441(e), any "partnership, association, corporation, organization, or other combination of persons organized under the laws of, or having its principal place of business in, a foreign country" is prohibited from contributing in elections. Indeed, despite the President's expressed fear that the decision would allow "foreign corporations" to make expenditures in elections, not only did *Citizens United* specifically not address that longstanding prohibition, but the Supreme Court has summarily reaffirmed that ban since. *See Bluman v. Federal Election Commission,* 132 S. Ct. 1087 (2012).

Thus, it is against this backdrop of the real nature and extent of the issue that campaign finance law enforcement can be discussed.

III. Problems of Enforcement

A. "Newberryism"

I have already noted some examples of criminal prosecution in the area of campaign finance as abuse of power for political gain. The problem of using campaign finance law to punish political opponents through threats of criminal prosecution is hardly new and points to the need to tread carefully. Indeed, the first campaign finance case ever to reach the Supreme Court illustrates that problem. Ninety-five years ago, Truman Newberry, a well-mannered scion of an old-money Detroit family, suddenly found himself under federal indictment and his very name synonymous with political corruption. Newberry's "crime"? He had run for the United States Senate as a long-shot underdog against the President's handpicked candidate and nation's most famous man, Henry Ford. Thanks to a skillful ad campaign financed by nearly $200,000 in contributions from Newberry's family members and friends (the equivalent of about $3 million in 2013), he had won.

This story is detailed in the fascinating new book, *Curbing Campaign Cash*, by Paula Baker, an Associate Professor of History at The Ohio State University. It is a cautionary story about government regulation of honest money and the political choices of the electorate.

Progressive reformers, seeking to cleanse politics from the "taint" of money, had passed a law limiting a Senate candidate in Michigan to spending $3,750, or less than $60,000 in today's dollars. Defeating a man as well-known as Ford on such a budget was likely impossible.

But the law contained a giant "loophole" – it applied only to spending by the candidate, not to spending undertaken by a committee on the candidate's behalf. Newberry hired Paul King, a young political whiz, to manage a campaign committee, and paid little attention to what King did after that. What transpired was the most expensive Senate campaign in history at that time, as King raised funds from Newberry's friends and family, hired campaign workers across Michigan, and blanketed the state with newspaper ads. King highlighted Newberry's military service as well as that of his two sons, contrasting it with Ford's pacifism and the military deferment granted to his son, the star-crossed Edsel. Newberry's major campaign plank was his opposition to the League of Nations.

When Newberry defeated Ford, Newberry's opponents cried foul. They argued that the large sums spent on his behalf tainted the election and constituted "corruption" and "fraud." President Wilson, who had personally recruited Ford for the race, set his Department of Justice upon Newberry, even before Election Day. Eager to avoid Michigan juries sympathetic to Newberry, the government convened a grand jury in New York on the theory that Newberry had signed papers related to his candidacy there. Nevertheless, the grand jury voted 16-1 against an indictment. Unperturbed, Attorney General Thomas Walsh then ordered the FBI to investigate possible violations of the Federal Corrupt Practices Act.

Meanwhile, Henry Ford deployed his vast fortune to hire investigators to comb the state of Michigan, "[taking] every bit of local bragging and complaining as ... a kernel of fact." Ford fed the information he gathered to the Attorney General, who arranged for a special prosecutor to handle the case. The case was brought in Grand Rapids, rather than the more logical venue of Detroit, Newberry's residence and campaign headquarters, because the government thought it would get a more favorable bench and jury there. At trial, in fact, a wildly partisan Judge Clarence Sessions proclaimed that "the very life of the Nation is threatened" by the "filth and poison" of campaign spending, "infinitely more to be feared than the terrors of the Ku Klux Klan." The judge excluded most of Newberry's evidence, then gave the jury a strained interpretation of the statute, and an instruction that "drew a straight line to a guilty verdict."

Newberry would eventually be vindicated by the U.S. Supreme Court – another prosecution foundering on the shoals of the Constitution – but "Newberryism" would be the standard phrase for political corruption for the next decade.

In these events, Baker sees a warning of the unintended consequences of regulation. Turn-of-the-century progressives sought to get not only money but politics out of politics. In doing so, they got more of each.

To anyone who has followed the campaign finance saga of the last two decades, the story has a remarkable sense of familiarity to it. In the partisan campaign and abuse of prosecutorial power to unseat Newberry ("a political job, from beginning to end," said Michigan's senior Senator, Charles Townsend), newspaper editorials were referenced as fact, self-serving statements by opposition politicians held forth as evidence of wisdom from those who understood the alleged dangers best, and naked abuses of government power praised by sanctimonious advocates of "good government." "Reformers" were themselves prepared to cut most any corner and unfairly smear any reputation if it helped in obtaining the political goal of "good government" reform. And always, the debate was conducted in high dudgeon: "rhetorical ambitions soared far higher than the record before them," notes Professor Baker.

Such rhetoric contributed to and played off of public ignorance. Kathleen Lawler, the Clerk to the Senate Committee on Elections, complained that voters would say, "[W]e must help stamp out this terrible scourge of Newberryism that is destroying our state and our nation." But "[w]hen asked – 'What is Newberryism?'..., they did not know...."

This certainly rings a bell today, when most voters who could not even tell you what a "Super PAC" is believe they are bad and incorrectly believe that they do not disclose their donors. Indeed, one of the most frustrating things about the campaign finance debate today remains the sheer demagoguery of the issue.

Observers of today's debates will also recognize the rank hypocrisy and incumbent self-dealing in the early reform movement. Senators saw Henry Ford as a one off – but if money could elect an empty suit such as Truman Newberry against a better-known opponent (and most incumbents are better known than their challengers), whose seat was safe? So the laws targeted the type of influence that Newberry, but not Ford, might bring to bear.

Of course, whether the public was ill-served by the election of Newberry is a different question altogether. Despite the lack of "disclosure," Michigan voters were fully aware by Election Day of the campaign's record spending. Meanwhile, though his engineering and business achievements are incontestable, in matters of public affairs Ford was more the empty suit than Newberry. He was ignorant of history (he testified to the Senate that the American Revolution happened in 1812, and that Benedict Arnold was a writer) and government (when first approached about running by a Wilson confidante, he asked, "What does a Senator have to do?"). He believed that Newberry's campaign had been financed by "a gang of Jews" as part of "a conspiracy to control the Senate."

The abuse of federal investigatory and prosecutorial power, neglect for the rule of law, innuendo and character assassination, incumbent self-dealing, rank hypocrisy, and unintended consequences of efforts to purify the system, all present in the Newberry case and to one degree or another in reform politics today, should make us glad "campaign finance reform" has gone no further than it has.

B. The Prosecution of John Edwards

Newberryism has not gone away. The dangers of criminal prosecution were again illustrated just last year in the prosecution of John Edwards. Allison Hayward, our former Vice President for Policy, wrote that "We should be grateful that the John Edwards jury has reached its verdict – and found Edwards not guilty on one count of taking an illegal campaign contribution. A guilty verdict could have meant much trouble for all campaign finance regulation. If Edwards had been found guilty on that count, we could have entered an 'Alice in Wonderland' world, where conduct that would not draw the ire of civil law enforcement can lead to prison. Because Edwards could [have been] convicted for taking a contribution that the Federal Election Commission, which regulates campaign finance, wouldn't even regard as a political donation."

Edwards is not a man who deserves any sympathy, and it is certainly possible that his actions, and those of his supporters, might have violated other federal laws or, had Edwards still been in office, Senate ethics rules. But the question here is not sympathy for Edwards, but possible prosecutorial overreach that is itself an abuse of power.

When the case was originally brought, there was much political concern that it was based on a political vendetta by a Republican U.S. attorney. Worse, prosecutors seemed to have relied on the vague language that the payments to Edwards's mistress were intended "to influence" a campaign. In recent years, prosecutors have become increasingly zealous in their efforts to squeeze all kinds of unethical conduct into the rubric of campaign finance and honest service laws. The public is not well-served by the likes of John Edwards – but nor is it well served by ambitious, overly-zealous prosecutors who stretch and abuse vague campaign finance laws in pursuit of high-profile convictions.

C. Criminal Penalties

Vague election laws combined with criminal penalties are a recipe for abusive political prosecutions. It is a threat both to the First Amendment and to honest government. In the case of

the Michigan auto dealers, which I discuss above, prosecutors were unable to gain convictions in cases that went to trial; but the threat of prison time convinced many defendants to plead no contest and pay fines.

Similarly, as the Edwards prosecution proved, much of campaign finance law is vague, complicated, or both. Because of the potential infringement on civil liberties, Congress should avoid creating additional criminal penalties to existing or new campaign finance laws. Arguably, there are already too many provisions that provide for criminal penalties. The Bipartisan Campaign Reform Act of 2002 extended the statute of limitations for many criminal violations of campaign finance laws, made more provisions of the law subject to criminal sanctions, and required the United States Sentencing Commission to issue guidelines for campaign finance law violations. Other recent high profile political prosecutions for vague allegations of campaign finance laws have similarly come apart at the seams, as in the prosecution of Ted Stevens. Unfortunately, far too often the damage is done by the time the law catches up to the hysteria. Stevens was convicted just days before the election, which he lost by less than 1% of the vote, and only vindicated posthumously after a plane crash.

The message we should send to the American people is that political participation is a good thing, not a bad thing. For half a century, the message of those who advocate the increase of strict campaign finance laws has been that political participation is bad, that people who donate are only out for themselves, and that political speech is, quite literally, dangerous. It is no wonder that the confidence in Democratic institutions has declined.

D. The Need for Campaign Finance Law Simplification

We don't measure the effectiveness of police by how many people are shot or how many citizens are convicted. Similarly, there is widespread agreement that the IRS should not be evaluated by how many penalties are collected or properties seized. To evaluate, we look at the crime rate and the tax compliance rate.

The federal election laws and regulations now contain over 376,000 words. But this just scratches the surface of election law. There are nearly 1,900 advisory opinions and nearly 7,000 enforcement actions that provide guidance on what these vague laws might mean. As the Supreme Court noted in *Citizens United*, "Campaign finance regulations now impose 'unique and complex rules' on '71 distinct entities.' These entities are subject to separate rules for 33 different types of political speech. The FEC has adopted 568 pages of regulations, 1,278 pages of explanations and justifications for those regulations." (Citing Brief for Seven Former Chairmen of FEC).

Congress's vague laws often can't be interpreted by the FEC itself. For example, in August 2012, the FEC considered an Advisory Opinion Request for the National Defense Committee filed by our organization asking whether seven proposed ads would trigger FEC regulation. The FEC said three of the ads would not trigger FEC regulations, but the FEC could not render an opinion on the other four ads, and could not decide on whether the group had to register with the FEC. The problem is not the FEC – it is the law.

The most pressing need for Congress is actually to make campaign finance law a lot simpler. How can we expect the FEC or the Department of the Justice to fairly enforce laws that no one can understand? It is literally impossible today to navigate campaign finance laws without a lawyer, and even then, your lawyer might not be able to give you a straight yes or no answer.

As a result, well-meaning citizens often stumble into breaking these laws, in part because the thresholds on regulated speech are absurdly low – for example, current law requires reporting of all independent expenditures over just $250.

E. Mr. T's Cadillac

A recent example of how citizens can trip over election laws was highlighted in a U.S. News & World Report article on a Mr. T. Augurson. Last year, he customized his Cadillac in stunning chrome and printed on the car's exterior a sign urging citizens to vote for President Barack Obama's reelection. Even though Mr. Augurson spent well over $250 on his rolling billboard, he never reported the independent expenditure to the FEC. His car also failed to carry the required disclaimer indicating who had paid for the message, how that person could be reached, and that the message was not authorized by any candidate or candidate's committee.

How was Mr. Augurson supposed to know about these reporting and disclaimer laws? Even if he had known about the law, deciding to what to report was far from straightforward. What counts toward the independent expenditure? The whole cost of the car? Or just the cost of the customization? Part of the customization, including the chrome body, or just the printing on the car? Then there is the matter of what states with primaries he drove through and when, which is important in deciding when to file the various reports and for what activity? To further complicate this real-life puzzle, consider that some FEC commissioners have publicly stated the cost of gas should count as campaign speech too.

F. Concern over Coordination

There has been a great deal of controversy about the adequacy of the regulations regarding independent expenditures. Unfortunately, much of this discussion has been ill-informed or misleading. I have attached an appendix to my statement with excerpts from the FEC brochure on coordinated communications and independent communications. As you can see, the regulations on this activity are quite extensive. The brochure does not contain the regulations themselves, but offers a commendable attempt to describe them in layman's terms.

It is not surprising that independent campaigns often use similar messages to the campaigns they are trying to support. This does not mean that there is any illegal coordination. In fact, it should hardly be surprising, when you consider how modern political campaigns are designed. The independent organizations pay for their own polling, and they can determine fairly easily what messages will resonate with the public and then design their advertising around such themes. In many cases, these groups will use similar themes to those used by the campaigns they are supporting.

Some critics of enforcement complain that few enforcement actions have resulted in penalties. But the reason for this is likely because the incentive to cheat is low (because it is not difficult to design an effective independent campaign) and the penalty is high.

If there is concern about the amount of money being raised and spent by these independent citizen organizations, the answer is fairly simple. Allow citizens to donate more money directly to candidate committees and political parties. If candidates and political parties are able to raise and spend more money, there will be fewer funds donated to independent organizations.

IV. Enforcement and the Nature of the Federal Election Commission

As part of the 1974 Amendments to the Federal Election Campaign Act, Congress created the Federal Election Commission and provided it with "exclusive jurisdiction with respect to the civil enforcement" of the Act. Almost from the start, the Reform Community has been deeply disappointed with the Federal Election Commission, and from cynicism or honest belief has blamed the agency for many of the failures of regulation. But understanding the FEC and its design is important to understanding the problems of using another agency designed for one thing – say, the smooth functioning of securities markets, regulation of broadcasting, or tax collection – for another purpose, such as regulation of campaign spending.

A. General Principles

Independent agencies are created for several reasons. An independent agency's singularity of purpose can be vital in developing and enforcing a unified government policy. That singularity of purpose can also help the agency to develop expertise. Perhaps most important to early theories of independent commissions was the notion that insulating such bodies from partisan politics would improve public policy.

With these principles in mind, we can see how what some would describe as "bugs" in the FEC structure are, to many, crucial "features."

Perhaps the most important feature of the FEC's design is the one that most bothers many reformers – its bipartisan makeup. Most federal independent agencies are directed by a board or commission with some guaranteed level of bipartisan makeup. Only the FEC and the U.S. International Trade Commission have equal size blocks of commissioners, with 3 from each major party, and only the FEC then requires a four vote majority for action. Nevertheless, it is highly doubtful that this is really the reason for the FEC's perceived failures. See Michael M. Franz, *The Devil We Know? Evaluating the Federal Election Commission as Enforcer*, 8 Elec. L. J. 167 (2009); Allison R. Hayward & Bradley A. Smith, *Don't Shoot the Messenger: The FEC, 527 Groups, and the Scope of Administrative Authority,* 4 Elec. L. J. 82 (2005); Bradley A. Smith and Stephen M. Hoersting, *A Toothless Anaconda: Innovation, Impotence and Over-enforcement at the Federal Election Commission*, 1 Elec. L. J. 145 (2002); *Colloquia: Federal Election Commission Panel Discussion, Problems and Possibilities*, 8 Admin. L. J. Am U. 223 (1994) (comments of former FEC General Counsel Larry Noble). The FEC typically divides on straight partisan lines approximately one to four percent of the time, though that number has risen in recent years and was at ten percent of enforcement matters in 2012. Furthermore, in

enforcement matters, a 3-3 result resolves the issue – the prosecution ends. There is nothing particularly unusual in that result, just as a tie vote in the Senate means a bill does not go forward.

Furthermore, the reason for the FEC's unique design should be obvious. If some measure of guaranteed bipartisanship is viewed as a valuable thing in most independent agencies, it would seem absolutely essential for an agency whose core mission is to regulate the political process, in ways that can determine who wins and who loses elections. This is a question both of preventing actual abuse of the Agency for partisan gain, and preventing the appearance that the Agency's decisions are motivated for partisan gain. In short, there is a strong argument for why the FEC is structured as it is, and it is to prevent one party from changing the regulatory regime for partisan gain.

The FEC also has an enforcement process that aims to resolve matters through conciliation rather than fines or litigation. This, too, has drawn much criticism from those seeking "stronger" enforcement. But this process exists, as well, for a reason. The overwhelming number of complaints and violations at the FEC are not over corruption, but over inadvertent violations of the law. Many are nothing more than administrative violations against the state. The cost to a political candidate of having been found to have "violated the law," however, can be great; the rewards to a zealous prosecutor or even FEC Commissioner or General Counsel who is seen to be crusading for "clean elections" are perhaps even greater in the other direction. Structuring the system around voluntary conciliation agreements is an intentional means to depoliticize the complaint process. Again, placing primary enforcement responsibility with Justice, the IRS, or another agency whose process is geared to leveling direct sanctions dramatically alters the balance, and does so in a way that may reward overly aggressive prosecution by government officials in this sensitive First Amendment area.

Thus, while it is true that almost all government agencies have structural features to insulate them from politics, the FEC has more political safeguards than most agencies and it has them for very compelling reasons.

B. Problems with Dividing Authority for Enforcement

Recently, other federal agencies have been tasked with or have found themselves facing additional responsibilities relating to the enforcement of campaign finance laws.

Dividing the regulatory function confuses the law and makes it difficult to manage a unified government policy. We have already seen the results of this type of division of labor when Congress gave some disclosure police power to the Internal Revenue Service in 2000. The result was and remains substantial public confusion and a complex yet loophole riddled system. Adding a third and even fourth federal disclosure scheme is not likely to be enlightening so much as maddening.

Divided authority also erodes agency familiarity with the law. Campaign finance law has become one of the most complex areas of constitutional law imaginable. For example, the IRS faces far fewer issues regarding elections in its everyday business than does the FEC. Its culture and expertise are therefore quite different from that of the FEC, which regularly faces these

issues. Indeed, one reason for the frustration of the Reform Community with the FEC has been the unwillingness of that Community to accept the Constitutional restraints under which the FEC operates. Those who seek to push regulation onto other agencies often do so precisely because they seek to bypass such constitutional sensitivities that are, and ought to be, a hallmark of the FEC – the agency charged by Congress with "exclusive civil enforcement" of campaign finance laws.

Such efforts can create a host of new problems. Under strong political pressure, for example, the Federal Communications Commission recently required that political ad files, which formerly were available for public inspection at a broadcaster's office, be placed on the Internet. Its effort hasn't worked out that well. Following FCC recommendations on how to comply with the new regulation, many broadcasters simply scanned and placed the contents of their political file online. As a result, a number of media buyers have had funds stolen from their bank accounts by identity thieves who take banking information off the publicly available on-line files. Peter Overby, *Thieves Target Political Ad Consultants on New FCC Site,* March 28, 2013 (National Public Radio). Would the FEC have made such a mistake? We don't know. But we know that the FCC is not a disclosure agency. Operating outside its area of expertise, its rules and advice created major new problems.

Similarly, in the last year alone, the IRS has illegally disclosed confidential tax return information of politically sensitive non-profit groups on at least three occasions involving an unknown number of organizations. As a result, last month a large and bipartisan group of prominent non-profit attorneys sent a strongly worded letter warning of the consequences of such disclosures. As the letter noted:

> We are concerned that these recent reports will have significant negative consequences. Organizations fearful of such disclosures may be less forthcoming and intentionally vague about their activities on applications for exemption, Form 990s, and other filings. Donors may be deterred from giving if they fear their contributions might be improperly disclosed.
>
> Moreover, organizations that espouse particular ideologies may be convinced – and may persuade others – that the IRS or its employees are biased against those ideologies and are engaged in a deliberate effort to undermine the organizations through deliberate improper disclosures. These results are all possible, whether improper disclosures by the IRS are malicious or merely the result of unintentional errors by agency staff.

Few view the FEC as sensitive to the First Amendment. Yet for all its faults, it is better than most other agencies in that sensitivity. The other agencies simply do not have the expertise or agency culture to enforce such laws. Enforcement of such complex law is difficult, and Congress should not attempt to create new enforcement agencies or give existing agencies new powers that would stray from their mission.

C. Problems with IRS Enforcement of Campaign Finance Law

The Internal Revenue Service had also long used, consistent with its culture, mission, and expertise as a tax collection agency, a flexible test for determining the tax exempt status of

groups that do some political work, but that have a non-political "major purpose." But the Courts have consistently required a "bright line" test for the FEC when regulating political speech. For political speakers, operating with very low thresholds to trigger status as regulated political committees, such bright lines are essential – there is little room for error. Charged with a new mission for which it lacks knowledge and expertise, and which is tangential to its core responsibilities, the IRS has yet to produce any type of bright line test similar to that used by the FEC. As a result, politically active groups can be reasonably sure they are complying with the Federal Election Campaign Act, only to be left to guess whether they will be pursued by the IRS in any case.

For social welfare and business associations, there is no clear guidance about the level of permissible political activity as a portion of the organization's budget, much less guidance as to what counts as political activity. The only thing that is clear is that express advocacy counts as political activity, but whether a group can spend 49% or 20% of its budget on such activity remains an unanswered question.

But probably more important, the move into political regulation has embroiled the IRS in political fights the Service should avoid. Given that from the 1930s through the 1970s there was considerable history of presidents of both parties attempting to use the IRS to attack political enemies, the Service has long been particularly prickly, and justifiably so, about being dragged into political wars. In fact, in the 1990s, the Service pressed many groups operating under Section 501(c)(4) of the Code to reorganize under Section 527, or to create an affiliated 527. Neither 501(c)(4) nor 527 organizations pay income tax on contributions for their exempt activities. Thus, as 527s have no IRS limits on their political activities, moving groups from (c)(4) to 527 status had no revenue effects yet helped the IRS avoid decisions about whether a group's activities were political or not, thus keeping it out of political disputes. By attempting to force the IRS back into the regulation of political activity, however, Congress places the IRS in an awkward place it prefers not to be, of having to make audit and tax exemption decisions about politically or public policy oriented entities.

Equally as important, the collection of trillions of dollars in taxes each year is based on what the IRS calls the self-assessment feature of the tax laws, where citizens and businesses calculate and pay their taxes. If the agency develops a reputation as a partisan lapdog of the party in power, that could lead to more citizens cheating on their taxes, with potentially disastrous implications for the budget deficit. If the level of compliance with just the income tax laws alone were to drop just one percentage point due to a decline in the Service's reputation for fairness, that could cost the government over $170 billion in tax collections over a 10 year period.

The Service has quickly learned that that is not possible to avoid politics once it is given the assignment to regulate overtly political activity. It has been buffeted by politicians from both parties with regularity for its disclosure and enforcement policies regarding non-profits. The IRS may be rapidly hitting the point at which it will be mired in regulatory gridlock – no new regulations or changes in existing regulations will be considered with good faith by members of Congress, each being viewed instead as a partisan scheme.

The IRS gives us a cautionary tale: the agency is not equipped or structured to do the job it was asked to do in overseeing political activities. It is, after all, the tax collection agency. This

dual regulatory scheme has created confusion in the regulated community and among the public, and created a series of seams and loopholes that the least scrupulous and most lawyered could exploit. Further, it has embroiled the Service in political battles in such a way that it now cannot address substantial areas of its core mission because its actions are so suspect on the Hill. It would be a mistake to ask the IRS to play an even greater role in the enforcement of campaign finance laws.

V. Conclusion and Recommendations

Any legislation emanating from Congress should be based on three principles:

1. Moderation;
2. Simplification; and
3. Respect for the First Amendment and a recognition that political participation should be encouraged, not discouraged, and praised, not vilified.

Specifically, Congress must begin by recognizing that the substantial majority of increased political spending in 2012 was unrelated to *Citizens United* or even *SpeechNow.org v. FEC*. These are important cases with meaningful consequences, to be sure. They have helped to open up the political system, level the playing field, and increase competition; the doomsday predictions offered when the decisions were announced in the spring of 2010 have not come true. But note that while total spending increased by approximately 37 percent from 2008 to 2012 elections, it increased by approximately 27 percent from the 2004 to 2008 elections, before these decisions and when McCain-Feingold was in full effect. These decisions probably account for no more than 15 to 20 percent of increased spending.

Second, concerns about "undisclosed" spending must be placed in context. The current disclosure regime is the most extensive in U.S. history. Only a bit more than five percent of spending in 2012 came from groups that do not disclose donors, and even that overstates the issue, since many of these groups, their missions, their general source of support, and often specific supporters are well known from other sources. By contrast, prior to the 1970s virtually no campaign donations or expenditures by candidates or political parties were publicly reported. Yet, no one then complained about dysfunctional government, legislative gridlock, or the imminent end of democracy.

Generally speaking, we as a society believe that moderation in law enforcement is good. Few of us wish to live in the police state necessary to try to prevent all violent crime, for example – and even then, we don't think we could really end *all* violent crime. Even the most ardent proponents of vigorous enforcement of border security understand that there will be some illegal immigration.

The same principle is true in campaign finance – especially since we are dealing with an area of law with sensitive First Amendment implications. Many of the things that some people argue are signs of "ineffective enforcement" are simply signs that we have other values in play. The FEC's bipartisan make-up, the target of so much criticism, exists because, I trust, few members of this Subcommittee or the Senate would be eager to allow a partisan board controlled by the opposing party to regulate campaign speech. The FEC's enforcement process, with its

sometimes cumbersome emphasis on voluntary conciliation, reflects the understanding that most violations are inadvertent, not intentional. We have historically sought to minimize the role of the IRS in politics, not to increase it, because we know that the credibility of the tax system, based largely on voluntary compliance, relies on the perception and reality that the IRS is not and will not be used for partisan purposes.

Second, the law is already too complex. We don't need new disclosure rules and more enforcement agencies – we need to consolidate responsibility for enforcement within the FEC, as originally provided for in the Federal Election Campaign Act Amendments of 1974.

We should look to address perceived problems by simplifying and liberalizing the law, not by suppressing political activity or calling for more aggressive enforcement in an area of core First Amendment freedoms. For example, if we are concerned that Super PACs and 501(c)(4) groups are less regulated than candidates and parties, let's simplify and remove or ease restrictions on candidates and parties. The current limit on giving to candidates is $2,600. If that were merely adjusted for inflation since 1974, when Congress first enacted limits, it would now be $4,700. Adjusted for inflation, the annual limit on giving to national parties would not be $32,400, but $94,200. All of the limits should be adjusted for inflation. We should also dramatically raise, or abolish, the limits on coordinated spending between parties and candidates, and the limits imposed by McCain-Feingold in 2003 on state and local parties. It makes no sense to force an artificial barrier between parties and their own candidates.

Congress should also consider lifting the ban on corporate contributions to candidates. Most corporations cannot afford to operate PACs, so the current system favors large corporations and national unions over small business and union locals that cannot afford to operate PACs. Corporate contributions could be subject to the same limits as individuals – there is no reason why a $4,700 from a corporation is more corrupting than a $4,700 contribution from that corporation's president.

All of these steps would help to place political parties and candidate campaigns on more equal footing with Super PACs and 501(c)(4) organizations, drawing more money into these formal structures and away from the other organizations more effectively than devoting more effort to enforcement and reducing First Amendment protections for politically involved citizens and groups.

As limits are adjusted for inflation, we should also raise disclosure thresholds substantially. There is no reason to disclose every $200 contribution. These amounts are not remotely corrupting, hinder serious analysis of donors by swamping observers with information, and invade the privacy of small donors for little or no gain. We should consider renewing the tax credit for small dollar political donations, both making more money available and singling that political participation is a good thing, not a bad thing.

In short, we should be using carrots, not sticks. Doing so is likely to be more effective and it will not do partisan damage to agencies such as the IRS or encroach on First Amendment freedoms.

Political participation is a good thing, and financial participation is an important component of that. Our nation's founders, remember, pledged not just their "lives" and "sacred honor," but also their "fortunes." So let's look for reform that rewards rather than punishes.

Thank you.

APPENDIX

EXCERPTS FROM FEDERAL ELECTION COMMISSION BROCHURE ON COORIDINATED COMMUNCIATIONS AND INDEPENDENT EXPENDITURES

Key Terms

Before discussing the distinctions between coordinated and independent communications, it is helpful to define a few key terms: public communication, express advocacy, and clearly identified candidate.

A public communication is "a communication by means of any broadcast, cable or satellite communication, newspaper, magazine, outdoor advertising facility, mass mailing or telephone bank to the general public, or any other form of general public political advertising." Communications over the Internet are not public communications unless the communications are placed for a fee on another person's web site. 11 CFR 100.26.

A communication "expressly advocates" if it includes a message that unmistakably urges the election or defeat of a clearly identified candidate. See 11 CFR 100.22.

A "clearly identified candidate" is one whose name, nickname, photograph or drawing appears, or whose identity is apparent through unambiguous reference, such as "your Congressman," or through an unambiguous reference to his or her status as a candidate, such as "the Democratic presidential nominee" or "Republican candidate for Senate in this state." 11 CFR 100.17.

Coordinated Communications

When an individual or political committee pays for a communication that is coordinated with a candidate or party committee, the communication is considered an in-kind contribution to that candidate or party committee and is subject to the limits, prohibitions, and reporting requirements of the federal campaign finance law.

In general, a payment for a communication is "coordinated" if it is made in cooperation, consultation or concert with, or at the request or suggestion of, a candidate, a candidate's authorized committee or their agents, or a political party committee or its agents. 11 CFR 109.21. To be an "agent" of a candidate, candidate's committee, or political party committee for the purposes of determining whether a communication is coordinated, a person must have actual authorization, either express or implied, from a specific principal to engage in specific activities, and then engage in those activities on behalf of that specific principal. Such activities would also result in a coordinated communication if carried out directly by the candidate, authorized committee staff, or a political party official. 11 CFR 109.3(a) and (b).

Candidate-Prepared Material

Generally, an expenditure made to distribute or republish campaign material produced or prepared by a candidate's campaign is an in-kind contribution to that candidate, and not an independent expenditure. 11 CFR 109.23. However, exceptions related to volunteer activity for

party committees and candidates may apply. For more information, consult the "Volunteer Activity" brochure.

Three-Prong Coordination Test

FEC regulations establish a three-prong test to determine whether a communication is coordinated. All three prongs of the test—payment, content and conduct—must be met for a communication to be deemed coordinated and thus an in-kind contribution.

Payment Prong

In order to satisfy the payment prong, the communication need only be paid for, in whole or in part, by someone other than a candidate, a candidate's authorized committee, a political party committee, or an agent of the above.

Content Prong

The content prong relates to the subject matter and timing of the communication. A communication that meets **any one** of these four standards satisfies this part of the test:

1. A public communication that expressly advocates the election or defeat of a clearly identified candidate;
2. A communication that is an **"electioneering communication"** as defined in 11 CFR 100.29 (i.e. a broadcast communication that mentions a federal candidate and is distributed to the relevant electorate 30 days before the primary election or 60 days before the general election);
3. A public communication that republishes, disseminates or distributes in whole or in part **campaign materials** prepared by a candidate or a candidate's campaign committee; or
4. A public communication that is:

   a. Made **within 90 days before an election** and:

      - Refers to a clearly identified House or Senate candidate and is publicly distributed in that candidate's jurisdiction; or
      - Refers to a political party, is coordinated with a House or Senate candidate, and is publicly distributed in that candidate's jurisdiction; or
      - Refers to a political party, is coordinated with a political party, and is publicly distributed during a midterm election cycle

   b. Made **120 days before a Presidential primary election through the general election** and:

      - Refers to a clearly identified Presidential or Vice Presidential candidate and is publicly distributed in a jurisdiction before the clearly identified federal candidate's election in that jurisdiction; or
      - Refers to a party, is coordinated with a Presidential or Vice Presidential candidate, and is publicly distributed in that candidate's jurisdiction; or
      - Refers to a political party, is coordinated with a political party, and is publicly distributed during the Presidential election cycle.

For communications that refer to both a party and a clearly identified federal candidate see 109.21(c)(4)(i)-(iv).

Conduct Prong

The conduct prong examines the interactions between the person paying for the communication and the candidate, authorized committee or political party committee, or their agents. A communication satisfies this part of the test if it meets **any one** of the **five standards** regarding the conduct of the person paying for the communication and the candidate, the candidate's committee, a political party committee or agents of the above:

1. If the communication is created, produced or distributed at the **request or suggestion** of the candidate, candidate's committee, a party committee or agents of the above; or the communication is created, produced or distributed at the suggestion of the person paying for the communication and the candidate, authorized committee, political party committee or agent of any of the foregoing **assents** to the suggestion. 11 CFR 109.21(d)(1).
2. If the candidate, the candidate's authorized committee or party committee is **materially involved** in decisions regarding the content, intended audience, means, or mode of the communication, specific media outlet used, the timing or frequency or size or prominence of a communication. 11 CFR 109.21(d)(2).
3. If the communication is created, produced or distributed after one or more **substantial discussions** about the communication between the person paying for the communication or the employees or agents of that person and the candidate, the candidate's committee, the candidate's opponent or opponent's committee, a political party committee or agents of the above. 11 CFR 109.21(d)(3).
4. If the person paying for the communication **employs a common vendor** to create, produce or distribute the communication, and that vendor:
    - Is currently providing services or provided services within the previous 120 days with the candidate or party committee that puts the vendor in a position to acquire information about the campaign plans, projects, activities or needs of the candidate or political party committee; and
    - Uses or conveys information about the plans or needs of the candidate or political party, or information previously used by the vendor in serving the candidate or party, and that information is material to the creation, production or distribution of the communication. 11 CFR 109.21(d)(4).
5. If a person who has previously been an **employee or independent contractor** of a candidate's campaign committee or a party committee during the previous 120 days uses or conveys information about the plans or needs of the candidate or political party committee to the person paying for the communication, and that information is material to the creation, production or distribution of the communication. 11 CFR 109.21(d)(5).

Formal agreement or collaboration between the person paying for the communication and the candidate, authorized committee or political party committee, or their agents, is not required. 11 CFR 109.21(e).

QUESTIONS SUBMITTED BY SENATOR AMY KLOBUCHAR FOR MYTHILI RAMAN, PATRICIA HAYNES, LAWRENCE M. NOBLE, GREGORY L. COLVIN, AND BRADLEY A. SMITH

QUESTIONS FOR THE RECORD
Senate Judiciary Committee
"Current Issues in Campaign Finance Law Enforcement"
April 9, 2013

Senator Amy Klobuchar

1. Executive Branch Role - Given that legislative solutions may be difficult to enact, what the most important steps that executive branch agencies, including the FEC, IRS, and the FCC, should take in providing oversight of the activities of Super PACs and other related groups?

2. Rules on Coordination - Could the IRS or the FEC make stronger rules to curb coordination between outside groups and candidates? What could such rules look like?

3. Impact of Citizens United - There has been a lot of discussion about what the real world impact of *Citizens United* has been and will be going forward.

   - Can you describe in general terms what trends or major shifts you have seen in campaign finance since the Citizens United ruling?

   - What, in your view, has this done to the public's perception of our elections and our government?

QUESTIONS SUBMITTED BY SENATOR CHARLES SCHUMER FOR MYTHILI RAMAN AND PATRICIA HAYNES

Hearing – Current Issues in Campaign Finance Law Enforcement
Senate Committee on the Judiciary, Subcommittee on Crime and Terrorism
April 9, 2013

Senator Charles E. Schumer, Questions for the Record (April 16, 2013)

Questions for Deputy Chief Patricia Haynes (IRS, Criminal Investigation)

1. Acting AAG Raman testified, "An individual or entity seeking to skirt existing legal limitations under the campaign finance laws through contributions to a 501(c) may do so free from public disclosure of donors to the FEC, with a lack of any required disclosure to the IRS coincident with the contribution, and with restrictions on prosecutors' access to any eventual IRS disclosures."

   a. **Deputy Chief Haynes, do you agree with Acting AAG Raman's statement? If not, why not?**

   b. **What changes to current law, regulation and/or practice would permit the IRS and DOJ prosecutors to work together more effectively to ensure enforcement of our campaign finance laws?**

2. I am concerned about social welfare groups engaging in political campaign activities not filing, or filing inaccurate, Form 990s.

   a. **How many social welfare groups that engaged in political campaign activities in 2010, 2011, and 2012 have failed to file the required Form 990s?**

   b. **Were any of these groups notified in 2010, 2011, and 2012 that they may be in violation of the law? If so, how many?**

   c. **What resources is the IRS putting towards making sure that groups claiming to be social welfare organizations file accurate Form 990s?**

   d. **Does the IRS plan, this year, to challenge in federal court the tax-exempt status of any social welfare groups for abusing their tax exempt status by engaging in political campaign activities?**

3. Critics argue that the IRS is failing to adequately enforce current law, particularly in situations where nonprofits are engaging in political activity.

   a. **If a nonprofit social welfare group is, in fact, primarily engaged in political activity, does the IRS have the authority to change the group's tax status? Please elaborate.**

   b. **Has the IRS ever changed a social welfare group's tax status? If so, what was the new tax status? Please elaborate.**

Hearing – Current Issues in Campaign Finance Law Enforcement
Senate Committee on the Judiciary, Subcommittee on Crime and Terrorism
April 9, 2013

Senator Charles E. Schumer, Questions for the Record (April 16, 2013)

Questions for Acting Assistant Attorney, General Mythili Raman (DOJ, Criminal Division)

1. Acting Assistant Attorney General Raman, in your testimony you state, "When the public and law enforcement can see who is making contributions, the Department can better detect, investigate, and prosecute contributions exceeding statutory limits, contributions from banned sources, and bribes."

   How should our disclosure laws be changed to help with enforcement?

2. In your testimony you state that "enforcement of our campaign finance laws is a top priority." At the same time, you state, "An individual or entity seeking to skirt existing legal limitations under the campaign finance laws through contributions to a 501(c) may do so free from public disclosure of donors to the FEC, with a lack of any required disclosure to the IRS coincident with the contribution, and with restrictions on prosecutors' access to any eventual IRS disclosures."

   a. **Do our campaign finance laws create a *disincentive* to filing accurate reports regarding campaign spending? What are options for creating an incentive to filing accurate reports regarding campaign spending?**

   b. **What changes to current law, regulation and/or practice would permit DOJ prosecutors and the IRS to work together more effectively to ensure enforcement of our campaign finance laws?**

3. Foreign citizens, foreign corporations, and foreign labor unions are prohibited from giving or spending money on U.S. elections, but a foreign donor may donate to a U.S. nonprofit. In some cases, the U.S. nonprofit may not know the true source of a donation if a shell corporation or other intermediary is used. The Internet could also be a source of foreign contributions that are hard to trace.

   a. **Does the DOJ have any evidence that foreign money might have been spent on the 2012 elections? If so, please describe the evidence and the amount of money at issue.**

   b. **What is the DOJ doing to prevent foreign money from influencing U.S. elections?**

   c. **What safeguards exist to ensure that a 501(c) engaging in political activity is not accepting and using donations from foreign sources for political activity? Does DOJ have access to information necessary to enforce the ban on use of foreign donations for political activity? Please elaborate.**

RESPONSES OF MYTHILI RAMAN TO QUESTIONS SUBMITTED BY SENATORS SCHUMER AND KLOBUCHAR

Questions for the Record
Mythili Raman
Acting Assistant Attorney General
Criminal Division
U.S. Department of Justice

Subcommittee on Crime and Terrorism
Committee on the Judiciary
United States Senate

"Current Issues in Campaign Finance Law Enforcement"
April 9, 2013

QUESTIONS POSED BY SENATOR CHARLES E. SCHUMER

1. **Acting Assistant Attorney General Raman, in your testimony you state, "When the public and law enforcement can see who is making contributions, the Department can better detect, investigate, and prosecute contributions exceeding statutory limits, contributions from banned sources, and bribes."**

   How should our disclosure laws be changed to help with enforcement?

Response:

The Department's efforts to enforce our campaign finance laws would be assisted by laws designed to provide reasonable public disclosure of large contributions to 501(c) organizations engaged in significant election-related spending by requiring timely reporting of such contributions to the Federal Election Commission (FEC). The Department would further welcome legislation providing a clear and commonsense definition of illegal coordination. We stand ready to assist Congress in developing such measures.

2. **In your testimony you state that "enforcement of our campaign finance laws is a top priority." At the same time, you state, "An individual or entity seeking to skirt existing legal limitations under the campaign finance laws through contributions to a 501(c) may do so free from public disclosure of donors to the FEC, with a lack of any required disclosure to the IRS coincident with the contribution, and with restrictions on prosecutors' access to any eventual IRS disclosures."**

   a. **Do our campaign finance laws create a disincentive to filing accurate reports regarding campaign spending? What are options for creating an incentive to filing accurate reports regarding campaign spending?**

Response:

Because 501(c) organizations may accept unlimited contributions and need not disclose their donors to the FEC, there may be an incentive for donors to circumvent public disclosure requirements by contributing to 501(c) organizations engaged in significant election-related spending, rather than to entities that must disclose their donors to the FEC. Moreover, the influx of unlimited and undisclosed money to outside organizations, and opaque rules regarding what constitutes coordination, may create an incentive for campaigns to coordinate their activities with these groups. However, such coordination may turn expenditures by outside organizations into contributions to the campaign—contributions that may be prohibited because they exceed the limitations on amounts of contributions or because they come from prohibited sources. This could be addressed by a clear and commonsense definition of illegal coordination, and by requiring timely reporting to the FEC of large contributions to 501(c) organizations engaged in significant election-related spending. The Department recognizes that disclosing the names of donors to 501(c) groups is a complex issue, and is ready to assist the Committee in developing measures that are narrowly tailored to the goal of ensuring that our campaign finance laws are not circumvented.

b. What changes to current law, regulation and/or practice would permit DOJ prosecutors and the IRS to work together more effectively to ensure enforcement of our campaign finance laws?

Response:

As noted above, a law requiring timely reporting to the FEC of large contributions to 501(c) organizations engaged in significant election-related spending, and a clear and commonsense definition of illegal coordination, would assist the Justice Department's efforts to prosecute violations of our campaign finance laws, where appropriate and consistent with the Principles of Federal Prosecution.

3. Foreign citizens, foreign corporations, and foreign labor unions are prohibited from giving or spending money on U.S. elections, but a foreign donor may donate to a U.S. nonprofit. In some cases, the U.S. nonprofit may not know the true source of a donation if a shell corporation or other intermediary is used. The Internet could also be a source of foreign contributions that are hard to trace.

a. Does the DOJ have any evidence that foreign money might have been spent on the 2012 elections? If so, please describe the evidence and the amount of money at issue.

Response:

We cannot comment on the existence of uncharged allegations or investigations. However, the Department has charged two cases involving illegal contributions of foreign funds in prior election cycles. One case involved contributions to an unwitting federal candidate in South Carolina from 2006 to 2009. The defendant in that case was convicted by a jury on March 1, 2013. The other case involved a Jordanian national who allegedly made contributions in the names of others in 2007 and 2008 to three

unwitting Presidential campaigns and an unwitting Florida state campaign. The charges against that defendant remain pending.

b. What is the DOJ doing to prevent foreign money from influencing U.S. elections?

Response:

The Department is responding to the challenge of potential foreign influence over elections at any level of American government by continuing to train its election crime prosecutors and investigators regarding the issue; by working with law enforcement partners to insure that intelligence concerning potential illegal conduct is properly shared with criminal investigators; and, if wrongdoing is detected, by bringing criminal prosecutions, where appropriate and consistent with the Principles of Federal Prosecution, against those funneling foreign money into U.S. elections.

c. What safeguards exist to ensure that a 501(c) engaging in political activity is not accepting and using donations from foreign sources for political activity? Does DOJ have access to information necessary to enforce the ban on use of foreign donations for political activity? Please elaborate.

Response:

501(c) organizations are required, on an annual basis, to describe their spending and to disclose their donors to the IRS. The IRS may thus be in a position to identify where a 501(c) organization engaged in election-related spending has accepted contributions from foreign sources, unless the 501(c) organization is falsely reporting donor information. That contribution information is not available to the Department's election crime prosecutors and investigators outside the context of a specific investigation.

QUESTIONS POSED BY SENATOR AMY KLOBUCHAR

4. **Executive Branch Role - Given that legislative solutions may be difficult to enact, what the most important steps that executive branch agencies, including the FEC, IRS, and the FCC, should take in providing oversight of the activities of Super PACs and other related groups?**

Response:

Because the FEC, IRS and FCC operate independently of the Department of Justice, the Justice Department is not in a position to comment on what, if any, additional steps those agencies should take in providing oversight of the activities of Super PACs and related groups. The Department, however, stands ready to work with those agencies, where appropriate and consistent with the Principles of Federal Prosecution, to continue to vigorously investigate violations of our campaign finance laws and our anti-corruption laws. We also stand ready to assist Congress in developing legislation that could improve the Executive Branch's oversight capabilities in this area.

5. **Rules on Coordination - Could the IRS or the FEC make stronger rules to curb coordination between outside groups and candidates? What could such rules look like?**

Response:

It would not be appropriate for the Department to comment on the independent regulatory efforts of the IRS and the FEC. However, as a general matter, the Department's efforts to enforce our campaign finance laws would be assisted by laws designed to provide reasonable public disclosure of large contributions to 501(c) organizations engaged in significant election-related spending by requiring timely reporting of such contributions to the FEC. The Department's enforcement efforts would also benefit from a clear and commonsense definition of illegal coordination. We stand ready to assist Congress in developing legislation in this area.

6. **Impact of Citizens United - There has been a lot of discussion about what the real world impact of Citizens United has been and will be going forward.**

   a. **Can you describe in general terms what trends or major shifts you have seen in campaign finance since the Citizens United ruling?**

Response:

The Department has worked aggressively to combat corruption and the appearance of corruption through rigorous enforcement of the limitations on the amounts and sources of contributions set forth in our campaign finance laws. Those limitations have formed the basis upon which we have brought numerous federal criminal cases, with most involving the use of conduit contributions to disguise the true source and amount of illegal contributions.

The trend since *Citizens United* is that very large sums are now raised and spent by Super PACs and certain 501(c) organizations. These Constitutionally-protected expenditures are not "contributions" to a campaign and, thus, are not subject to the source and amount limitations that have traditionally provided the basis for criminal charges.

b. What, in your view, has this done to the public's perception of our elections and our government?

Response:

In the wake of *Citizens United*, the Department is concerned that the lack of a clear and commonsense definition of illegal coordination between campaigns and independent expenditure entities, and the lack of public disclosure of large contributions to 501(c) organizations engaged in significant election-related spending, have increased the opportunities for unseen quid pro quo corruption. Such corruption, where it occurs, undermines the fairness of our elections and the legitimacy of our government.

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

NATIONAL DIRECTOR
FOR LEGISLATIVE
AFFAIRS

The Honorable Patrick Leahy
Chairman
Committee on the Judiciary
United States Senate
Washington, DC 20510

Dear Mr. Chairman,

I apologize you have not received responses from the IRS to several of the Questions for the Record (QFRs) submitted by your Committee Members. Ms. Haynes, the witness at the April 9 hearing, is not a subject matter expert in this area. Additionally, she has left the Agency; therefore, this letter is in response to those QFRs, and we will not be providing any additional information.

I assure you, we take these matters very seriously. I am available to discuss the matter further, should you have concerns.

Sincerely,

Leonard T. Oursler

National Director for
Legislative Affairs

RESPONSES OF LAWRENCE M. NOBLE TO QUESTIONS SUBMITTED BY SENATOR KLOBUCHAR

Response of Lawrence M. Noble
to
QUESTIONS FOR THE RECORD
Senate Judiciary Committee
"Current Issues in Campaign Finance Law Enforcement"
April 9, 2013

Senator Amy Klobuchar

1. **Executive Branch Role - Given that legislative solutions may be difficult to enact, what the most important steps that executive branch agencies, including the FEC, IRS, and the FCC, should take in providing oversight of the activities of Super PACs and other related groups?**

   The most important step is for executive branch agencies to interpret and enforce the laws that Congress has already enacted in a clear, fair and forceful manner consistent with congressional intent.

   While the FEC has never been an overly aggressive enforcement agency, over the last 10 years it has increasingly become dysfunctional, undermining the very law it is charged with enforcing. The six-member Commission routinely splits 3-3 on important issues regarding the regulation of SuperPACs and other groups. Where the FEC has been able to come to some decisions, the result has usually been to officially weaken previously established prohibitions, limitations and disclosure requirements. For example, through both actions, as well as deadlocks preventing action, it has narrowed and effectively nullified rules that would have required more disclosure of the source of funds for political activity. Likewise, it promulgated and then interpreted coordination rules so that the laws prohibiting coordination between candidates and independent expenditure groups that raise and spend unlimited soft money no longer contain meaningful limitations on candidates working closely with these organizations. The FEC's dysfunction has even prevented it from undertaking a rulemaking regarding the long-standing prohibition on direct corporate and union fundraising for candidates. In addition, the FEC has launched few investigations, let alone actually sought enforcement of the law, in recent years.

   The IRS's function is limited to ensuring that certain groups claiming tax exempt status comply with the tax laws. A lack of clarity in the IRS rules regarding what is appropriate activity for 501(c)(4), and a lack of enforcement of the rules that do exist, has led to many organizations undertaking political activity that is prohibited under the Internal Revenue Code. Unless and until the IRS makes clear the tax exempt organizations will not be permitted to undertake political activity that does not comply with the Internal Revenue Code, these organizations will continue to abuse their tax-exempt status.

2. **Rules on Coordination - Could the IRS or the FEC make stronger rules to curb coordination between outside groups and candidates? What could such rules look like?**

FECA has long required that expenditures made "in cooperation, consultation, or concert with, or at the request or suggestion of, a candidate" or his or her agent," be treated as a contribution, and thus subject to limitations and prohibitions of the law. From the Supreme Court's 1976 ruling in *Buckley v. Valeo,* where the Court held that individuals can make unlimited independent expenditures in elections, to its 2010 ruling in *Citizens United,* holding that corporations can also make such unlimited independent expenditures, the Court has always been clear that those expenditures must be undertaken independently of candidates. In fact, the Supreme Court has consistently envisioned a campaign finance world where there is no coordination of any type between a person or entity making an independent expenditure and the candidate. The reality, however, is quite different.

Despite the requirements of the law and the Supreme Court's assumption that independent expenditures would be truly independent of a candidate, the FEC has defined coordination narrowly. The FEC allows the candidate to appear at events and fundraise for an independent expenditure committee (SuperPAC) whose sole function is to support that candidate, even where the committee was started and is run by former staffers for the candidate. Under the FEC rules, unlimited corporate donations can be solicited at a fundraising event featuring the candidate, as long as the candidate employs the fig-leaf of a statement that he or she is only allowed to ask for money under the federal limits and prohibitions. The result is what is commonly referred to as the candidate's own "independent expenditure committee." The fact that that the FEC allows a candidate to have what appears to be the candidate's own independent expenditure committee shows how far the FEC has moved away from the concepts behind the Supreme Court's distinction between coordinated and independent expenditures.

The FEC could begin to rectify the problem by coming up with stronger coordination rules. Among the more important elements of such a rule would be:

- Application to communications that promote or support the candidate, or attacks or opposes his or her opponent, at any time, or refers to the candidate or an opponent of the candidate in a set time period preceding election.

- Actions triggering coordination would include:

    - The organization making the expenditure is directly or indirectly formed or established by, or at the request or suggestion of, or with the encouragement or approval of, the candidate or his or her agent.

    - A candidate or his or her agent raises funds, assists in the raising of funds, or appears at events for an entity making expenditures supporting that candidate or opposing his or her opponent.

- The person or entity making the expenditure has had communications with the candidate or his or her agent about the candidate's campaign needs, fundraising, projects, plans, activities, strategies or messaging.

- The person or entity making the expenditure utilizes someone who is or has been has been employed or retained as a political, media, or fundraising adviser or consultant for the candidate or has held a formal position with a title for the candidate or who has provided professional services involving advertising, messaging, strategy, policy, polling, allocation of resources or fundraising, to the candidate during the election cycle.

While this is not intended to be an all-inclusive list, using this framework would require the separation between the candidate and independent expenditure committees that the Supreme Court assumes exists and the law requires.

3. **<u>Impact of Citizens United</u> - There has been a lot of discussion about what the real world impact of *Citizens United* has been and will be going forward.**

   - **Can you describe in general terms what trends or major shifts you have seen in campaign finance since the Citizens United ruling?**

While *Citizens United,* for the first time, allowed corporations and labor unions to make independent expenditures in federal elections, its impact has been far greater than the legal holding due to how it is being applied. *Citizens United* is directly responsible for those corporate or union communications that expressly advocate the election or defeat of a federal candidate, where the corporation or union makes the expenditure directly and is identified. The rise of SuperPACs, which are political committees that can use corporate or union money to make independent expenditures, is due to *Speechnow.org v. FEC,* a 2010 decision of the U.S. Court of Appeals for the District of Columbia Circuit. SuperPACs, however, still disclose their donors. Therefore, as a direct result of *Citizens United* and *Speechnow,* we have seen corporate and union money used to directly advocate the election or defeat of federal candidates.

However, the biggest impact from *Citizens United* is the tremendous increase in independent expenditures by 501(c)(4) organizations (and other groups) who can now utilize unlimited corporate and union funds for such ads and are not being required to disclose the source of those funds. The fact that they are not being required to disclose the source of their funding is due to the failure of the FEC to enforce the disclosure rules for independent expenditures. The Supreme Court, in *Citizens United,* assumed that the source of funding for these independent expenditures would be disclosed. But the FEC's application of the law has prevented such disclosure.

Additionally, as discussed above, we have seen the rise of the so-called "candidate independent expenditure" groups, which use unlimited individual and corporate funds, relying on the FEC's very narrow application of the coordination rules. Without Congress or the FEC taking action, we should expect to see an increase in this activity.

- **What, in your view, has this done to the public's perception of our elections and our government?**

The current state of our campaign finance system is undermining the public's trust in our government. Rather than a democracy where the government gets its authority from the consent of the governed, the public sees a government that operates based on the consent of well-funded special interests. Regardless of whether an elected official voted for a bill because he or she truly believed in its merits, the public now assumes that Congress is responsive only to those who spend large sums of money to get candidates elected. This cynicism will continue to grow and undermine the public's trust in, and respect for, our elected leaders. Inevitably, people will question the value of their vote if they believe that who is elected is determined by who has the wealthiest backers and that, once in office, elected officials respond to those who funded their campaigns. This undermines the very foundation of our democracy.

RESPONSES OF GREGORY L. COLVIN TO QUESTIONS SUBMITTED BY SENATOR KLOBUCHAR

QUESTIONS FOR THE RECORD
Senate Judiciary Committee
"Current Issues in Campaign Finance Law Enforcement"
April 9, 2013

Senator Amy Klobuchar

Responses from Gregory L. Colvin, Adler & Colvin, San Francisco

1. *Executive Branch Role - Given that legislative solutions may be difficult to enact, what are the most important steps that executive branch agencies, including the FEC, IRS, and the FCC, should take in providing oversight of the activities of Super PACs and other related groups?*

Since my law practice is devoted to nonprofit, tax-exempt law, I will focus on the steps the Internal Revenue Service can take. As you know, my testimony and my supplemental statement address the question of IRS oversight in depth and I will not repeat all that here. In short, I believe that the IRS, exercising its regulatory authority, could and should:

A. Reconsider its interpretation of the primary purpose test for Section 501(c)(4) and other non-charitable 501(c) exempt organizations, so that the upper limit for political campaign activities is reduced from "less than primary" to "insubstantial." This would be more consistent with other precedents requiring that "private benefit" activities within a 501(c)(4) entity be limited to an insubstantial level, such as the *Vision Service Plan* decision. Following those precedents, the presence of a single non-exempt purpose, if substantial in nature, would defeat the entity's tax exemption. Revenue Ruling 81-95 would need to be withdrawn and a new ruling issued to clarify the tax treatment of political campaign activities, and the Service should make plain that this principle applies similarly to other tax-exempt classifications, such as (c)(5) labor unions, (c)(6) trade associations, and (c)(7) social clubs. Otherwise, the public interest (c)(4) groups would be disadvantaged compared to the other 501(c) organizations that serve special interests and are expected to be, in the wake of *Citizens United*, even more active in politics.

B. Promulgate regulations defining "political intervention" clearly and consistently for all parts of the Internal Revenue Code that rely upon that term, including the prohibition in Section 501(c)(3), the limitation applicable to other Section 501(c) categories, and the denial of business expense deduction under Section 162(e). The vague and uncertain "facts and circumstances" approach used by the IRS should be replaced with bright line definitions, safe harbor exceptions, and illustrative examples, patterned after the public charity and foundation lobbying regulations that the Service issued in 1990. The 2013-14 Priority Guidance Plan for the IRS and Treasury should launch this regulations project, with public hearings and other input, and a target date of January 1, 2016, for completion.

C. As an interim measure, provide bright-line definitions and exceptions to distinguish issue advocacy from political campaign advertising for all purposes under the Internal Revenue Code, by issuing a new Revenue Ruling before January 1, 2014. The two multiple-factor tests that presently apply to issue ads, found in Revenue Rulings 2004-6 and 2007-41, should be withdrawn and replaced with a single test. This would allow the Service to put an improved rule in place for issue ads in the 2014 elections, while it pursues the comprehensive regulatory reform to be finished in time for the 2016 campaign season.

2. *Rules on Coordination - Could the IRS or the FEC make stronger rules to curb coordination between outside groups and candidates? What could such rules look like?*

The FEC has greater expertise than does the IRS when it comes to distinguishing independent from coordinated expenditures, and so the FEC should take the lead on forging stronger rules. Under federal tax law, independent and coordinated political expenditures are treated equally as political intervention, so the IRS has not needed to define them separately. However, if the FEC could provide improved guidance on the question of what constitutes "coordination," defining coordinated expenditures as contributions to the candidates involved, it would be a simple matter for the IRS to follow suit. Hopefully, state election commissions would do so as well. Tax-exempt organizations in particular need to know what contacts and communications they may have with candidates without crossing the line into coordination. For example, a charity should be able to inject its issues into the campaign by asking candidates to take a position on fair pay for working women. However, the charity must avoid paying for any communications to voters on such issues that are improperly coordinated with the candidates.

3. *Impact of Citizens United - There has been a lot of discussion about what the real world impact of Citizens United has been and will be going forward.*

   - *Can you describe in general terms what trends or major shifts you have seen in campaign finance since the Citizens United ruling?*
   - *What, in your view, has this done to the public's perception of our elections and our government?*

I believe we have seen a range of public perceptions, from greater enthusiasm for civic engagement in some quarters to greater apathy in others. Internet technology has made receiving information and acting upon it much easier and cheaper, and there is, at least for now, a sense that grass roots groups can take on the big moneyed interests and compete for political influence at many levels and in many segments of government. On the other hand, as organizing methodologies become more sophisticated, the level of investment needed to compete will be an increasingly high barrier to entry.

From my perspective representing tax-exempt organizations and their donors, the trends I have seen since *Citizens United* (and the related *SpeechNow* decision allowing the formation of SuperPACs) are as follows.

- We have seen a cultural shift, by a small but growing set of very wealthy individuals, toward a willingness to invest very large amounts of their own money to influence federal, state, and local elections, including by running for office themselves.
- A few large corporations and other businesses have begun to test the waters, making contributions to independent expenditure committees, and more are sure to follow in future years. Even if most businesses refrain from making obvious political expenditures in their own names, those that do will figure out how to realize an enormous return on their investments in political influence.
- Labor unions, who did not seek or want the *Citizens United* ruling, have had to increase spending from their general treasury funds to try to match business-side spending, focusing on ground operations now that they can reach out beyond their members to the general public.
- Generally, the number of donors and amounts of money raised in both direct and independent contributions has increased, due not only to *Citizens United* and *SpeechNow* but also to the efficiency of Internet solicitation and the use of critical issues to motivate people to give.
- The overall escalation of campaign spending at all levels of government has increased the price of running for office, the time needed to court large donors, and the need to develop outside allies to augment the candidates' and parties' own efforts.
- Certainly the ability of very large donors to invest in outside support for their favored political party nominees has led to the continuation of certain campaigns for nomination far past the point when they would otherwise be viable. An article in the *Columbia Journalism Review* suggested that outside spending after *Citizens United* has had more impact in primary elections than in general elections so far.[1]
- Before the *Citizens United* decision, nonprofit as well as business corporations were prohibited from making independent expenditures in federal elections and in half of the states. When that prohibition fell away, the weakness of the IRS limitations on political spending by Section 501(c) organizations was exposed.
- Charitable 501(c)(3) organizations are still banned from political intervention by the tax code, but the IRS definition of that term is vague and amorphous. Most charities stay far away from election activity, but some are getting more aggressive with voter guides, candidate litmus tests, and even sermons that endorse candidates.
- Those 501(c) organizations NOT banned from political spending by the tax code, but simply limited by the "less than primary" (49%) test, have become the

[1] http://www.cjr.org/united_states_project/how_super_pacs_succeeded_in_20.php?page=all

vehicles of choice for donors wishing to avoid public disclosure. They include (c)(4) social welfare groups and (c)(6) business and professional associations.

- While the new (c)(4) funds affiliated with SuperPACs may have become the most controversial, the (c)(6) category is the most likely to be exploited by business corporations seeking anonymity because their trade associations already have huge primary lobbying operations that provide natural cover for secondary independent political expenditures. Further, a (c)(6) can overtly pursue business interests; it has no requirement to promote social welfare purposes as a (c)(4) does.
- As I detail in my main testimony, the inability of the IRS, so far, to regulate 501(c) political spending qualitatively (allowing thinly-disguised and targeted "issue" ads) or quantitatively (allowing 49% to be spent on express political campaigning) has led to massive abuses and a crisis in public trust for the nonprofit sector.

RESPONSES OF BRADLEY A. SMITH TO QUESTIONS SUBMITTED BY SENATOR KLOBUCHAR

ANSWERS OF BRADLEY A. SMITH
CHAIRMAN, CENTER FOR COMPETITIVE POLITICS
to
QUESTIONS FOR THE RECORD
Senate Judiciary Committee
"Current Issues in Campaign Finance Law Enforcement"
April 9, 2013

Senator Amy Klobuchar

April 22, 2013

1. Executive Branch Role - Given that legislative solutions may be difficult to enact, what the most important steps that executive branch agencies, including the FEC, IRS, and the FCC, should take in providing oversight of the activities of Super PACs and other related groups?

ANSWER:

I would begin by taking issue with the idea that there are "solutions" necessary, implying some "problem." The "problem" appears to be the claim that Americans do not know who is funding elections. However, FEC numbers released in the last week show that this is even less of an issue than it appeared on April 9.

Final FEC statistics released on April 19 are that $7.136 billion was raised and $7.005 billion spent on the 2012 federal elections. Of that, less than $300 million, or less than 4.3 percent, was spent by organizations that do not disclose all of their donors to the FEC. *See* Federal Election Commission, *FEC Summarizes Campaign Activity of the 2011-2012 Election Cycle*, April 19, 2013.

As I noted in my prepared testimony, even this low percentage exaggerates the percentage of "undisclosed" donors, since in fact many of these spenders and their agenda were well known to the public, such as Planned Parenthood or the U.S. Chamber of Commerce.

Chairman Whitehouse has commented at several points in this hearing alleging a "pattern" of "often" using "shell corporations" to hide a donor's identity. But in fact, there is no evidence of any such pattern or that it is used "often." In fact, there have been three reported cases in the 2012 cycle of using "shell" corporations; in the most widely reported case, that of W. Spann LLC, the donor and his attorney who incorporated the "shell" appear to have been under the impression that the use of a shell was legal, undoubtedly because much of the hysteria about "dark money" has implied that such activity was clearly legal. In each case, the identity of the person funding the "shell" was discovered and publicized in the press within 72 hours. Meanwhile, candidate campaigns, party researchers, and various so-called "good government" groups (many of which do not reveal the names of their donors) routinely review campaign finance reports looking for illegal activity, so there is little reason to think that there are frequent instances of such conduct going undetected. In short, this is simply not a great problem, unless one has the unrealistic expectation that no person will ever violate a law.

The second alleged "problem" appears to be the notion that many groups, when filing with the IRS, are not properly defining their anticipated activities. However, that claim

seems to rest on a legal conclusion that is at best in dispute. It is not at all clear that groups are making, as stated by Chairman Whitehouse, false statements to the IRS. We should be careful about pronouncing people guilty before we gather the facts.

The Federal Election Campaign Act states that the Federal Election Commission "shall have exclusive jurisdiction with respect to civil enforcement" of our nation's campaign finance laws (most violations are civil violations, not criminal). The FEC is designed for this in ways that the IRS, the FCC, the SEC, and other federal agencies are not – in particular through its bipartisan structure and conciliation procedures.

It is particularly important that the IRS not be converted into a campaign finance enforcement agency. The IRS is responsible for the tax code, and the history of presidential abuse of the IRS and the tax code to target political opposition, through both Democratic and Republican administrations, make it important that Congress not look to the IRS to address perceived issues in campaign finance.

Conspicuously absent in this hearing is any claim that the IRS is acting in a political manner now, or failing to efficiently collect revenue due the U.S. government. In short, this hearing, to the extent it involves the IRS, is about turning the IRS into a mechanism to police perceived campaign finance issues. This is a serious mistake.

If we are actually concerned that some organizations are reporting under Section 501(c) of the Internal Revenue Code rather than Section 527 – which has no impact on revenue collection – then the IRS could take action to make its definition of political activity more clear. But there is no evidence that, from a perspective of revenue collection and enforcement, its current definition is a problem. If it be insisted that the IRS change this definition, however, the best and most easily done method would be to adopt the definition used by the FEC, based on numerous Supreme Court cases beginning with *Buckley v. Valeo,* 424 U.S. 1. This would bring the IRS definition into line with the FEC definition which, because it is shaped by Supreme Court precedent, cannot be easily changed. It would also keep the IRS out of partisan politics.

Similarly, the FCC has also been abused over the years for partisan purposes, and ought not be dragged into refighting the wisdom of Supreme Court decisions or used to try to regulate political speech.

As I noted in my prepared testimony, recent efforts to use the FCC and the IRS for campaign finance regulation have not gone well. Similarly, as I and my colleague Allen Dickerson demonstrate in our recent paper, *The Non-Expert Agency: Using the SEC to Regulate Partisan Politics*, 3 Harvard Business Law Review __ (forthcoming 2013, available in draft at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2239987, the SEC is a poor vehicle for campaign finance enforcement.

As for the FEC itself, that agency should move to revise its advice on member solicitations for political action committees, which were written prior to the U.S. Court of Appeal's 9-0 decision authorizing so-called "Super PACs" in *SpeechNow.org v. FEC.* Revising member solicitation rules for Super PACs that support only or predominantly one candidate would largely solve the concerns that have sometimes been voiced about "coordination" between candidates and "Super PACs."

At the present time, there is more disclosure of campaign sources than ever before in our history. We know that disclosure discourages political participation: that is why groups that themselves call for others to disclose their donors, such as the Center for Reform and Ethics in Washington ("CREW") and Public Citizen do not disclose their own donors. (CREW, for example, is currently resisting in federal court a subpoena for the names of its donors, *see* Reply Brief of Non-Party CREW to Quash Subpoena, *Castro v. Sanofi Pasteur Inc.*, No. 1:12-mc-00629 (D.D.C.) (arguing that compelled disclosure of donors would have "a potential for chilling the free exercise of political speech and association guarded by the First Amendment.")) The Supreme Court has recognized that danger repeatedly, *see e.g. Buckley v. Valeo,* 424 U.S. at 64 ("We long have recognized that significant encroachments on First Amendment rights of the sort that compelled disclosure imposes cannot be justified by a mere showing of some legitimate governmental interest."), *Gibson v. Florida Legislative Comm.,* 372 U. S. 539 (1963); *NAACP v. Button,* 371 U. S. 415 (1963); *Shelton v. Tucker,* 364 U. S. 479 (1960); *Bates v. Little Rock,* 361 U. S. 516 (1960);

NAACP v. Alabama, 357 U. S. 449 (1958). Modern research shows that that concern is well founded. *See* Alexandre Couture Gagnon & Filip Palda, *The Price of Transparency: Do Campaign Finance Disclosure Laws Discourage Political Participation by Citizens' Groups?,* 146 Public Choice, 353 (2011); Jeffrey Milyo, *Campaign finance red tape: strangling free speech and political debate*, Institute for Justice (2007).

At this point, I think one would be hard pressed to make a case that non-disclosure of political donors is more of a problem than non-disclosure of journalist sources or Members' private conversations and meetings. There are costs inherent in pressing for still more compulsory disclosure and threatening criminal investigations, tax audits, and denial of otherwise proper broadcast or other licenses, and little benefit to be gained.

Chairman Whitehouse seems to presume in his comments that there is some regularly occurring underlying conduct, such as the alleged false speech mentioned frequently in the hearing, that is illegal and not constitutionally protected. Even if true, it does not mean that the government has carte blanche to investigate and regulate the speech of innocent Americans however it chooses, in the name of preventing an underlying crime. For example, mail fraud is illegal and not constitutionally protected per se, but no one would seriously suggest that we should require all Americans to disclose all items put in the mail to help fight alleged mail fraud.

The failure to consider the actual dimensions of disclosure and the amount of disclosure already required by law; the inability to tie it to corruption of the political process; the

unsupported assertions of large scale use of shell corporations; and the tone of hostility toward the speech and in particular the speakers, noted in several asides about the *Citizens United* case, makes this enterprise begin to look like a partisan witch hunt. This partisan approach and open hostility to dissenting voices will damage, not enhance, public confidence in the integrity of officeholders.

2. Rules on Coordination - Could the IRS or the FEC make stronger rules to curb coordination between outside groups and candidates? What could such rules look like?

ANSWER

Investigations of alleged "coordination" are among the most intrusive that occur in the campaign finance realm. Such investigations typically require review of internal political strategy memoranda, confidential conversations, private polling data, and extensive review of documentary and other evidence.

Thus, it is not surprising that no definition of "coordination" has been devised that satisfies anything close to a majority. Recall that even as so-called "reform" organizations complained that the FEC's coordination criteria were too lax in the 1990s, the Supreme Court struck down the FEC's interpretation of its own coordination rules as unconstitutional, *Colorado Republican Federal Campaign Committee v. FEC,* 518 U.S. 604 (1996), and a lower federal court struck down another FEC interpretation three years later in *FEC v. Christian Coalition,* 52 F. Supp. 2d 45 (1999).

Congress attempted to re-write the rules itself as part of the Bipartisan Campaign Reform Act of 2002, only to finally give up when it could not reach agreement, and simply order the FEC to write new rules.

The purpose of anti-coordination rules is widely misunderstood. For example, it is frequently held up as evidence of "coordination" that independent spenders are run by persons known to have previously supported the candidate supported by the group, or by known political partisans. But that merely states the obvious – independent campaigns are not going to be run by persons who do not have a) political experience, and b) views in support of those the group supports. The purpose of regulations preventing "coordination" is to prevent express conversations between parties that would provide opportunities for direct quid pro quo exchanges. As analyses of the 2012 election come out, it becomes clear that in fact there is no evidence of substantial illegal coordination, and that independent expenditures are indeed not as effective as direct candidate expenditures.

As noted above, the IRS should play no role in enforcement of campaign laws. However, also as noted, the FEC could largely address the claims of improper coordination by changing its solicitation rules, which were written before *SpeechNow.org v. FEC,* which allowed "Super PACs." Currently, the rules allow a candidate to appear at a fundraiser for a PAC and solicit funds up to the limits up to the amounts permitted in the Act. This made sense at the time adopted but with the advent of single-candidate independent expenditure committees (Super PACs) may no longer be appropriate. This

is a relatively simple regulatory fix that so far has been blocked by Commissioners on the FEC who insist that reform of disclosure regulation must include the types of measures that Congress has so far resisted in the form of the various failed versions of the "DISCLOSE Act." The Center for Competitive Politics would provide detailed recommendations to the FEC if it were to undertake a properly limited rulemaking to revise the regulations at 11 CFR 300.

3. Impact of Citizens United - There has been a lot of discussion about what the real world impact of *Citizens United* has been and will be going forward.

    - Can you describe in general terms what trends or major shifts you have seen in campaign finance since the Citizens United ruling?

ANSWER

The biggest effect of *Citizens United* and *SpeechNow.org v. FEC* has been to help bring more seats into play and level the playing field for challengers. In both 2010 and 2012 we have seen far more competition for seats, especially in the House. Moreover, "Super PACs" have spent more heavily for challengers than traditional donors and spenders. In 2010, for example, Super PACs leveled the partisan playing field both on an overall basis, and in numerous specific races. For a few specific examples, including overall spending equalization between the two major parties, *see* Bradley A. Smith, *Super PACs Level the Playing Field,* U.S. News & World Report, Jan. 13, 2012, available at http://www.usnews.com/debate-club/are-

super-pacs-harming-us-politics/super-pacs-level-the-playing-field. Again in 2012, Super PACs provided new opportunities for challengers and helped to equalize spending in the presidential race between the President, who was able to spend all of his primary money attacking his Republican challenger, and the challenger, who had to use his primary funds in a primary election. Substantial Democratic spending margins in the elections of 2004 and 2008 gave way to a more equal distribution of spending in 2012.

Total Super PAC and 501(c) spending, which existed before 2010 in the form of "issue advocacy," and which are not of *Citizens United* but of *Buckley v. Valeo* and *SpeechNow.org*, appear to have accounted for approximately 15 percent of all spending in 2012. Since much of this existed prior to *SpeechNow.org,* we can safely assume that *SpeechNow.org* has accounted for some growth in expenditures (a good thing, as higher campaign spending has been shown to create a better informed electorate), but it has not created an "explosion" (or any of the other colorful terms we hear) in spending – perhaps as much as 10 percent of total spending can be attributed to *SpeechNow.org* and *Citizens United.* Spending by for-profit corporations, the primary result of *Citizens United,* appears to have been well under five percent of total spending. Thus these two decisions are important decisions in increasing political spending (as noted, empirically a good thing for those who care about an informed electorate) and enforcing First Amendment rights, but they are not the earth-shattering decisions they are sometimes portrayed as being. As noted, they also appear to have helped to level the playing field between incumbents and challengers, and between political parties, and to have made

more races competitive.

- What, in your view, has this done to the public's perception of our elections and our government?

ANSWER

At this point, the question cannot be answered with any certainty. There has been little analysis and too little time to make serious judgments, given the numerous factors that affect public confidence in government. The members of this panel, myself included, and the Members of this Committee and the entire Senate will, I think, see what they want to see.

Historically, however, we know that public perception of elections and government has declined in the aftermath of major campaign "reform" efforts aimed at restricting spending and contributions and reducing participation. Public trust in government dropped sharply after passage of FECA in 1971, after the FECA Amendments in 1974, and after passage of the Bipartisan Campaign Reform Act in 2002. *See* John Samples, The Fallacy of Campaign Finance Reform 114-15 (2006). Conversely, public trust and confidence in government has typically gone up during periods of rapid increases in political spending, such as during the "soft money" heyday of the 1990s.

In my view, *Citizens United* has had little effect on public perception of government. I have yet to meet more than the barest handful of people whose opinions have changed. Democrats tend to believe that Republicans are corrupt, but not that Democrats are. Republicans think the opposite. Some people believe that *Citizens United* is corrupting politics. Others

believe that efforts to "fix" *Citizens United,* such as the so-called DISCLOSE Act, or these hearings themselves, are evidence of corrupt government being used for partisan advantage.

What we do know is that voter turnout has been high in both the 2010 and 2012 elections; and that the elections have presented more of a clear choice to Americans than most elections, and especially in 2010, a more serious discussion of the role of government in the United States than we have seen in many election cycles.

Partisan efforts to suppress political speech will not increase trust in government or the people's perception of government.

MISCELLANEOUS SUBMISSIONS FOR THE RECORD

March 22, 2012

Hon. Douglas H. Shulman
Commissioner
Internal Revenue Service
Room 3000 IR
1111 Constitution Avenue, N.W.
Washington, DC 20224

Lois Lerner
Director of the Exempt Organizations Division
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Re: Petition for rulemaking on candidate election activities by Section 501(c)(4) groups

Dear Commissioner Shulman and Director Lerner:

On July 27, 2010, Democracy 21 and the Campaign Legal Center submitted to the Internal Revenue Service a "Petition for Rulemaking on Campaign Activities by Section 501(c)(4) Groups."

The Petition challenged as contrary to law the existing regulations that define eligibility for an organization to qualify for section 501(c)(4) tax-exempt status. The Petition called on the IRS to initiate a rulemaking proceeding to revise and clarify its regulations regarding the extent of candidate election activities that a "social welfare" organization can engage in under 26 U.S.C. § 501(c)(4).

Since then, we have heard nothing from the IRS to indicate that such a rulemaking is under consideration.

Meanwhile, developments in the course of the 2012 national elections have served to underscore the fact that inadequate and flawed IRS regulations are facilitating widespread misuse of the tax laws by organizations claiming tax-exempt status under section 501(c)(4) in order to keep secret the donors financing their candidate campaign-related expenditures.

This is seriously undermining the integrity of the tax laws and the credibility of the nonprofit sector. According to a column in *Roll Call*:

> "Charitable organizations depend on the confidence and trust of the public for support," said Diana Aviv, president and CEO of Independent Sector, which represents the nonprofit and philanthropic community. Campaign spending by nonprofits, she added, could pose "a serious reputational risk" to the sector.[1]

We are writing again to strongly urge the IRS to act on our Petition promptly and initiate a rulemaking proceeding. The IRS must take steps to properly interpret and enforce the tax law and stop these abuses from continuing to explode in our elections.

Recently, a group of Democratic Senators and a group of Republican Senators have each separately written to the IRS, both complaining about the agency's administration of section 501(c)(4). One group of Senators argues that the agency is too intrusive in its inquiries into the candidate election activities of applicants for 501(c)(4) "social welfare" status. The other group of Senators argues that the agency is too lax in enforcing the limits on candidate campaign activities by such groups.

The IRS has a statutory responsibility to administer and enforce the tax laws as interpreted by the courts, without regard to political pressure. These letters from the Senators, however, serve to confirm that it is essential for the IRS to initiate a rulemaking to provide clarity and a legally correct bright line standard for determining when a group is eligible to receive tax-exempt status under section 501(c)(4).

The Internal Revenue Code provides that section 501(c)(4) groups must engage "exclusively" in social welfare activities. 26 U.S.C. § 501(c)(4). The regulations implementing this provision state, however, that "social welfare" organizations must be "primarily engaged" in social welfare activities. 26 C.F.R. § 1.501(c)(4)–1(a)(2)(i).

Although the IRS has clearly and correctly stated that "social welfare" activities do not include activities that constitute participation or intervention in candidate elections, it has not clearly or properly defined the "primarily engaged" standard that was established by the agency to serve as a cap on such candidate campaign activities.

In the absence of a proper regulation, the standard has been widely misinterpreted to mean that section 501(c)(4) groups can engage in candidate election activities so long as such activities do not constitute a majority of the group's spending – that is to say, they can spend up to 49 percent of their expenditures on candidate campaign-related activities.

This is in conflict with the statutory language and with court interpretations of this language which hold that "social welfare" organizations cannot engage in any "substantial" amount of non-exempt activity. This means that section 501(c)(4) organizations cannot do more than an *insubstantial amount of candidate election activity*, whether or not it is their "primary" purpose.

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[1] E. Carney, "Rules of the Game: Bad News for Nation's Nonprofits," *Roll Call* (March 20, 2012).

However, as we documented in our Petition and in other letters we have sent to you,[2] a number of groups claiming tax exempt status under section 501(c)(4) are engaging in substantial candidate election activities this election cycle – spending tens of millions of dollars to directly influence the 2012 candidate elections, much as such groups also did to influence the 2010 elections. This candidate campaign activity is bound to increase as the 2012 general election draws closer.

For instance, as we discussed in our letter to you of December 14, 2011, one section 501(c)(4) group, American Action Network, reportedly spent $26 million on candidate campaign-related activities in 2010, which was approximately *87 percent* of the organization's total spending that year. Another supposed "social welfare" organization, Americans Elect, is seeking ballot access as a political party in all 50 states for the purpose of nominating and running its own presidential candidate. The group has already obtained this status as a political party in a number of states. A group cannot be a "political party" and a "social welfare" organization at the same time.

The extent of the candidate election activities by these and other groups appears on its face to violate even the current ineffectual regulatory standard that limits participation in candidate campaign-related activities by section 501(c)(4) "social welfare" organizations. The activities certainly violate both the statutory language of section 501(c)(4) and the court interpretations of that provision.

The IRS must act expeditiously to revise and clarify the "primarily engaged" standard and to conform its regulations to the statute as construed by the courts. Absent action by the IRS, it is a virtual certainty that candidate election activities by groups improperly claiming tax-exempt status under section 501(c)(4) will escalate.

The stakes here are very high for the country and for the integrity of our elections. Organizations are improperly claiming tax-exempt status under section 501(c)(4) in order to keep secret the donors financing their candidate campaign-related expenditures. Citizens have a basic right to know who is giving and spending money to influence their votes.

Since section 501(c)(4) groups (unlike section 527 "political organizations") are not required to publicly disclose their donors, the sources of the money such groups spend for candidate election activities are hidden from public scrutiny.

Recent press reports have taken note of the increased candidate campaign spending by section 501(c)(4) groups, and the use of such "social welfare" groups specifically for the purpose of keeping secret the donors financing their candidate election activities.

One report in *Politico* noted that corporations have generally not contributed to so-called "Super PACs," which are federally registered political committees that are required to report their donors to the FEC. The report explained:

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[2] *See* Letters of October 5, 2010, September 28, 2011, December 14, 2011 and March 9, 2012.

> Instead, corporate lobbyists and others say companies have preferred to give to politically active nonprofits that allow their donations to stay anonymous. . . .
>
> Millionaires and others might see an advantage to giving to super PACs, but one in-house corporate lobbyist told POLITICO that "nondisclosure is always preferred" when it comes to any contribution to mitigate any public perception issues and shareholder controversy.
>
> It's unclear how much money is being directed to nonprofit advocacy organizations – 501(c)(4)s – which do not have to disclose their donors to the Federal Election Commission but are in many cases associated with Super PACs.[3]

By allowing groups to claim tax exempt status under section 501(c)(4) while also engaging in substantial candidate election activity, the IRS is serving to deny citizens essential campaign finance information about the money being spent to influence federal elections.

This is information that the Supreme Court in *Citizens United* said "permits citizens and shareholders to react to the speech of corporate entities in a proper way. This transparency enables the electorate to make informed decisions and give proper weight to different speakers and messages." *Citizens United v. FEC,* 130 S. Ct. 876, 916 (2010).

The widespread abuse of the tax laws by groups improperly claiming section 501(c)(4) tax-exempt status will continue and grow until the IRS revises its regulations to conform with the statutory provision in the Internal Revenue Code and with court interpretations holding that tax-exempt groups may not engage in more than an insubstantial amount of non-exempt activity.

The IRS must move promptly to set a new clear, bright-line and administrable standard for determining eligibility for 501(c)(4) tax status, and ensure that such standard complies with the statute. Absent such action by the IRS, the agency will bear direct responsibility for the misuse and abuse of the tax laws by groups that are flooding our elections with secret money.

We strongly urge the IRS to promptly institute a rulemaking proceeding to address this matter. We would appreciate receiving a response from the IRS to our letter regarding what action the agency is prepared to take.

Sincerely,

/s/ Gerald Hebert	*/s/ Fred Wertheimer*
J. Gerald Hebert	Fred Wertheimer
Executive Director	President
Campaign Legal Center	Democracy 21

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[3] A. Palmer and A. Phillip, "Corporations not funding super PACs," *Politico* (March 8, 2012).

WASHINGTON
LEGISLATIVE OFFICE

April 9, 2013

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Senate Judiciary Committee
Subcommittee on Crime and Terrorism
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Honorable Lindsey Graham
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Re: Current Issues in Campaign Finance Law Enforcement

Dear Chairman Whitehouse and Ranking Member Graham:

The American Civil Liberties Union writes to offer comments in advance of today's hearing on current issues in campaign finance law enforcement, and we thank the subcommittee for its attention to this topic. Although the ACLU opposes campaign finance measures that violate the First Amendment, we strongly agree that constitutional campaign finance laws should be enforced vigorously and consistently to assure the integrity of our electoral, legislative and administrative systems at all levels of government.

We briefly comment on several specific issues below, highlighting a number of areas of common ground between the ACLU and proponents of campaign finance reform.

1. Continue to Crack Down on Conduit Contributions

The ACLU supports efforts by the Internal Revenue Service and other federal law enforcement agencies to investigate and prosecute conduit contributions, in which an entity or individual attempts to mask the true source of a direct political contribution by using a straw contributor. Even in a system of unlimited contributions, such transactions, which present a significantly heightened risk of outright bribery and limit the public's ability to properly gauge the loyalties of the candidates they support, are particularly pernicious. The ACLU has long recognized that the prevention of real or perceived corruption may present a compelling government interest that can support properly tailored restrictions on political activity.

There is little that is more corrupting than masking direct contributions to political candidates through the use of straw contributors.

2. Appropriately Enforce the Coordination Rules

Many advocates on both sides of the campaign finance debate properly recognize that independent expenditure-only committees ("IECs")—colloquially and inaccurately termed "Super PACs"—present a heightened risk of corruption when they coordinate their activities with a particular candidate. As the Supreme Court recognized in *Buckley v. Valeo*, however, truly uncoordinated independent expenditures are unlikely to present a risk of quid pro quo corruption, may actually harm a candidate, and represent literal political speech in support or opposition to a candidate for public office, which, if anything, is what the First Amendment was adopted to protect from government censorship.[1] As the Supreme Court explained in *Buckley*:

> Unlike contributions, such independent expenditures may well provide little assistance to the candidate's campaign and indeed may prove counterproductive. The absence of prearrangement and coordination of an expenditure with the candidate or his agent not only undermines the value of the expenditure to the candidate, but also alleviates the danger that expenditures will be given as a quid pro quo for improper commitments from the candidate. Rather than preventing circumvention of the contribution limitations, § 608(e)(1) severely restricts all independent advocacy despite its substantially diminished potential for abuse.[2]

That said, many IECs—encouraged by the current challenges facing the Federal Election Commission—engaged during this past cycle in conduct that could result in coordination.[3] For instance, on numerous occasions, IECs shared vendors with the campaigns they supported.[4] While some of this conduct may be illegal under current regulations,[5] many vendors claim to have availed themselves of the firewall safe harbor, which may be insufficient to prevent tacit or even active coordination.[6] The current regulation is phrased in very broad terms, and merely requires—for coordinated communications—that the firewall be "designed and implemented to prohibit the flow of information between employees or consultants providing services for the person paying for the communication and those employees or consultants currently or previously

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1 424 U.S. 1 (1976).

2 *Id.* at 47.

3 *See* Mike McIntire & Michael Luo, *Fine Line Between 'Super PACs' and Campaigns*, N.Y. Times, Feb. 25, 2012, at A1 ("Rules the commission adopted in 2003, still on the books, allow for regulation of [non-advertising activities of candidates and IECs], but they have been largely ignored.").

4 T.W. Farnam, *Vendors Finesse Law Barring 'Coordination' By Campaigns, Independent Groups*, Wash. Post., Oct. 13, 2012 ("The Democratic Congressional Campaign Committee shares 10 vendors with the major super PAC helping Democrats win House races, the House Majority PAC.").

5 *See* 11 C.F.R. § 109.21(d)(4) (2013).

6 *See* 11 C.F.R. § 109.21(h) (2013).

providing services to the candidate. . . ."[7] Current regulations may need to be revised to cover other activities beyond those envisioned in the coordinated communications regulation.[8]

Similarly, although this presents significant First Amendment considerations and must be addressed with care, candidate communications with, or directed at, IECs raise additional concerns and may present another area where regulations could be tightened to promote public integrity without running afoul of the Constitution. During the last election cycle, several practices that were claimed not to present unlawful coordination raised heightened concerns of constitutionally relevant quid pro quo corruption. These included direct fundraising appeals by candidates to IECs, candidates making public statements about the value of IEC communications and candidates appearing in IEC promotional material.[9] Not only do these practices facilitate actual coordination through communications between the candidate and IEC staff, they also often spur donations to the IEC, which in certain cases—under the logic of *Buckley* and, indeed, *Citizens United*[10]—could be considered in-kind direct contributions.[11]

Great care, however, must be taken not to repeat the mistakes of earlier efforts to reform the coordination rules. Past proposals have, for instance, failed to exempt true issue advocacy groups, which often communicate with a candidate for public office (particularly in the context of lobbying) in advance of identifying them in issue advocacy material.[12]

Appropriate regulations should also consider the practical difficulty in distinguishing between "functionally equivalent" issue advocacy (that is, advocacy that could be construed as supporting or opposing the election of a candidate without using express terms of support or opposition) and legitimate issue advocacy (communications urging a candidate to take a position on a particular issue, or that praise or criticize a candidate for past positions). Revised coordination rules should

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7 11 C.F.R. § 109.21(h)(1) (2013).

8 *See* 11 C.F.R. § 109.20(b) (2013) (requiring reporting as in-kind contribution *any* coordinated expenditure that is not made for a coordinated communication).

9 *See* Michael W. Macleod-Ball, *One Key to Campaign Finance Reform?*, ACLU.org, June 21, 2012, http://www.aclu.org/blog/free-speech/one-key-campaign-finance-reform.

10 *Citizens United v. Fed. Elections Comm'n*, 130 S. Ct. 876, 909-10 (2010).

11 Direct fundraising appeals by a candidate to an IEC skirt much closer to the "hallmark of corruption" cited in *Citizens United*—namely, "dollars for political favors." *Id.* at 910 (quoting *Fed. Elections Comm'n v. Nat'l Conservative Political Comm.*, 470 U.S. 480, 497 (1985) [hereinafter "*NCPAC*"]. When a candidate appears at an IEC event, promotes the IEC, increases the fundraising prowess of the IEC and is consequently and directly rewarded by independent expenditures expressly promoting the candidate, logic suggests that the danger of quid pro quo corruption—that the candidate will "take notice of and reward those responsible for PAC expenditures by giving official favors to the [PAC contributors] in exchange for the supporting messages"—is amplified. *NCPAC*, 470 U.S. at 498.

12 *See* Letter from Laura W. Murphy & Joel M. Gora to the Senate in Opposition to the McCain-Feingold Bipartisan Campaign Reform Act of 2001, § II (Mar. 20, 2001), *available at* http://www.aclu.org/free-speech/letter-senate-opposition-mccain-feingold-bipartisan-campaign-finance-reform-act-2001.

draw clear lines between issue and express advocacy to prevent the chilling of legitimate issue advocacy.

3. Provide Adequate Resources for and Mandate Timely § 501(c) Determinations

Finally, we also urge Congress to directly address the concerns of many that structural problems at the Internal Revenue Service—including lack of funding and incentives—may have allowed organizations claiming tax exemption to skirt rules designed to limit express political advocacy by such organizations.[13] Congress has the power and ability to provide appropriate resources and direction to the Tax Exempt and Government Entities Division of the IRS, and to mandate that determinations be made in a timely fashion. Congress may also appropriately tailor the timing requirements for tax filings by organizations claiming exemption to provide for appropriate determinations in advance of federal elections. This would address the concern with both backlog and the related problem that organizations are able to operate as tax exempt groups for a significant amount of time before their applications are considered.

Importantly, we do not offer a view on the propriety of the "primary purpose" test, and we urge Congress and the IRS to continue to exempt true issue advocacy from the sweep of "political activit[y]" as that term is interpreted under 26 C.F.R. § 1.501(c)(4)-1 (2013).

4. Conclusion

There is much that can be done within the bounds of the Constitution to address the understandable concerns of many about the influence of large aggregations of wealth on the political system. We present a few of these options above, and we urge Congress and federal law enforcement to focus on these achievable and effective measures before, as some advocate, restricting political speech. Targeting straw donations, perfecting the anti-coordination rules and addressing the serious tax-exempt backlog at the IRS would all leave the Constitution unharmed while doing much to improve the integrity of our elections and our government.

Please do not hesitate to contact Gabe Rottman, legislative counsel/policy advisor, at 202-675-2325 or grottman@dcaclu.org with any questions.

Sincerely,

Laura W. Murphy

Laura W. Murphy
Director, Washington Legislative Office

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[13] *See* Dan Berman & Kenneth T. Vogel, *Crossroads GPS Said Elections Wouldn't Be 'Primary Purpose'*, Politico, Dec. 14, 2012; Kenneth P. Vogel & Tarini Parti, *The IRS's 'Feeble' Grip on Big Political Cash*, Politico, Oct. 15, 2012; T.W. Farnam & Dan Eggen, *Lax Internal Revenue Service Rules Help Groups Shield Campaign Donor Identities*, Wash. Post., Mar. 9, 2011; Michael Luo & Stephanie Strom, *Donor Names Remain Secret as Rules Shift*, N.Y. Times, Sept. 20, 2010, at A1.

Gabriel Rottman
Legislative Counsel/Policy Advisor

cc: Members of the Senate Judiciary Subcommittee on Crime and Terrorism

Testimony Submitted by
Democracy 21 President Fred Wertheimer

Hearing on Current Issues in
Campaign Finance Law Enforcement"

Subcommittee on Crime and Terrorism

Senate Judiciary Committee

April 9, 2013

Democracy 21 appreciates the opportunity to submit this testimony for the record and appreciates the important leadership of Senator Sheldon Whitehouse in examining the serious problems that exist today concerning the enforcement of campaign finance laws.

My name is Fred Wertheimer and I am president of Democracy 21, a nonprofit, nonpartisan organization that supports effective campaign finance laws to protect our political system from corruption, to empower ordinary Americans citizens in the political process and to inform citizens about who is giving and spending political money to influence their votes.

Democracy 21 strongly supports the efforts by the committee to examine the issues surrounding the enforcement of federal laws that deal with campaign finance activities, including the federal campaign finance laws and the tax laws that relate to campaign activities.

Federal Election Commission

The campaign finance enforcement problems start with the Federal Election Commission.

In order to be effective, laws have to be enforced and people have to believe that they will be enforced. In the case of the FEC, however, we have a completely dysfunctional enforcement agency. Three current commissioners on the six-member Commission are ideologically opposed to the campaign finance laws and have consistently refused to properly interpret and enforce the laws.

This has created a "wild west" approach to the laws where participants in the electoral process know they can pretty much do whatever they want without facing consequences for violating the laws.

I would like to submit for the record an Issue Brief recently published by Democracy 21 in conjunction with the American Constitution Society entitled "The FEC: The Failure to Enforce Commission."

The Issue Brief details how the Federal Election Commission has undermined the campaign finance laws with flawed regulations and blocked the enforcement of the laws based on ideological objections. It also spells out the structural problems that have existed from the establishment of the FEC in 1974 and that have helped to create today a "completely dysfunctional" agency.

The Issue Brief concludes, "We have reached the point where we have the illusion of campaign laws because in reality, there is little or no enforcement of these laws."

The Issue Brief sets forth a proposal to create a new campaign finance enforcement agency with strong enforcement powers, adequate resources and a new structural approach for the agency.

The Brief also notes the failure of President Obama to nominate new commissioners to the FEC to replace the four Commissioners now sitting as lame ducks whose terms expired and who are ineligible to be reappointed (A fifth lame duck Commissioner recently left the agency creating a fifth position that needs to be filled.) It is essential for new commissioners be appointed to the FEC who are committed to properly interpreting and enforcing the campaign finance laws.

Department of Justice

The failure of the FEC to carry out its exclusive civil enforcement powers and the flawed regulations adopted by the FEC in a number of areas have made it more difficult for the Justice Department to carry out its criminal enforcement responsibilities.

Nevertheless, given the abdication of enforcement by the FEC, it is important for the Justice Department to investigate serious potential violations of the campaign finance laws and bring criminal enforcement proceedings where appropriate.

In this regard, on January 4, 2011 we sent a report to the Justice Department entitled "A Democracy 21 Report: Leading Presidential-Candidate Super PACs and The Serious Questions That Exist about Their Legality." I ask that a copy of our report be placed in the record.

This was followed with a series of letters raising serious questions about potential illegal coordination between a number of candidate-specific Super PACs and the candidates they were exclusively supporting in the 2012 presidential election. The letters can be found on the Democracy 21 website at www.democracy21.org and are dated January 10, 2012, January 13, 2012, February 15, 2012, February 21, 2012, March 5, 2012, March 6, 2012 and January 3, 2013.

In our letters, we asked the Justice Department to conduct investigations and, where appropriate, to bring criminal enforcement proceedings. In our view, illegal coordination took place in the 2012 presidential election, even under the weak FEC coordination regulations that exist. Given

the non-existing enforcement by the FEC, the only place to potentially obtain enforcement of the campaign finance laws has been the Justice Department.

We are not aware of any actions taken by the Justice Department regarding our letters.

Internal Revenue Service

An additional serious enforcement problem has occurred at the IRS.

In the wake of the disastrous 2010 Supreme Court decision in the *Citizens United*, a number of groups have improperly claimed tax-exempt status as section 501(c)(4) "social welfare" organizations in order to hide from the American people the donors financing their campaign activities.

Beginning in 2010, Democracy 21, joined by the Campaign Legal Center, sent a series of letters to the IRS asking the agency to investigate and take appropriate action against a number of groups that appeared to be ineligible for 501(c(4) tax-status and using this status to evade campaign finance disclosure requirements. The letters can be found on the Democracy 21 website and are dated October 5, 2010, September 28, 2011, December 14, 2011, March 9, 2012, April 17, 2012, July 23, 2012, August 9, 2012, August 21, 2012, September 27, 2012, December 3, 2012, January 2, 2013 and January 16, 2013.

Democracy 21, joined by the Campaign Legal Center, also submitted a petition to the IRS on July 27, 2011 challenging as contrary to law the existing regulations governing eligibility for 501(c)(4) tax-status and asking for a proceeding to adopt new rules. After not receiving a substantive response from the IRS, we sent a second letter regarding our petition to the IRS on March 22, 2013 further making the case for a rulemaking proceeding.

On July 17, 2012 we received a response from the IRS regarding our petition for a rulemaking that stated:

> The IRS is aware of the current public interest in this issue. These regulations have been in place since 1959. We will consider proposed changes in this area as we work with the IRS Office of Chief Counsel and the Treasury Department's Office of Tax Policy to identify tax issues that should be addressed through regulations and other published guidance.

The IRS to our knowledge, however, has not taken any action to open a rulemaking proceeding.

Meanwhile, blatant misuse of the tax laws by groups improperly claiming tax-exempt status continues to occur and citizens continue to be denied campaign finance information they have a right to know.

Conclusion

The integrity and effectiveness of our campaign finance laws and related tax laws is being seriously undermined by the absence of proper enforcement of these laws.

The abject failure of the FEC to properly enforce the campaign finance laws is a national scandal and is providing license for wholesale violation of the laws. The failure of the IRS to stop groups from misusing the tax laws in order to hide campaign finance information which citizens are entitled to know is its own scandal.

In order to protect the integrity of our democracy and political system against corruption, it is imperative for Congress to address the lack of enforcement of the campaign finance laws that currently exists. It is essential to make clear that campaign finance laws cannot be ignored with impunity.

Thank you again for the opportunity to submit our testimony.

ADDITIONAL SUBMISSIONS FOR THE RECORD

Submissions for the record not printed due to voluminous nature, previously printed by an agency of the Federal Government, or other criteria determined by the Committee, list

Petition for rulemaking on campaign activities by section 501(c)(4)

http://www.democracy21.org/uploads/D21__and__CLC__Petition__to__IRS__7__27__2011.pdf

Democracy 21 report: leading presidential-candidate super PACs *http://www.democracy21.org/uploads/Democracy__21__Super__PAC__Report__1__4__2012.pdf*

"The FEC: The Failure to Enforce Commission" by Fred Wertheimer and Don Simon *http://www.acslaw.org/sites/default/files/Wertheimer__and__Simon—The Failure to Enforce Commission.pdf*

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