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IRS Responds to Rulemaking Petition Submitted by Democracy 21 and Campaign Legal Center, Says Agency Will Consider Changing Rules for 501(c)(4) Eligibility

In a letter sent today to the IRS, Democracy 21 and the Campaign Legal Center acknowledged and welcomed a July 17, 2012 letter from Lois Lerner, IRS Director of the Exempt Organizations Division, stating that that the IRS "will consider proposed changes" in the regulations governing eligibility for section 501(c)(4) tax-exempt status.

On July 27, 2011, Democracy 21, joined by the Campaign Legal Center, submitted to the IRS a "Petition for Rulemaking on Campaign Activities by Section 501(c)(4) Organizations." The groups wrote the IRS again on March 22, 2012 urging the agency to undertake the rulemaking.

According to today's letter to the IRS:

> We welcome Ms. Lerner's statement in your July 17 letter that the IRS "will consider proposed changes" in the regulations governing eligibility for tax-exempt status under section 501(c)(4) organization. But we want to stress once again that the need for urgent action we noted in our July 27, 2011 letter is all the more true today.
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> We strongly urge the IRS to promptly institute a rulemaking proceeding to address this matter. We also strongly urge the IRS to act expeditiously in the interim to stop the blatant abuses of the tax laws that are resulting in massive amounts of secret money being laundered into our national elections by groups claiming to be "social welfare" organizations.

According to Democracy 21 President Fred Wertheimer:

> The letter we have received from the IRS provides an important new development in the effort to end the massive amounts of secret money being spent in federal elections by groups claiming 501(c)(4) tax-exempt status. We believe this is the first time the IRS has publicly indicated it will consider new regulations to govern the eligibility of groups for 501(c)(4) tax-exempt status.

> Ms. Lerner states that the IRS regulations have been in place since 1959, more than a half century ago. Circumstances have changed dramatically since then. Effective new IRS regulations would eliminate the current efforts by phony "social welfare" groups to inject secret contributions into federal elections by claiming to be 501(c)(4) groups.
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> The IRS letter provides a potential second breakthrough in the multi-prong effort to end the massive amounts of secret money that have returned to federal elections for the first time since the Watergate scandals. The first breakthrough occurred in federal district court on March 30, 2012 when Representative Chris Van Hollen (D-MD), represented by the Democracy 21 Legal Team, won a lawsuit striking down an FEC regulation that gutted existing disclosure requirements for contributions spent to make electioneering communications. Another important part of the multi-prong effort involves the fight that will continue in Congress next year to enact comprehensive new disclosure laws for outside spending groups.

In her July 17 letter to the reform groups, Ms. Lerner 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.

According to today's letter from the reform groups to the IRS:

> We believe the letter from Ms. Lerner recognizes the controversy that currently exists over the role that groups claiming status as "social welfare" organizations are playing in our elections, post-*Citizens United.*

The letter to the IRS from the reform groups stated:

> [D]evelopments in the course of the 2012 national elections have served to underscore that IRS regulations that are contrary to law are facilitating widespread misuse and abuse of the tax laws by organizations claiming tax-exempt status under section 501(c)(4) as "social welfare" organizations, in order to keep secret the donors financing their campaign-related expenditures.
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> Campaign-related spending by section 501(c)(4) groups whose overriding purpose clearly appears to be influencing elections, has grown exponentially since we first called on the IRS to conduct a rulemaking proceeding a year ago.

According to today's letter, the Petition submitted to the IRS by Democracy 21, joined by the Campaign Legal Center, stated:

> The large scale spending ofsecret contributions in federal elections by section 501(c)(4) organizations is doing serious damage to the integrity and health of our

> democracy and political system. The IRS needs to act promptly to address this problem by issuing new regulations to stop section 501(c)(4) organizations from being improperly used to inject tens of millions of dollars in secret contributions into federal elections. The new regulations must conform with the IRC and withcourt rulings interpreting the IRC. The regulations should provide a bright-line standard that implements the insubstantial expenditures standard set forth by the courts and specifies a limit on the amount of campaign activity that a section 501(c)(4) organization may undertake consistent with its tax-exempt status. The IRS needs to act expeditiously to ensure that the new regulations are in effect in time for the 2012 presidential and congressional elections. Petition at 18-19 (emphasis added).

Today's letter to the IRS also noted that the reform groups have sent several letters to the IRS challenging the claims by a number of groups that they were entitled to tax-exempt status as 501(c)(4) "social welfare" groups and asking the IRS to investigate the groups. The groups included Crossroads GPS, Priorities USA, American Action Network and Americans Elect.

The letter sets forth recent published reports that show why the reform groups believe the overriding purpose of Crossroads GPS is to influence elections.

The letter stated:

> Political operatives are using "social welfare" organizations as conduits for injecting secret money into federal elections by attempting to exploit what they claim to be purported ambiguities in existing IRS standards.
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> These operatives argue, for example, that as long as ads do not contain "express advocacy" they can attack or promote candidates in whatever way they want and such ads do not constitute "intervention or participation" in campaigns, and thus may be run without limit by a section 501(c)(4) organization.
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> The IRS, however, has made clear that ads do not need to contain "express advocacy" in order to be treated as "intervention or participation" in campaigns for purposes of section 501(c)(4). *See, e.g.,* Rev. Rul. 2004-6 (listing six factors that "tend to show" that an ad is for the purpose of influencing a candidate election.)
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> The political operatives also argue that a "social welfare" organization can spend up to 49 percent of its revenues on overt campaign intervention, without running afoul of the rules that currently require a section 501(c)(4) organization to be "primarily engaged" in social welfare activities. *See* 26 C.R.F. 1.501(c)(4)-1(a)(2)(i).
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> Such claims have gone unchallenged by the IRS, despite the fact that the IRS has never set forth a "49 percent" rule. The IRS has failed to clarify its rules regarding the amount of candidate election-related activity a section 501(c)(4) "social welfare" group is permitted to conduct. As a result, groups claiming status as section 501(c)(4)

organizations have been allowed to become major players in influencing the 2012 federal elections and to use secret contributions to do so.

The failure of the IRS to take action on this matter has allowed groups that are in reality campaign operations – but claim to be 501(c)(4) "social welfare" groups – to make assertions about IRS rules that are unsupported by law, and thereby to provide a veil of secrecy for the donors financing their campaign-related expenditures.