INTRODUCTION

At roughly four million words, the Internal Revenue Code is no stranger to bright-line rules.\(^1\) Taxpayers know the point at which their income moves into a higher tax bracket,\(^2\) the moment they can begin withdrawing money from retirement accounts without facing a penalty,\(^3\) and whether they can claim exemptions and credits for a child born in a given tax year, even if she arrived at 11:59 p.m. on December 31.\(^4\) IRS officials maintain that such rules make the Code easier to administer and are meant to signal to the public that the system is fair—look up your taxable income and filing status, and you have your tax.\(^5\)

Not all of the law that the agency is tasked with administering lends itself to this approach, however. When it comes to Section 501 of the Internal Revenue Code, the role of the IRS is not to define and calculate income, deductions, and credits, but rather to capture the animating spirit of that section of the Code, cordoning off from taxation those entities that Con-
gress has deemed worthy of tax exemption. Here, there are few bright-line rules. Instead, the agency looks at all “facts and circumstances” to determine whether an organization’s activities qualify it for a tax exemption.

This approach has been controversial in recent years, particularly when it comes to policing the line of permissible campaign activity. For “social welfare” groups organized under Section 501(c)(4), campaign-related activities are permitted only if they are not the group’s primary function. In the wake of reports in May 2013 that IRS employees had used politically charged terms to flag certain requests for recognition of tax-exempt status under Section 501(c)(4)—the “Tea Party scandal”—calls

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7 See generally I.R.C. § 501.


9 Section 501(c)(4) grants tax-exempt status to “[c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes,” so long as “no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.” I.R.C. § 501(c)(4). While this Article deals with 501(c)(4) “social welfare” organizations, many of its insights and arguments can apply equally to other “non-charity” 501(c) groups that are also permitted limited political participation, including unions (organized under 501(c)(5)) and trade associations and business organizations like the Chamber of Commerce (organized under 501(c)(6)).

10 Treas. Reg. § 1.501(c)(4)-1 (2013). In some contexts the difference between an entity’s “purpose” and its “activities” may be germane, but they are not for the purpose of the following discussion. In contrast, charitable organizations organized under Section 501(c)(3) are prohibited from engaging in any such activity. I.R.C. § 501(c)(3).

11 I use the term “Tea Party scandal” advisedly. While that is how the events leading to and arising from the TIGTA Report have become known in the common vernacular, the expression is a misnomer. See, e.g., Andy Kroll, The IRS Tea Party Scandal, Explained, MOTHER JONES (Nov. 21, 2013, 1:19 PM), http://www.motherjones.com/politics/2013/05/irs-tea-party-scandal-congress-nonprofit-obama. Investigations revealed that groups across the political spectrum received similar treatment. See infra notes 73-77 and accompanying text; STAFF OF H. COMM. ON OVERSIGHT & GOV’T REFORM, 113TH CONG., NO EVIDENCE OF WHITE HOUSE INVOLVEMENT OR POLITICAL MOTIVATION IN IRS SCREENING OF TAX-EXEMPT APPLICANTS (Comm. Print 2014), available at http://democrats.oversight.house.gov/uploads/Cummings%20Report%20on%2039%20IRS%20Transcripts%20050614.pdf. But see STAFF OF H. COMM. ON OVERSIGHT & GOV’T REFORM, 113TH CONG., DEBUNKING THE MYTH THAT THE IRS TARGETED PROGRESSIVES: HOW THE IRS AND CONGRESSIONAL DEMOCRATS MISLED AMERICA ABOUT DISPARATE TREATMENT (Comm. Print 2014), available at http://oversight.house.gov/wp-content/uploads/2014/04/4-7-2014-IRS-Staff-Report-w-appendix.pdf (arguing that conservative groups were flagged for further review based on their political beliefs while non-conservative groups were flagged for non-political reasons). Tax academics may know the same controversy as the “IRS Scandal” after a long-standing entry on Professor Paul Caron’s popular TaxProf Blog, see, e.g., Paul Caron, The IRS Scandal, Day 399, TAXPROF BLOG (June 12, 2014), http://taxprof.typepad.com/taxprof_blog/2014/06/the-irs-scandal-9.html, but others have suggested that this term is not sufficiently specific.
were renewed for the agency to update its 1959 regulations for assessing when an organization’s political campaign activity jeopardizes its status as a social welfare organization. Commentators disagree on what the provisions should say—for example, the definition of political activity and the amount of campaign-related activities that should be permitted a social welfare group—but there is a rare note of agreement as to how the question should be approached: with clear, up-front rules.

The IRS put its toe into the regulatory water with a November 2013 Notice of Proposed Rulemaking (“NPRM”), which embraced a more rules-oriented approach. The NPRM attempted to define political activity, but declined to suggest an acceptable level of such activity. By the time the comment period closed six months later, the proposed rules had garnered more than 150,000 comments—the most the IRS had ever received in response to a proposed rule, with the number of comments exceeding the number of 501(c)(4) groups in existence by 50 percent. It is clear that the NPRM was the opening salvo in a longer battle. The proposed rules were criticized by advocates on both sides of the political aisle, and Republi-

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14 See id. at 71,538 (inviting “comments from the public on what proportion of an organization’s activities must promote social welfare for an organization to qualify under section 501(c)(4) and whether additional limits should be imposed on any or all activities that do not further social welfare”).


16 The proposed regulations were attacked by advocates on both the left and the right for being simultaneously overinclusive and underinclusive. See, e.g., Our First Reaction to Proposed Regulations from IRS/Treasury on Tax-Exempt Political Campaign Activity, PUB. CITIZEN (Dec. 6, 2013), http://www.citizen.org/documents/blp-reaction-irs-political-campaign-spending.pdf (noting that the proposed IRS rules “have labeled whole categories of civic engagement as political ‘candidate-related
cans in Congress responded by introducing legislation that would prohibit the IRS from issuing regulations in this area for at least a year. The IRS subsequently announced that there would be a public hearing on the question and that the proposed rulemaking would be revised and resubmitted for comment.

For now, any serious analysis of the IRS’s current proposal—the what—is premature and likely to be overtaken by events. The question of how the IRS should approach the issue, however, is extremely ripe. This Article focuses on the latter question.

Historically, the IRS’s assessment of an organization’s primary activity has been nuanced—or as nuanced as a large bureaucracy can get. Rather than relying on a series of formulaic rules (e.g., a precise percentage of revenue spent on political activity, or whether advertisements use “express” words of advocacy), the agency’s functional review requires it to balance a series of factors based on the specific facts at hand. In this regard, the IRS’s approach to gauging political activity stands in sharp contrast to the approach embraced in the parallel legal regime of campaign finance law.

Whether originating in congressional statute, agency pronouncement, or judicial decision, the campaign finance rules administered by the Federal Election Commission (“FEC”) favor the bright-line, up-front type of legal command endorsed by many political reformers.

This dialectic reflects a long-running tug-of-war among policy experts and academic theorists. The perennial question is how to structure a system of laws in a way that best balances competing considerations of cost, efficiency, and, most fundamentally, effectiveness—defined, in this case, as
how closely the behaviors induced by legal commands map onto the desired social and legal norms. To what extent should a law’s contents and contours be detailed up front in a rule, and to what extent should it describe a standard that leaves to the adjudicator the task of determining its specific application? In shorthand, scholars refer to this debate as one of “rules versus standards,” although most acknowledge that the “choice between rules and standards is one of degree.” It is, however, a helpful dichotomy to consider in evaluating how the IRS and taxpayers can best determine whether a 501(c)(4) social welfare organization is, as the law requires, “primarily engaged in promoting in some way the common good and general welfare of the people of the community” and “operated primarily for the purpose of bringing about civic betterments and social improvements.”

Viewed through this lens, the IRS has been regulating the permissible level of political activity of social welfare groups through application of an ex post standard—the facts and circumstances test. Reformers want to see this replaced by an ex ante rule that will clearly demarcate the lines of permissible activity.

Critics level many charges against the IRS’s standards-based approach for identifying overly political groups. They argue that the agency’s multifactor methodology is too complex and that the standards fail to provide sufficient guidance to leaders of social welfare organizations. They worry that people seeking to manipulate the system will find ways to spend in federal campaigns while still avoiding disclosure. They fret that the results taint the entire system—the special status of tax-exempt groups, the public’s faith in government, the authority of the IRS. They suggest that clear,

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24 See, e.g., TIGTA REPORT, supra note 12, at 14; Ezra Klein, The IRS Was Wrong to Target the Tea Party. They Should’ve Gone After All 501(c)4s., WASH. POST (May 10, 2013), http://www.washingtonpost.com/blogs/wonkblog/wp/2013/05/10/the-irs-was-wrong-to-target-the-tea-party-they-shouldve-gone-after-all-501c4s/.


bright-line rules will change behavior to better conform to social norms and will constrain agency discretion.\textsuperscript{27}

As this Article shows below, many of these premises are true: this is a complex area of law, and under the current system the agency’s final determination is, at the margins, unpredictable. When it comes to both tax and campaign finance, there will always be individuals seeking to circumvent the law. And certainly the public should be concerned for the robustness of the entire system. But all of these considerations counsel for retaining, with some modifications, the IRS’s standards-based approach to policing the campaign intervention line. They certainly do not support the contention that bright-line rules will markedly improve compliance or reduce the level of political participation by newly formed social welfare groups. Moreover, notwithstanding the political appeal of anti-IRS rhetoric, constraining the agency’s discretion in these cases will help no one but private actors looking for loopholes.

This Article reaches this conclusion through two independent lines of analysis. The first is largely theoretical. It examines the characteristics of rules—where the content of a legal command is provided ex ante—and standards—where the exact contours are determined as applied to a concrete set of facts ex post—as set out in legal scholarship over the last several decades. Following the lead of Professor Ellen Aprill, who recently conducted a similar inquiry with regard to 501(c)(3) charitable organizations but reached a different conclusion,\textsuperscript{28} this Article relies on the comprehensive framework set out by Professor Louis Kaplow in his article “Rules Versus Standards: An Economic Analysis.”\textsuperscript{29}

The second line of analysis is based on the observed effects of bright-line rules in the parallel regime of campaign finance law. Campaign finance is an obvious choice for comparison for several reasons. First, many of the concerns and considerations set forth above, including complexity and circumvention, apply with equal force in the campaign finance arena. Second, it is a natural foil: the Federal Election Campaign Act (“FECA”) is increasingly administered through bright-line rules.\textsuperscript{30} Finally, many of those calling for reform of Section 501(c)(4) are motivated by concerns about the evasion of existing campaign finance laws,\textsuperscript{31} so there is a practical appeal to testing the hypothesis that rules in this area would be more effective.

\textsuperscript{27} See, e.g., What is the Definition of Political Activity?, supra note 23.

\textsuperscript{28} See Aprill, supra note 23, at 645.

\textsuperscript{29} See Kaplow, supra note 21, at 600.


Part I of this Article describes how Section 501(c)(4) intersects with campaign finance laws and reviews its historical and legal underpinnings. It also briefly describes how this section of the Internal Revenue Code landed in the crosshairs of both the public and politicians in the spring and summer of 2013.

Part II situates the discussion of how to best administer the “primary activity” inquiry in the long-standing rules-versus-standards conversation and argues that this analysis indicates standards are preferable in this context. This section draws on scholarship in the areas of taxation, law and economics, and behavioral economics. While other scholars have suggested that this literature counsels for a “bright line” test for an organization’s level of political intervention, this Article reaches the opposite conclusion.

Part III contrasts the IRS’s use of the facts-and-circumstances test with the rules-based approach embraced in the campaign finance regime. It reviews the failure of bright-line rules to enforce Congress’s stated goal of reducing or eliminating the flow of large, undisclosed funds into federal elections and highlights how a failure of rules led to the recent crisis.

Taken together, this analysis shows that replacing the “primary activity” inquiry with a rule rather than standard would most benefit those who seek to circumvent the law rather than protect the social values the standard is meant to safeguard. It also demonstrates that there is a natural limit to the efficacy of rules in situations where, like here, there is a culture of circumvention and relatively low enforcement; rules can offer, at most, a safe harbor for cautious actors. Lastly, it suggests that it is important to clearly identify whether a legal command is to be adjudicated under a rule or a standard.

These conclusions will inform Part IV, which makes recommendations for revising the process of reviewing 501(c)(4) recognition requests and briefly considers existing proposals for doing so.

An opening caveat: this Article proceeds with the assumption that there is neither significant appetite nor political will for dramatically altering either the Internal Revenue Code or the Code of Federal Regulations to address political activity by social welfare groups and similarly situated groups such as unions or business associations—an assumption supported by both the IRS’s recent proposed rulemaking and reaction thereto. It should be noted, however, that there are other provocative options for re-


33 See NPRM, supra note 13, at 71,541; see also notes 16-17, supra.
turning 501(c)(4) to its “social welfare” roots that go considerably further than altering the nature of the legal command. These include reinforcing the legislative language that restricts 501(c)(4) organizations to acting “exclusively” in the social welfare, 34 enforcing the gift tax against donations to social welfare organizations, 35 and mandating public disclosure of all donors to social welfare organizations. 36 Another approach would redefine “social welfare,” eliminate the campaign intervention limitation for these groups altogether, and allow them to organize primarily around election activities. 37 These options are worthy of consideration, but are not discussed in this Article.

I. SECTION 501(C)(4): AN OVERVIEW

Section 501(c)(4) groups have long been understood to be appropriate vehicles for limited campaign activity thanks to a bit of interpretive sleight of hand. The legislation granting social welfare organizations tax-exempt status requires that they function “exclusively for the promotion of social welfare,” and IRS regulations specify that “promotion of social welfare does not include direct or indirect participation or intervention in political campaigns.” 38 However, the same regulations tweak the definition of “exclusively” to provide that an “organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some

35 Although no statute or regulation prevents contributions to 501(c)(4) organizations from being subjected to the gift tax (as opposed to 527 contributions, which are explicitly excepted from the tax), the IRS appears to have abandoned pursuit of the matter. See Douglas Oosterhouse, Note, Campaign Finance Reform and Disclosure: Stepping-Up IRS Enforcement as a Remedial Measure to Partisan Deadlock in Congress and the FEC, 65 RUTGERS L. REV. 261, 288-89 (2012); see also Ellen P. Aprill, Once and Future Gift Taxation of Transfers to Section 501(c)(4) Organizations: Current Law, Constitutional Issues, and Policy Considerations, 15 N.Y.U. J. LEGIS. & PUB. POL’Y 289, 291 (2012) (noting that the IRS could impose a gift tax on 501(c)(4) donations but questioning whether it should do so).
way the common good and general welfare of the people of the community.” Thus, the argument runs, a social welfare organization can engage in political campaign activity so long as it is “primarily” focused on its tax-exempt mission.

As a result, “exclusively” in the social welfare context has come to mean something quite apart from the common vernacular. Indeed, until the IRS suspended examination of exempt organizations’ political activity in the wake of the May 2013 U.S. Treasury Inspector General for Tax Administration (“TIGTA”) report, internal documents suggest that the IRS permitted social welfare groups to spend up to 49 percent of their resources on political activity. This allowance stands in a marked contrast to 501(c)(3) charities, which are completely prohibited from engaging in campaign activity. It also explains why advocates on both the right and left are united

42 I.R.C. § 501(c)(3) (exempting “[c]orporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.” (emphasis added)). See also Roger Colinvaux, The Political Speech of Charities in the Face of Citizens United: A Defense of Prohibition, 62 CASE W. RES. L. REV. 685, 686 (2012).
in advocating for rules: campaign finance reform proponents want to clarify (and restrict) the definition of “exclusively,” and its opponents want a favorable (and broad) definition of “primarily.”

An instinct to turn to the historical underpinnings of Section 501(c)(4) to resolve this tension is understandable. However, its origins are sufficiently nebulous that the lens of present-day events provides a helpful—and perhaps necessary—frame to consider the problems Section 501(c)(4) raises. Thus, this Part begins with an overview of how Section 501(c)(4) currently operates and the backlash that has resulted in recent years. It then briefly reviews the legislative and regulatory history of social welfare groups and describes how the courts have largely skirted constitutional questions in upholding the IRS’s determinations regarding whether to grant an exemption and, by implication, the facts-and-circumstances method used to reach its result.

A. The “Primary Activity” Test and the “Tea Party Scandal”

The existing statutory and regulatory scheme creates gaps that frustrate the purposes of both federal election law and the Internal Revenue Code. Because a social welfare organization cannot, by definition, be organized primarily to participate in political campaigns, it is not subject to FEC jurisdiction—and, thus, disclosure requirements—as a federal political committee. At the same time, by organizing under 501(c)(4), the organization can also evade the disclosure requirements the IRS places on 527 organizations—the intended tax “home” for political parties, political action committees (“PACs”), and the like. It can also enjoy the arguably more favor-

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43 See, e.g., Complaint, supra note 12, at 2 (arguing that the IRS’s broad definition of “primarily” is in contravention of the text of the Internal Revenue Code).
45 See I.R.C. § 501(c)(3); Treas. Reg. § 1.501(c)(4)−1(a)(2) (as amended in 1990); 2 U.S.C. § 431(4)(A) (2012). Although FECA broadly defines a “political committee” to include, inter alia, “any committee, club, association, or other group of persons which receives contributions aggregating in excess of $1,000 during a calendar year or which makes expenditures aggregating in excess of $1,000 during a calendar year,” the FEC has added a restrictive gloss to the statute, ruling that only organizations that are “organized primarily for the purpose of influencing” elections must register as political committees. 2 U.S.C. §§ 431(4)(A), (9)(B)(iii); see FEC v. Akins, 524 U.S. 11, 14-15 (1998); Akins v. FEC, 736 F. Supp. 2d 9, 13-16 (D.D.C. 2010) (reviewing nearly twenty years of litigation on this question).
46 See Richard Briffault, The 527 Problem . . . and the Buckley Problem, 73 GEO. WASH. L. REV. 949, 959-60 (2005). While social welfare groups can be taxed on their political activity, they can avoid this tax by setting up a separate fund. See I.R.C. § 527(f)(3). Expenditures made by the separate segregated fund must be disclosed, but the original donors of the funds are shielded as the money comes from
able tax treatment offered by Section 501 (fewer income categories are exempt for groups organized under Section 527 than those organized under Section 501).⁴⁷

These discrepancies carried less import when corporations—the most common 501(c)(4) organizational form—were largely prohibited from participating directly in political campaigns.⁴⁸ They became far more important after the Supreme Court determined in Citizens United v. FEC⁴⁹ that unrestricted corporate expenditures on political activities cannot be banned so long as they are not “coordinated” with a candidate or her campaign and, shortly thereafter, the D.C. Circuit Court of Appeals struck down contribution limits to groups that make only independent expenditures.⁵₀

Unlike 501(c)(3) charities, 501(c)(4) social welfare groups are not required to apply for and receive recognition of their tax-exempt status.⁵¹ Nevertheless, many choose to do so, and following the Citizens United decision in 2010, applications for 501(c)(4) status skyrocketed—from 1,735 in 2010, to 2,265 in 2011, to 3,357 in 2012.⁵² Election watchdog groups charge that social welfare organizations have become the refuge of funders seeking to flood federal and state campaigns with “dark money,” or money from undisclosed (and frequently untraceable) sources.⁵³ Because social welfare organizations are subject to few disclosure requirements, they are ideal recipients of money from donors who wish to remain anonymous.⁵⁴

the social welfare group, not individuals. See id. § 527(j); TIGTA REPORT, supra note 12, at 2; see also infra note 55.

⁴⁷ Compare I.R.C. § 527(b) with I.R.C. § 501(a), (b).

⁴⁸ In 1986 the Supreme Court carved out a limited exception to the ban on corporate independent expenditures (express advocacy) for a corporation that meets three criteria: first, that it is “formed for the express purpose of promoting political ideas, and cannot engage in business activities”; second, that it “has no shareholders or other persons affiliated so as to have a claim on its assets or earnings”; and third, that it “was not established by a business corporation or a labor union, and it is its policy not to accept contributions from such entities.” FEC v. Massachusetts Citizens for Life, Inc., 479 U.S. 238, 264 (1986).


⁵₀ Id. at 360; SpeechNow.org v. FEC, 599 F.3d 686, 698 (D.C. Cir. 2010).

⁵¹ See TIGTA REPORT, supra note 12, at 1.

⁵² Id. at 3. Because 501(c)(4) groups are not required to apply for recognition of status in order to begin operations, id. at 1, it is likely that these figures undercount the true increase in social welfare organizations.

⁵³ See Russ Choma, OpenSecrets.org’s Resources on Politically Active Tax-Exempt Groups, OPENSECRETS.ORG (May 15, 2013), http://www.opensecrets.org/news/2013/05/501c-factsheet.html (referring to 501(c)(4) organizations as dark money groups whose spending increased explosively during the last three election cycles); see also Thomas B. Edsall, Dark Money Politics, N.Y. TIMES OPINIONATOR BLOG (June 12, 2013, 9:39 PM), http://opinionator.blogs.nytimes.com/2013/06/12/dark-money-politics/?_r=0 (attributing the exponential growth of federal election campaign cash flow through 501(c)(4) organizations to the fact that 501(c)(4)s do not have to reveal their donors).

⁵⁴ Peter Overby, Group Behind Election Ads Weighs In on Tax Deal, NAT’L PUB. RADIO (Dec. 14, 2010, 3:00 PM), http://www.npr.org/2010/12/14/132060878/Conservative-Group-Wades-Into-Tax-
The money donated can be either used by the 501(c)(4) group for campaign activity that is “secondary” to the organization’s primary purpose,\(^{55}\) donated to another 501(c)(4) group to fund that group’s “secondary” political activities,\(^{56}\) or sent to politically active 527 groups subject to stricter disclosure requirements, conveniently “scrubbed” of information about its original source.\(^{57}\)

Debate (quoting Carl Forti, political director for the Crossroads groups, as stating that Crossroads GPS was created because some donors “didn’t want to be disclosed” (internal quotation marks omitted)).

\(^{55}\) If a social welfare group spends money on political activities as defined by the IRS, see I.R.C. § 527(e)(2) (2012), it must pay a tax on the lesser of its investment income or its expenditure. I.R.C. § 527(f). As many organizations have no or little investment income, this is not a great burden. See, e.g., ADAM RAPPAPORT, CITIZENS FOR RESPONSIBILITY & ETHICS IN WASHINGTON, THE DARK MONEY DEBATE: RESPONSES TO ARGUMENTS AGAINST REFORMING IRS TREATMENT OF 501(C) GROUPS 14-15 (2014), available at http://www.citizensforethics.org/page/-/PDFs/General%20CREW/Reforming_IRS_501c_Treatment_CREW_1_2014.pdf?nocdn=1 (“As a factual matter . . . tax-exempt organizations engaged in politics do not pay much, if any, tax under section 527. The section 501(c)(4) organizations that spent the most money on political activity in 2010 and 2012 reported far less investment income than political activity, meaning they paid tax on the lower amount and thus were subsidized for most of their political activity. For example, Crossroads GPS reported spending $74,510,334 on political activity in 2012, and earning no investment income at all.”). It can avoid this tax by registering a separately segregated fund under Section 527(f), but all donors to such a fund must be disclosed. See I.R.C. § 527(f)(3).

\(^{56}\) See, e.g., Matea Gold, Secret Donors Pour Millions of Dollars into Crossroads GPS, L.A. TIMES (Apr. 17, 2012), http://articles.latimes.com/2012/apr/17/news/la-pn-secret-donors-pour-millions-of-dollars-into-crossroads-gps-20120417; Americans For Tax Reform—Cycle 2012 Donors, OPENSECRETS.ORG, http://www.opensecrets.org/outsidespending/contrib.php?cmte=Americans+for+Tax+Reform&cycle=2012 (last visited Feb. 4, 2014) (noting, inter alia, that Crossroads GPS donated $26,400,000 to Americans For Tax Reform in 2010 and 2011 and that it was not required to disclose who contributed to that donation). Currently, there is no rule requiring these transfers to “count” as political activity for the purposes of the primary purpose test, although under the IRS’s proposed regulations this would change. See NPRM, supra note 13, at 71,541-42 (proposing that a contribution made to 501(c) organizations will not count as a contribution to an organization engaged in candidate-related political activity only if an officer of the recipient organization certifies that his or her organization does not engage in candidate-related political activity, and a written attestation is made stating that the funds will not be used for candidate-related political activity).

\(^{57}\) Although the Bipartisan Campaign Reform Act of 2002 (“BCRA”) included a provision designed to at least partially foreclose this circumvention by requiring the disclosure of all contributors of $1000 or more to any group that runs an “electioneering communication,” the FEC subsequently interpreted that provision to refer to only those donors who contributed expressly for the purpose of funding such communications, echoing the Court’s decision in Buckley as well as a similar and long-overlooked regulation on disclosure of independent expenditures. See Buckley v. Valeo, 424 U.S. 1, 74-82 (1976) (per curiam); 2 U.S.C. § 434(f)(3); 11 C.F.R. § 109.10(e)(vi) (2014); Trevor Potter & Bryson B. Morgan, THE HISTORY OF UNDISCLOSED SPENDING IN U.S. ELECTIONS & HOW 2012 BECAME THE “DARK MONEY” ELECTION, 27 NOTRE DAME J.L. ETHICS & PUB. POL’Y. 383, 417 (2013). The FEC’s interpretation of BCRA’s electioneering communications disclosure provision was further narrowed in a subsequent ruling to require the disclosure of only donors who gave more than $1,000 with the express purpose of funding a particular electioneering communication. See 11 C.F.R. § 104.20(c)(9); Fed. Election Comm’n, Statement of Reasons of Chairman Matthew S. Petersen and Commissioners Caroline C. Hunter and Donald F. McGahn, MUR 6002, at 5 (Aug. 13, 2010), available at
These expansive options come with few disclosure requirements. A social welfare group is expected to report its donors to the IRS, but this list is not publicly available. It also must make a timely disclosure to the FEC if it funds certain broadcast advertisements, but it generally does not have to disclose the source of the funds behind the advertisements. The only disclosure required for other campaign activities is to the IRS in an annual Form 990 filing, which takes place long after the spending occurs. Moreover, as a practical matter, unearmarked funds contributed to another social welfare group do not “count” towards the originating organization’s campaign, and thus do not factor into the “primary purpose” analysis.

In the wake of *Citizens United*, political players rushed to exploit these lacunae. As reported by the Center for Responsive Politics, the “total spent by nondisclosing groups more than doubled from $127.1 million in the 2010 cycle to well over $300 million in 2012.” Considering that these numbers are based on the organizations’ own reports to the FEC, and that the only activity they were required to report was express or “functionally” express advertising, the actual amount spent on campaign activity by social welfare groups that do not disclose their donors is likely higher.

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59 See I.R.C. § 4965; 11 C.F.R. § 104.4. See also supra notes 53 and 55.
60 See 2 U.S.C. § 434(f) (2012); 11 C.F.R. § 104.4. For an organization whose taxable year tracks the calendar year, 990s are not due until the following March, and in practice most groups request and are granted two three-month extensions. See INTERNAL REVENUE SERV., INSTRUCTIONS FOR FORM 990 RETURN OF ORGANIZATION EXEMPT FROM INCOME TAX, at 6 (2013), available at http://www.irs.gov/pub/irs-pdf/i990.pdf. Organizations can extend this reporting deadline further by changing their tax year. Many reports relating to the 2012 elections were not available to analysts until September 2013.
The IRS, in contrast, did not rush; in fact, quite the opposite. In the spring of 2013, the Exempt Organizations division of the IRS attracted the ire of members of Congress, particularly Republicans, when TIGTA reported that agents had held up requests for recognition of exemption under Section 501(c)(4) by groups with conservative-sounding names.64 (It later emerged that groups with progressive-sounding names had also been flagged.65) The application processing was delayed—in some cases by more than three years—because the reviewing IRS agents were concerned that the requesting entity was engaged in an impermissible level of political campaign activity, and there was an internal lack of guidance on how such cases should be processed.66

While the congressional inquiry did not reveal the sinister motivations behind the delays that some had predicted, it did highlight a number of special considerations that will inform the analysis below. First, the complexity of the problem is inherent in the issues and interests involved; it is not attributable to the choice of either a standard or a rule. Applications for 501(c)(4) exempt status described a wide range of activities that could not be classified without context.67 Similarly, 501(c)(3) charities face a total prohibition on political activity—a clear, bright-line rule. This rule has not lessened the amount of administrative and judicial resources devoted to parsing what is political activity, however, in large part because each case

64 TIGTA REPORT, supra note 12, at 5.
66 See TIGTA REPORT, supra note 12, at 17; The IRS: Targeting Americans for Their Political Beliefs: Hearing Before the H. Comm. on Oversight & Gov’t Reform, 113th Cong. 5 (2013) [hereinafter Hearings] (statement of Rep. Elijah E. Cummings, Ranking Minority Member, H. Comm. on Oversight & Gov’t) (stating that IRS agents received little guidance and no oversight).
67 See, e.g., The IRS’S Systematic Delay and Scrutiny of Tea Party Applications: Hearing Before the H. Oversight & Gov’t Reform Comm., 113th Cong. 16 (2013) (written testimony of Carter Hull, Former Tax Law Specialist, Internal Revenue Serv.) (noting that “there was a great deal of variance among the groups and each application needed to be developed according to its particular facts and circumstances”); see also Hearing on Public Charity Organizational Issues, Unrelated Business Income Tax, and the Revised Form 990: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways & Means, 112th Cong. 92 (2012) (statement of Professor Donald Tobin on increased complexity of public charities).
poses its own unique complexities. Indeed, a recent revenue ruling on the subject applied the rule to twenty-one different hypothetical situations, and over at least three of the past election cycles the IRS has conducted an intensive Political Activities Compliance Initiative that focused on 501(c)(3) groups and included both educational and compliance components.

Second, the motivation to circumvent the legal norms in this area is strong. Press reports prior to the 2012 election and the agency’s observations suggest that the spike in 501(c)(4) group applications between 2010 and 2012—during which time they nearly doubled—had less to do with a surge in altruistic impulses and much more to do with the desire to avoid the spending and disclosure limitations of campaign finance laws by taking advantage of the newly discovered right of corporations to spend freely in elections.

Third, notwithstanding the specter of Nixonian retaliation schemes, the investigation showed that far from being in thrall to the White House,
most of the IRS agents processing the social welfare applications were largely oblivious to the political implications of their actions. Their focus was on determining the content of the law with, as some noted, little guidance on how to evaluate newly formed organizations such as Crossroads GPS, which was founded by former Bush White House advisor Karl Rove and spent more than $71 million on election activity in the 2012 cycle.

The lack of political awareness suggested by agents’ use of the shorthand “Tea Party group” to refer to the issue internally and the fact that the suspect applications appear to have first been flagged as an emerging issue by a self-described “conservative Republican” both underscore the apolitical nature of the IRS’s approach. As we will see in Part III, this stands in sharp contrast to the FEC’s administration of FECA.

The “scandal” largely faded from the headlines as congressional investigations failed to find any evidence of political animus behind the delays in

73 Memorandum from Democratic Staff to Democratic Members of the Oversight and Gov’t Reform Comm. (July 16, 2013), at 35-36, available at http://democrats.oversight.house.gov/sites/democrats.oversight.house.gov/files/migrated/images/user_images/gt/MemoOnNoPoliticalTargetingAtIRS.pdf (testimony of Holly Paz) (explaining that use of term “Tea Party” internally was “sort of a shorthand reference . . . . [I]t’s like calling soda ‘Coke’ or . . . tissue ‘Kleenex.’ They knew what they meant, and the issue was campaign intervention. . . . [M]any of these employees have been with the IRS for decades and were used to a world where how they talked about things internally was not something that would be public or that anyone would be interested in.”). Indeed, only two positions at the IRS are political appointments—the commissioner and chief counsel—and the commissioner was a Republican appointee at the time the events in question occurred. STAFF OF H. COMM. ON OVERSIGHT & GOV’T REFORM, 112TH CONG., POLICY AND SUPPORTING POSITIONS 124-27 (Comm. Print 2012), available at http://www.gpo.gov/fdsys/pkg/GPO-PLUMBOOK-2012/pdf/GPO-PLUMBOOK-2012.pdf; see also Rick Ungar, No Dirty Politics in IRS Investigations of Tea Party, FORBES (May 10, 2013, 5:15 PM), http://www.forbes.com/sites/rickungar/2013/05/10/no-dirty-politics-in-irs-investigations-of-tea-party/. In contrast, the Department of State has nearly 250 political positions. STAFF OF H. COMM. ON OVERSIGHT AND GOV’T REFORM, supra, at 103-13.

74 See, e.g., Hearings, supra note 66, at 5 (stating that IRS agents received little guidance and no oversight).


77 Deirdre Shesgreen & Gregory Korte, Republican at Cincinnati IRS: Scrutiny Was ‘Normal,’ USA TODAY (June 18, 2013, 7:49 PM), http://www.usatoday.com/story/news/politics/2013/06/18/irs-tea-party-scrutiny/2436289/.
processing.\textsuperscript{78} Left in its wake were less salacious but more trenchant questions about where to draw the line between charity and politics, the purpose of the income tax exemption, and how the IRS can best balance the twin goals of processing requests for recognition in a timely manner and preventing an end-run around the tax—and campaign finance—laws. Unfortunately, history provides scant help in answering these questions. The discussion below briefly reviews the history of the “primary activity” test and the deference courts have granted Congress in choosing what activities are entitled to a subsidy through Section 501.

B. The Fine Line Between Social Welfare and Politics: A Brief History of Section 501(c)

The notion of tax-exempt entities has existed for nearly as long as the concept of income tax itself.\textsuperscript{79} Its first modern U.S. version came in the nonprofit exemption in the Tariff Act of 1913 (passed the same year the Sixteenth Amendment was ratified).\textsuperscript{80} Lawmakers spent the next century expanding and refining this definition; today Section 501(c) lists twenty-nine categories of tax-exempt organizations.

In 2013, more than a million of the roughly 1.6 million groups claiming an exemption under Section 501 were 501(c)(3) charities, and a proportionately large amount of internal guidance and external commentary have focused on this section.\textsuperscript{81} These groups receive a double tax benefit: not only are they exempt from income tax, but unlike most other 501(c) organizations, donations to them are tax-deductible for taxpayers who itemize.\textsuperscript{82}

\textsuperscript{78} See Press Release, Ways and Means Comm. Democrats, supra note 65. None of the agents interviewed by congressional investigators believed that applications were targeted because of political bias inside the agency (nor was there evidence of White House interference in the process); instead, they were grouped together to avoid the risk of inconsistent treatment. See Sam Stein, IRS Targeted Progressive Groups, Too, Documents Reveal, HUFFINGTON POST (June 24, 2013), http://www.huffingtonpost.com/2013/06/24/irs-progressive-groups_n_3492679.html.


\textsuperscript{80} Tariff Act of 1913, ch. 16, § II (G)(a), 38 Stat. 114, 172 (1913) (exempting “any corporation or association organized and operated exclusively for religious, charitable, scientific, or educational purposes, no part of the net income of which inures to the benefit of any private shareholder or individual”).

\textsuperscript{81} See INTERNAL REVENUE SERV., INTERNAL REVENUE SERVICE DATA BOOK 2013, at 56 (2014), available at http://www.irs.gov/pub/irs-soi/13databk.pdf. Because some groups, such as churches or subsidiaries of entities that have already been approved for charitable status, do not need to apply for approval and not every entity is required to file an annual Form 990, this figure understates the total number of 501(c)(3) groups operating today. See, e.g., I.R.C. § 6033(a)(3) (2012).

\textsuperscript{82} A handful of non-501(c)(3) groups can also accept tax-deductible donations, including a few limited categories of social welfare organizations (certain veterans’ organizations and volunteer fire
There is a trade-off for this privilege. Charities and churches are permitted only a “non-substantial” amount of lobbying, and since 1954 they have been prohibited from intervening in political campaigns at all. They also must apply for recognition of their status with the IRS; social welfare groups may do so, but it is not required.

By contrast, 501(c)(4) groups, such as Planned Parenthood and the National Rifle Association, face no restrictions on their lobbying and are allowed a limited amount of campaign activity. These organizations also cannot accept tax-deductible donations; perhaps as a consequence, 501(c)(3) groups outnumber 501(c)(4) organizations by more than ten to one. Commentators have opined that these functional differences are the primary distinction between 501(c)(4) groups operating as “[c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, [or as] local associations of employees” and 501(c)(3) groups operating “exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes.” The purpose of each is to do good work for the community.

Despite—or perhaps because of—its ancient pedigree, little contemporary explanation exists in the congressional record discussing why lawmakers...

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83 See, e.g., Treas. Reg. § 1.501(c)(3)-1(e). A charity may choose to make a “Section (b)” safe harbor election, which permits it to spend 20% of its first $500,000 of “exempt purposes expenditures” on lobbying, 15% of the second $500,000, 10% of the third $500,000, and 5% of any additional expenditures, so long as total lobbying expenses do not exceed $1,000,000. I.R.C. §§ 501(h), 4911.

84 Id. § 501(c)(3) (providing that charities cannot engage in activity that influences or attempts to influence legislation). See also Benjamin M. Leff, “Sit Down and Count the Cost”: A Framework for Constitutionally Enforcing the 501(c)(3) Campaign Intervention Ban, 28 VA. TAX. REV. 673, 677 (2009) (questioning the constitutionality of the IRS’s complete ban on campaign-related activity by charities).

85 See TIGTA REPORT, supra note 12, at 1.

86 I.R.C. § 501(c)(4).

87 See id. § 170(c).

88 See INTERNAL REVENUE SERV., supra note 81, at 56 (reporting that in 2013 there were 1,052,495 Section 501(c)(3) charities and 91,056 Section 501(c)(4) social welfare groups).

89 I.R.C. § 501(c)(3).

90 Id. § 501(c)(3). See Raymond Chick & Amy Henchey, Political Organizations and IRC 501(c)(4), in EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION (CPE) TECHNICAL INSTRUCTION PROGRAM FOR FISCAL YEAR 1995, at 1 (1994), available at http://www.irs.gov/pub/irs-tege/cotopcm95.pdf. (“In practice, IRC 501(c)(4) has sometimes been used by both the courts and the Service as a ‘catchall’ exemption provision for organizations that lack the accepted essential characteristics of taxable entities, but elude classification under other subparagraphs of IRC 501(c).”).
ers chose to exempt certain charitable and benevolent organizations from federal tax. The legislative intent behind the original political campaign activity restrictions on tax-exempt groups is likewise lost to time thanks to a paucity of related legislative or agency history. What information we have demonstrates that, notwithstanding some inevitable overlap, lawmakers and regulators have always sought to distinguish political activities from charitable ones. The Treasury Department first denied tax deductions for contributions to organizations that “disseminate controversial or partisan propaganda” in 1919, and the lobbying restriction for 501(c)(3) groups was codified in 1934. Twenty years later, then-Senator Lyndon B. Johnson added a provision to that section of the Code denying 501(c)(3) tax-exempt status to “those who intervene in any political campaign on behalf of any candidate for any public office” by a floor amendment. Regulations issued

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91 Scholars and policy analysts have proposed a number of reasons for the social welfare exemption found in Section 501(c)(4), but these are more helpful as justifications for an exemption than as a methodology to distinguish those organizations actually exempted by Congress from those that are not. For example, one argument proposes that Congress wished to reward (or subsidize) charitable actions; a less generous gloss suggests that the exemption is a way of acknowledging that these groups perform activities that would otherwise fall to the government and, in doing so, save the government money by relieving it of the burden of serving those in need. See 26 C.F.R. § 1.501(c)(3)-1(d)(2) (2014) (defining “charitable” to include, inter alia, “[r]elief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare”). Another line of argument takes the position that there is no reasonable way to measure the net income of a nonprofit under traditional tax principles. See STAFF OF J. COMM. ON TAXATION, 109TH CONG., HISTORICAL DEVELOPMENT AND PRESENT LAW OF THE FEDERAL TAX EXEMPTION FOR CHARITIES AND OTHER TAX-EXEMPT ORGANIZATIONS 3-4 (Comm. Print 2005). A third line of argument proposes that organizations are either exempt because Congress has decreed it so or, less reductively, because the cost of administering the tax exceeds the expected benefit. See id. at 4. Even if the scope of any one of these suggestions were co-terminal with the groups described in Section 501, none lend themselves to a bright-line rule.

92 See Elizabeth Kingsley & John Pomeranz, A Crash at the Crossroads: Tax and Campaign Finance Laws Collide in Regulation of Political Activities of Tax-Exempt Organizations, 31 WM. MITCHELL L. REV. 55, 73 n.83 (2004) (“Unfortunately, no publicly available regulatory history sheds any light on the rationale underlying adoption of the IRS interpretation that social welfare activities do not include political activity.”).

93 See Oliver A. Houck, On the Limits of Charity: Lobbying, Litigation, and Electoral Politics by Charitable Organizations Under the Internal Revenue Code and Related Laws, 69 BROOK. L. REV. 1, 9 & n.44 (2003) (quoting T.D. 2831, 21 Treas. Dec. Int. Rev. 285 (1919)) (internal quotation marks omitted). The Treasury Department said no more at the time, but an interpretive ruling the following year explained, “It is a matter of common knowledge that propaganda in the popular sense is disseminated not primarily to benefit the individual at whom it is directed, but to accomplish the purpose or purposes of the person instigating it.” Id. at 10 (quoting S. 1362, II-2 C.B. 152 (1920)) (internal quotation marks omitted).


95 100 CONG. REC. 9604 (1954) (statement of Sen. Lyndon Johnson). The provision was inserted with no contemporaneous explanation, though some have speculated that a difficult reelection campaign
by the IRS in 1959 clarified the scope of these restrictions for 501(c)(3) groups and, for 501(c)(4) groups, added the above-quoted language stating that political campaign activity does not promote social welfare in the eyes of the IRS.\textsuperscript{96} The regulations administering Section 501(c)(4) remained largely unchanged until the recent rulemaking efforts.\textsuperscript{97}

In his examination of available records, Professor Oliver Houck suggests that at the time its income tax (and, indeed, campaign finance laws) was first being developed, America was caught between the “English view” that “[i]t is not charitable to change the status quo”\textsuperscript{98} (i.e., engage in political activity) and a more free-wheeling acceptance of political machinations as part of the “Big Democratic Bazaar.”\textsuperscript{99} This tension still exists today.

The facts-and-circumstances approach to the activity of social welfare organizations seeks to accommodate these competing viewpoints, and what commands the IRS and Congress have set out in this area do little more than maintain the distance between politics and the “common good” without clearly defining the line between them. That task Congress has left to the agency and the courts; the next sections outline their efforts in this regard.

C. \textit{Patrolling the Boundary Between Social Welfare and Politics: How the IRS Applies the Standard}

In administering the 1959 regulations, the IRS considers all relevant facts and circumstances in evaluating whether a social welfare organization has crossed the line into excessive political intervention.\textsuperscript{100} This approach is hardly unique; the IRS has used a facts-and-circumstances analysis under nearly every subsection of Section 501(c), not just 501(c)(4),\textsuperscript{101} and it has

\begin{footnotesize}
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\item \textsuperscript{96} Compare Treas. Reg. § 1.501(c)(3)-1(d)(2) (1959), with Treas. Reg. § 1.501(c)(4)-1(ii) (1960).
\item \textsuperscript{97} \textit{See} NPRM, supra note 13, at 71,535-36 (noting that, although the Section 501(c)(4) regulations have not been amended since 1959, Congress has undertaken some measures to clarify the proper level of permissible campaign activity for tax-exempt groups, specifically by enacting Section 527 of the Code in 1975, which provides the framework for regulating political organizations).
\item \textsuperscript{98} Houck, supra note 93, at 7.
\item \textsuperscript{99} Id. at 8.
\item \textsuperscript{101} \textit{See}, e.g., I.R.S. Gen. Couns. Mem. 39,792 (June 30, 1989) (asserting that a facts-and-circumstances analysis should be used to determine whether a group’s activities qualify it for tax-exempt status under Section 501(c)(3)); I.R.S. Gen. Couns. Mem. 37,772 (Nov. 30, 1978) (inferring from the facts and circumstances of the day-to-day activities of a trade association that the association
\end{itemize}
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applied this analysis to evaluate many different characteristics of social welfare groups, including public benefit, commerciality, and private inurement. Nor is the use of facts and circumstances limited to tax-exempt organizations; it mirrors the methodology the IRS has long used to provide content to legislative commands across the Internal Revenue Code, applying the law to the unique set of circumstances that a specific case presents. In this sense, it is hardly unusual; Congress asks the same of every agency. Through the years, Congress has accepted and even endorsed the IRS’s use of facts and circumstances to gauge an entity’s level of political activity.

The IRS typically sets out factors relevant to its analysis in publicly available documents. For example, Revenue Ruling 2004-6 lists several was eligible for tax-exempt status under Section 501(c)(6)); Rev. Rul. 58-589, 1958-2 C.B. 266 (applying a facts-and-circumstances test to determine whether a group qualifies as a tax-exempt social club under Section 501(c)(7)); I.R.S. Gen. Couns. Mem. 36,810 (Aug. 6, 1976) (applying facts and circumstances to find that payments to a cemetery were not for an exempt purpose under Section 501(c)(13)).

See, e.g., Rev. Rul. 73-349, 1973-2 C.B. 179 (finding that a grocery cooperative was not tax-exempt because it was not organized primarily for public benefit); Rev. Rul. 66-273, 1966-2 C.B. 222 (finding that a group that educates the community about the proper handling of shotguns is tax-exempt because the activity does not inure to the benefit of private individuals); Rev. Rul. 55-516, 1955-2 C.B. 260 (finding that a semiprofessional baseball club is not a tax-exempt social welfare club because the group’s principal activity was for commercial purposes).


See, e.g., Gonzales v. Oregon, 546 U.S. 243, 266 (2006) (recognizing “the presumption that Congress delegates interpretive lawmaking power to the agency rather than to the reviewing court” (quoting Martin v. Occupational Safety & Health Rev. Comm’n, 499 U.S. 144, 153 (1991)) (internal quotation marks omitted)).

See, e.g., H.R. REP. No. 100-495, at 1021-22 (1987) (Conf. Rep.) (noting House and Senate agreement, regarding the question of excise tax on foundations’ political activity, “that the determination of whether the primary purposes of an organization described in the provision are promoting the candidacy or prospective candidacy of an individual for public office is to be made on the basis of all relevant facts and circumstances”); STAFF OF JOINT COMM. ON TAXATION, 100TH CONG., LOBBYING AND POLITICAL ACTIVITIES OF TAX-EXEMPT ORGANIZATIONS 12 (Comm. Print 1987) (conceding the paucity of “clear standards” for determining who is a candidate in a political campaign, what constitutes intervention in a campaign, and when such intervention is attributable to a particular organization).

These include revenue rulings, revenue procedures, private letter rulings, and general counsel memoranda, which provide opinions on a specific set of facts (and are redacted for confidentiality). See, e.g., supra notes 101-03; see also Ellen P. Aprill, A Case Study of Legislation vs. Regulation: Defining Political Campaign Intervention Under Federal Tax Law, 63 DUKE L.J. 1635, 1649-50 (2014) (discussing the appropriate deference that should be accorded such rulings). Also available for review for anyone with an internet connection are Tax Court decisions, the Internal Revenue Manual, and past training
factors that would suggest that a communication from a social welfare group is intended to influence the election of a candidate (and therefore be subject to tax under Section 527(f)). It illustrates these factors by applying them to six hypothetical situations. An even more detailed revenue ruling was released in 2007 and provided significant guidance on what constitutes political intervention under Section 501(c)(3), with twenty-one separate examples applying the principles it set forth.

So where is the line? A common misapprehension among even some campaign finance professionals is that the political campaign intervention test largely tracks the lines drawn by FECA, which applies spending limitations and disclosure requirements only to communications containing express or functionally “express” advocacy. On the contrary, the IRS takes “a much broader scope to the concept of participation or intervention in a

documents from the EO division. See, e.g., Chick & Henchey, supra note 90, at 2; see also INTERNAL REVENUE SERV., supra note 40, at 1.

107 Rev. Rul. 2004-06, 2004-1 C.B. 328. The ruling also covered 501(c)(5) and 501(c)(6) organizations. Per the revenue ruling, these “include, but are not limited to, the following”:

a) The communication identifies a candidate for public office;
b) The timing of the communication coincides with an electoral campaign;
c) The communication targets voters in a particular election;
d) The communication identifies that candidate’s position on the public policy issue that is the subject of the communication;
e) The position of the candidate on the public policy issue has been raised as distinguishing the candidate from others in the campaign, either in the communication itself or in other public communications; and
f) The communication is not part of an ongoing series of substantially similar advocacy communications by the organization on the same issue.

Id. at 330.

108 Id.

109 Rev. Rul. 2007-41, 2007-01 C.B. 1421. The IRS long indicated that these same principles apply to its analysis of 501(c)(4) organizations, although under the proposed agency rulemaking the agency appears to anticipate changing this approach. See, e.g., Chick & Henchey, supra note 90, at 6 (“IRC 501(c)(4) does not define political campaign activities; instead, the definition and interpretation of terms used has occurred principally under IRC 501(c)(3)’); NPRM, supra note 12, at 71,535.

110 See 2 U.S.C. § 434(17) (2012) (defining “independent expenditure”); id. § 431(f)(g) (reporting requirements for electioneering communications and independent expenditures); see also FEC v. Wis. Right for Life, Inc., 551 U.S. 449, 482 (2007) (expanding definition of “electioneering communications’); Citizens United v. FEC, 558 U.S. 310, 366-68 (2010) (upholding disclosure requirements for electioneering communications); Donald B. Tobin, Campaign Disclosure and Tax-Exempt Entities: A Quick Repair to the Regulatory Plumbing, 10 ELEC. L. J. 427, 434 (2011) (noting that public comments by Steven Law, president of Crossroads GPS, suggested that he was conflating the FEC’s test for express advocacy with the IRS’s standards for intervention in a political campaign). Under the NPRM, the IRS would borrow from the FEC in defining “candidate-related political activity.” Compare, e.g., 2 U.S.C. § 434(f)(3)(A) (2007) (defining “electioneering communication” as “a broadcast, cable, or satellite communication that refers to a clearly identified candidate for federal office and is made within 60 days before a general election or 30 days before a primary election”), with Prop. Treas. Reg. § 1.501(c)(4)-1(a)(2)(iii)(1) 78 Fed. Reg. 71,535, 71,541 (Nov. 29, 2013) (defining “candidate-related political activity” as, inter alia, “[a]ny public communication . . . within 30 days of a primary election or 60 days of a general election that refers to one or more clearly identified candidates in that election or, in the case of a general election, refers to one or more political parties represented in that election”).
political campaign” than federal campaign finance laws. It will consider the totality of the circumstances, not formulaic definitions. For example, an organization’s use of its own website to endorse certain candidates would not be considered an “electioneering communication” subject to regulation by the FEC, but the IRS considers it political intervention for the purposes of evaluating the group’s primary activity. As discussed below, it is able to do so in part because the courts do not subject the primary activity restrictions to the same level of constitutional scrutiny as campaign finance restrictions.

D. The Political Intervention Limitation and the Courts

Because campaign finance reform implicates the First Amendment, its limitations, prohibitions, and other burdens are strictly scrutinized by the courts. Some have suggested that because they impact organizations’ decisions on whether to engage in certain kinds of speech, the political campaign intervention restrictions in Section 501 should also be subject to strict scrutiny. However, courts have repeatedly rejected these arguments under two different rationales.

The first line of cases adopts the view that tax breaks need not be accorded First Amendment protections. This rationale dates back to the 1930 Second Circuit opinion in *Slee v. Commissioner*. In upholding the agency’s decision to deny a tax exemption to the American Birth Control

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111 See Kindell & Reilly, * supra* note 95, at 349. (“The statute clearly states that participation or intervention in a political campaign includes publication or distribution of statements, which denotes that prohibited political campaign activity is not to be limited to statements. It would do violence to the statute, not to mention over 45 years of interpretation, to adopt the ‘express advocacy’ standard.” (emphasis omitted)); *see also* Rev. Rul. 2004-06, 2004-1 C.B. 328; Rev. Rul. 2007-41, 2007-1 C.B. 1421.


114 Compare I.R.C. § 527(e)(2) (2012), with 11 C.F.R. § 100.26 (2014); *see also NPRM, supra* note 13, at 71,541.


116 Some commentators have proposed “void-for-vagueness” as an alternate ground to challenge the facts and circumstances inquiry, *see e.g.*, Kingsley & Pomeranz, * supra* note 92, at 106-07, and such a challenge has found traction in campaign finance jurisprudence, *see e.g.*, Buckley v. Valeo, 424 U.S. 1, 40-41 (1976) (per curiam). However, the only significant vagueness challenge that has been upheld in the tax-exempt context came in a D.C. Circuit opinion about the IRS’s definition of “educational” for 501(c)(3) purposes more than thirty years ago, and the same court backed away from its holding a few years later. *See Big Mama Rag, Inc. v. United States*, 631 F.2d 1030, 1039 (D.C. Cir. 1980), *holding limited by Nat’l Alliance v. United States*, 710 F.2d 868, 874 (D.C. Cir. 1983). It is provocative today to contemplate a vagueness challenge to the facts and circumstances analysis for campaign intervention—and the potential implications for the IRS of a decision on these grounds—but it is beyond the scope of this Article.

117 *Slee v. Comm’r*, 42 F.2d 184, 185 (2d Cir. 1930).
League, Judge Learned Hand explained that “[p]olitical agitation as such is outside the statute, however innocent the aim,” adding, in a line that would appear in many subsequent opinions, “[c]ontroversies of that sort must be conducted without public subvention; the Treasury stands aside from them.” The Supreme Court affirmed this reasoning as recently as 2013 in *Agency for International Development v. Alliance for Open Society International, Inc.* This opinion appeared to answer, for now, speculation that language in *Citizens United* suggested that the Court might reconsider its cases affirming the political activity and lobbying restrictions in Section 501(c).

The second rationale was developed in Justice Blackmun’s concurrence in the Supreme Court’s 1983 case *Regan v. Taxation With Representation*. Taxation With Representation wished to organize as a 501(c)(3) organization so that it could accept tax-deductible contributions, but it objected to the limits Congress and the IRS placed on the ability of charitable organizations to lobby. The majority applied the *Slee* line of cases to hold that a right to free speech did not include the right to have other taxpayers subsidize that speech. Justice Blackmun acknowledged the potential First Amendment burden that lobbying restrictions place on a charitable organization, but he found constitutional comfort in the fact that the IRS provides a work-around: a 501(c)(3) organization can separately incorporate a 501(c)(4) affiliate. So long as it keeps adequate records to show that no tax-deductible contributions are being used for “impermissible” lobbying or political activity, it can both engage in lobbying activities and benefit from tax-deductible contributions. Indeed, this is the structure adopted today by many leading advocacy organizations.

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118 *Id.; accord Cammarano v. United States, 358 U.S. 498, 512 (1959); see also Regan v. Taxation With Representation, 461 U.S. 540, 549 (1983) (“We have held in several contexts that a legislature’s decision not to subsidize the exercise of a fundamental right does not infringe the right, and thus is not subject to strict scrutiny.”).*


122 *Regan, 461 U.S. at 545 (“The Code does not deny TWR the right to receive deductible contributions to support its non-lobbying activity, nor does it deny TWR any independent benefit on account of its intention to lobby. Congress has merely refused to pay for the lobbying out of public moneys.”). The Court relied on its earlier decision in *Cammarano*, which in turn had cited *Slee*. *Id. at 546.*

123 *Id. at 553 (Blackmun, J., concurring).*

124 *Id.; accord Houck, supra note 93, at 69. Although Justice Blackmun did not cite *Buckley v. Valeo*, the Court had used a similar rationale there when it found that spending restrictions on publicly-funded candidates were constitutional because a presidential candidate could always reject the public financing—as they eventually did. See *Buckley v. Valeo*, 424 U.S. 1, 101 (1976) (per curiam).*

In sum, the IRS has used a facts-and-circumstances test for more than five decades to evaluate an organization’s purpose and activities, including activities that arguably intervene in an election. This approach has been endorsed by Congress, both explicitly and tacitly, and upheld and employed by the courts.

Of course, “we’ve always done it this way” is hardly a justification for continuing to do so. The next section considers the advantages and disadvantages of both rules and standards and applies them to the IRS’s political activity limitations.

II. RULES VERSUS STANDARDS: THEORY AND PRACTICE

There are a number of criteria against which one could evaluate the comparative advantages of ex ante rules versus ex post standards. Most of the analysis below adopts the criteria suggested by Professor Louis Kaplow in his oft-cited article “Rules Versus Standards: An Economic Analysis”: the amount of “legal costs and the extent to which individuals’ behavior conforms to the law.” Considering the rules/standards framework from both a theoretical and practical vantage, this Article concludes that notwithstanding the current push for bright-line rules to identify excessive intervention in political campaigns, there is much to be said in defense of a standards-based regime. This is particularly true when one considers the degree of complexity, level of circumvention, and amount and nature of enforcement actions in this area.

A. The Framework

Many trees have been sacrificed to the detailed examination of rules and standards and the distinctions between them. In short, rules provide ex ante “bright lines” against which conduct can be judged; standards rely on an ex post adjudicator to consider how more general principles should apply in a specific case. The paradigmatic example of a rule is a speed limit

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126 Note that the following discussion uses “rules” and “standards” as terms of art as defined here-in. In particular, “rules” as discussed in this Article should not be confused with the results of agency rulemaking, which can, indeed, produce either rules or standards. See Kaplow, supra note 21, at 616-17 (noting that rules can be generated by legislatures, agencies, or courts).

127 Id. at 562.

128 Id. at 586; see also Ehud Gutel & Alon Harel, Uncertainty Revisited: Legal Prediction and Legal Postdiction, 107 Mich. L. Rev. 467, 479-81 (2008) (admitting that, although both rules and standards generate certain levels of uncertainty, there are distinct compliance and enforcement costs between the two); Russell B. Korobkin, Behavioral Analysis and Legal Form: Rules vs. Standards Revisited, 79 Or. L. Rev. 23, 46-47 (2000) (identifying the ways that rules and standards impact behavior, specifically, the way they affect an individual’s “self-serving bias”).
of fifty-five miles per hour; contrast this with a standard that exhorts drivers to travel at a “reasonable and prudent” speed.\(^{129}\) Rules thus have the advantage of clearly communicating expectations; standards have the advantage of taking into account special or changing circumstances (e.g., inclement weather; traffic conditions).

Professor Kaplow proposes a methodology for determining whether a rule or standard should be preferred in a given circumstance based on the total cost imposed by each approach.\(^{130}\) His analysis weighs the systemic cost of promulgating either a rule or standard against the systemic cost of enforcing it and adds to each side of the equation the societal costs of either regime, that is, how much it would cost individuals to acquire legal advice about the rule or standard and how likely it is in a given regime that they would do so.

Professor Kaplow’s analysis turns on a series of insights. First, because it is costly to determine a law’s precise content at any stage of the process, he assumes that it is more costly to promulgate a rule than a standard and more costly to enforce a standard than a rule. Therefore, the frequency with which a law is likely to be applied is “of central importance” in deciding whether it is worth engaging in a costly up-front procedure to define a precise rule or waiting until afterwards to apply a standard.\(^{131}\) The negligence standard in tort, for example, can apply to a diverse set of circumstances that would be difficult to identify in advance.\(^{132}\) On the other hand, as Professor Kaplow notes, “some federal income tax provisions apply to millions of individuals and billions of transactions”; in these situations, rules are generally preferable as they answer common questions in advance.\(^{133}\)

Professor Kaplow’s reasoning, and his preference for rules in situations where others might prefer standards, rests in large part on the costs associated with the intervening stage between promulgation and enforcement—namely, learning the law. Professor Kaplow assumes that individuals will choose to become informed about the contents of a rule or standard if the benefits of doing so outweigh the costs.\(^{134}\) Learning the law is presumed to be desirable because we want people’s behavior to conform to the underlying norms. Because it is cheaper to learn the content of a rule than to consider multiple factors and predict how a standard will be applied


\(^{130}\) Kaplow, supra, at 589-90.

\(^{131}\) Id. at 563.

\(^{132}\) Id. at 573.

\(^{133}\) Id. at 573, 577.

\(^{134}\) Id. at 574.
(consider again the speed limit example above), rules are generally preferable from an economics point of view. In a situation where the benefit of knowing the law would make one want to learn either the rule or standard, a rule lowers the cost of information acquisition. On the other hand, if the benefit is only marginal, it may be worthwhile to learn about a rule but not a standard, a result that again favors rules.

Professor Kaplow also rejects what he sees as a common analytic fallacy, namely, that “simple rules are often compared to complex standards; most commonly, it is asserted that rules tend to be over- and/or underinclusive relative to standards.” In other words, commentators conflate the choice of rules or standards with a choice of a simple or complex legal regime. However, as Professor Kaplow notes, either a rule or standard can be as complex as needed in order to capture the full content of the legal command; the only question is whether the potential outcomes are weighed ex post or ex ante. Thus, he argues that concerns about complexity should not factor into one’s decision to adopt a rule or standard. In his view, one should be able to achieve a nuanced outcome from either approach.


Notwithstanding the strong case that Professor Kaplow makes for rules in many situations where, at first blush, a standard may be preferable, the situation presented by the “Tea Party scandal” is not such an instance. Even under his analysis, the political activity of social welfare groups should continue to be evaluated under a facts-and-circumstances standard. The discussion below highlights theoretical and practical issues that lawmakers and regulators should consider as they contemplate reformation of the regulations governing 501(c)(4) groups and similar tax-exempt organizations.

1. Problems with Complexity

One can start by “problematizing” Professor Kaplow’s assertion that complexity ought not to factor in to one’s calculation of whether a rule or a standard is best suited to address a particular problem. While it may be true that both rules and standards can be as complex as necessary—the Internal

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135 Id. at 576.
136 Kaplow, supra note 21, at 588-89.
137 Id. at 586-96. Professor Kaplow suggests the following construction to evaluate rules that are “equivalent” to standards: “For any standard, consider the actual outcomes that would arise for all possible cases. Now, define the ‘rule equivalent to the standard’ . . . as that rule which attaches these same outcome to these cases.” Id. at 586.
138 Id. at 596 (“The main point to recognize is that there is no universal tendency for standards as they are actually applied to be more complex than rules that would plausibly be promulgated.”).
Revenue Code, after all, weighs in at nearly four million words—that is not the end of the inquiry. Complexity comes with its own set of issues. A rule “equivalent” to the current political activity limitation standard—that is, allowing the IRS to reach the same outcome for all reasonably foreseeable circumstances—would require a high level of complexity, and thus a high promulgation cost, but may not yield a corresponding reduction in enforcement costs. Promulgation costs are further exacerbated where a culture of circumvention (discussed further below) would require frequent changes to the rules. Complexity has another cost as well: it can undermine the public’s view of the government, thus achieving a result contrary to the stated goal of the Code (and, for that matter, campaign finance reform).\textsuperscript{139}

The level of detail required to anticipate every uncommon transaction makes it far more expensive to promulgate a rule against an uncommon transaction than it is to enforce a standard after the fact. This is not a new critique. In his defense of the IRS’s anti-abuse program, which eschews bright-line rules, Professor David Weisbach argues that even if “complexity neutrality” is possible in theory, it is not possible in practice for much of tax law.\textsuperscript{140} He points to a culture of tax avoidance and an emphasis on the form of transactions under the Internal Revenue Code as reasons that even a complex rule cannot substitute for a complex standard. A sufficiently complex ex ante rule must take into account not just common transactions that can be readily anticipated, but also all of the less common transactions that taxpayers will seek out if the common transaction is subject to tax or regulation.\textsuperscript{141}

The high probability that savvy taxpayers and their planners will seek to circumvent the rules also means that any rules would have to be updated frequently; the IRS (or Congress) would always be playing catch-up.\textsuperscript{142} Consider, for example, recent efforts to address offshore bank accounts\textsuperscript{143} or corporate profit shifting.\textsuperscript{144} Where there is a culture of avoidance, as with

\textsuperscript{139} See, e.g., S. Rep. No. 95-66 (1977) (proposing to reduce and simplify the complexity of the Internal Revenue Code as applied to individuals and businesses).

\textsuperscript{140} See generally David A. Weisbach, Formalism in the Tax Law, 66 U. CHI. L. REV. 860, 862 (1999) (describing anti-abuse program, specifically referring to the partnership anti-abuse rule, the original-issue discount anti-abuse rule, and the intercompany transaction anti-abuse rule).

\textsuperscript{141} Id. at 869.

\textsuperscript{142} See, e.g., Erik M. Jensen, Legislative and Regulatory Responses to Tax Avoidance: Explicating and Evaluating the Alternatives, 57 ST. LOUIS U. L.J. 1, 2 (2012) (“The target at which Congress and the Service are aiming is moving, and tax avoidance will always be with us.”).

\textsuperscript{143} See, e.g., STAFF OF SUBCOMM. ON INVESTIGATIONS OF S. COMM. ON HOMELAND SECURITY AND GOV’T AFFAIRS, 113TH CONG., OFFSHORE TAX EVASION: THE EFFORT TO COLLECT UNPAID TAXES ON BILLIONS IN HIDDEN OFFSHORE ACCOUNTS 10-22 (Comm. Print 2014) (summarizing thirty years of efforts to close loopholes related to overseas accounts); see also infra note 155.

\textsuperscript{144} See, e.g., Memorandum to the Permanent Subcommittee on Investigations from Senator Carl Levin, Chairman, and Senator John McCain, Ranking Minority Member, Permanent Subcommittee on Investigations, Re: Offshore Profit Shifting and the U.S. Tax Code—Part 2 (May 21, 2014); Caterpillar’s Offshore Tax Strategy: Hearing Before the Permanent Subcomm. on Investigations of the S.
both taxation and campaign finance, complex rules can become recursively more complex—and promulgation costs higher—as lawmakers attempt to staunch leaks. For these reasons, Professor Weisbach posits that the discriminating use of standards actually “prevent[s] the tax law from being too complex.”

Additionally, Professor Kaplow’s methodology requires a comparison of ex ante and ex post costs, so the expense of a complex rule would have to yield a comparative reduction in the cost of enforcement to make it worthwhile. However, this assumption of a corresponding cost reduction presumes that the most significant cost of an enforcement action comes in the deliberation over how a standard should be applied (i.e., the weighing of the relevant factors). Under either a rule or standard, however, the adjudicator must still gather the relevant facts, identify the legal command at issue, and apply those facts to the law.

For these reasons, an ex ante rule in a complex area is unlikely to significantly lessen the number of enforcement actions or the associated costs.

Consider, for example, the campaign intervention prohibition in Section 501(c)(3). The bright-line nature of this prohibition has not reduced the adjudicative burden on the IRS; on the contrary, for three recent election cycles the agency devoted considerable resources to examining reports of illegal campaign activities by charities and churches, and produced a number of reports and additional guidance on the subject.

A rule does not eliminate enforcement actions in complex cases; it merely changes the terms of the debate.

A further problem with complexity is that, to the extent that legal commands are intended to tell individuals how they should conduct themselves, the more complex either a rule or standard is, the more likely it is to diverge from the common understanding of the background norm. This


Weisbach, supra note 140, at 862.


See 2004 PACI REPORT, supra note 68, at 1; 2006 PACI REPORT, supra note 70, at 1; Exempt Organizations, supra note 70, at 1. In 2004, PACI was implemented as part of EO’s multi-faceted strategy to promote compliance with Section 501(c)(3)’s prohibition on improper political activity. According to the 2004 report, “43 agents, one full-time reviewer and one full-time classifier worked on” the project during the initiative’s initial year. See 2004 PACI REPORT, supra note 68, at 7.

See discussion infra regarding litigation over campaign finance rules.

Kaplow, supra note 21, at 597. Professor Kaplow argues that it is not necessarily true that one would have to expend more effort to learn a complex standard than a simple rule, because “[t]he likely (if not certain) result will often be just as obvious under the complex rule as under the [less complex] standard. For example, under a standard requiring safe driving, most drivers would readily anticipate that driving at night without headlights illuminated or parking in the middle of an intersection would be proscribed.
check on intuition may be desirable in some circumstances—we want people to make the effort to learn what animals are on the endangered species list, or to ensure that the chemicals they are dumping are not on a list of hazardous materials. However, where the question at issue is the integrity of the political process and, by extension, the legitimacy of legal commands themselves, a high level of complexity is counterproductive. It is also counterproductive for social welfare groups themselves, many of which traditionally have enjoyed a special status in the public (and congressional) eye in part because of the simple, intuitive appeal of their mission.

A complex legal regime risks alienating people at best or appearing antidemocratic at worst. Consider, for example, the criticisms leveled at the Internal Revenue Code. Notwithstanding the fact that much of its complexity derives from an effort to achieve an optimal degree of fairness and equity, many believe it loses sight of the forest for the trees. If a simple standard represents an organic—if imprecise—social goal, complex rules can resemble a patched-together Frankenstein, with only passing resemblance to the underlying norm.

Id. This is too easy an example, however. A standard requiring safe driving may accommodate the paradigmatic fifty-five mph speed limit, or it could allow drivers to proceed at sixty or even sixty-five miles per hour. A rule—as many drivers learn at some cost—is not as forgiving.


See Brian Galle, Charities in Politics: A Reappraisal, 54 Wm. & Mary L. Rev. 1561, 1597 (2013) (reviewing literature describing how charitable giving enhances a donor’s “warm glow”); see also supra note 90 and accompanying text.


See Andrew Morrison Stumpf, The Law is a Fractal: The Attempt to Anticipate Everything, 44 Loy. U. Chi. L.J. 649, 677 (2013) (arguing that “precision can be a bad thing” in the tax context: “For example, the U.S. Treasury’s replacement of the previous brief (but vague) requirement that tax-qualified retirement plans ‘not discriminate in favor of highly compensated employees’ with over one hundred pages of detailed nondiscrimination regulations answered a number of specific questions that had formerly been left to judges. At the same time, however, the regulations made clear that employers are free to design plans that specifically do so discriminate, up to a precisely drawn point that no one had imagined permissible under the old, ambiguous rule.” (citation omitted)).
2. Problems with Circumvention

The risk of fraud not only helps to highlight the fallacy of “complexity neutrality,” but it also is a concern in its own right. The history of both campaign finance and tax regulation is one of avoidance and circumvention. In such situations, the pure economic analysis of rules versus standards quickly breaks down.

Indeed, Professor Kaplow himself anticipated that his logic might not hold in a situation where a high risk of fraud or circumvention exists, noting that “if there are known rigid rules that a fraudulent actor can carefully circumvent, standards may be preferable in some contexts.” A standard allows adjudicators to evaluate conduct consistently even as behavior patterns shift. Actions that may not be caught by a rule—even a complex rule—are still covered by a standard.

Professor Weisbach expands on this point specifically in the tax context, observing that tax rules can lead to discontinuities that can affect behavior and encourage tax arbitrage. As he notes, in tax “[n]o matter how nuanced a rule is, it will create a bright line between the two types of transactions,” and “small changes in transactional form often create large changes in tax liability.” Such rules can impact behavior across all taxpayers. For example, a wealthy parent may seek to structure an inheritance to avoid the gift tax, while a low-income single parent may choose not to marry rather than risk losing the earned income tax credit.

Standards, on the other hand, do not have the same impact on decision making. While standards may have the same “all-or-nothing” effect once they are applied—a credit is allowed or denied, income is included in adjusted gross income or it is not—because their exact content is not known up front, taxpayers can only guess at probabilities. Thus, standards do not create the same incentives for socially disadvantageous or inefficient transactions that rules do.

In addition to not incentivizing “bad” behavior, social scientists have argued that the uncertainty that comes with standards can encourage “good” behavior by taxpayers and reduce circumvention. Where circumvention is

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155 See Kaplow, supra note 21, at 618-19 (“Such issues suggest that an appropriate framework, taking into account effects on legitimate and fraudulent behavior, would differ from the one presented here.”). Professor Kaplow also notes, correctly, that “laws of form are often designed to prevent fraud,” an insight that both explains reformers’ instincts for bright-line rules and anticipates why this instinct can be misguided. Id. at 618. An emphasis on the form of a transaction rather than its underlying purpose makes it easier to identify and exploit loopholes. Id.
156 See Weisbach, supra note 140, at 870.
157 Id. at 867, 872.
likely, there is an advantage to some murkiness at the margins. For example, Professor Sarah Lawsky notes that “[a] number of empirical studies have found that . . . uncertainty about one’s audit rate may increase tax compliance.” If there is even a chance an act will be found in violation of the law, many people will avoid it altogether. (Consider, for example, decisions you may have made in whether or not to claim certain deductions on your taxes.)

3. Problems with Enforcement

As noted above, a low number of enforcement actions generally counsels for standards over rules. The total cost of a handful of adjudications in which standards must be given meaning is presumed to be less than the cost of an up-front rulemaking process that must consider every possible outcome.

As a percentage of total returns filed, the IRS audit rate is low; in 2012, the overall audit rate for individuals was just over 1 percent, and just slightly higher—1.3 percent—for tax-exempt organizations. Even fewer of these cases raise the political intervention question and merit a review of all relevant facts and circumstances. For example, of the 237,653 charitable entities that filed Form 990 in 2006, only one hundred were examined for potential violations of the ban on campaign intervention for 501(c)(3) organizations.

The low enforcement rate and other realities of enforcement described below are relevant not simply to the relative costs of law promulgation and enforcement; they are also relevant to the impact of the law on individual

160 Id. at 1071.
161 See, e.g., Kaplow, supra note 21, at 563 (acknowledging that standards are preferable when the frequency of enforcement actions is low because standards can be applied to different sets of circumstances).
162 See IRS Releases Data on Audit Rates, CBIZ BLOG (Mar. 29, 2013), http://blog.cbiz.com/2013/03/IRS-audit-rates-for-businesses-individuals.html; see also Lawsky, supra note 159, at 1068 (discussing the low audit rates).
164 Cf. OMB Watch, THE IRS POLITICAL ACTIVITIES ENFORCEMENT PROGRAM FOR CHARITIES AND RELIGIOUS ORGANIZATIONS: QUESTIONS AND CONCERNS 8-9 (2006), available at http://www.foreffectivegov.org/files/pdfs/paci_full.pdf (remarking that, of the 191 examinations from the 2004 PACI Initiative, about 40 percent of them were dismissed as not meriting further investigation). Violations of the “political activity” prohibition were only found in 30 percent of the referred cases, and only three of the cases presented violations egregious enough to warrant revocation of tax-exempt status. Id. at 9.
165 See INTERNAL REVENUE SERV., supra note 81, at 56; 2006 PACI REPORT, supra note 70, at 3.
behavior.\textsuperscript{166} Professor Kaplow partially anticipates this impact in his analysis. He assumes that people will want to learn about the law so that they can follow it, and that the law will appropriately capture the underlying social norms. However, he notes that where the law will not hold individuals fully liable for the harm they cause, either because of a legal error or a misaligned penalty, the resulting disconnect can incentivize private action to learn about the law at the expense of the social values the law seeks to uphold (i.e., the discovery and exploitation of legal loopholes).\textsuperscript{167} Rules can thus simultaneously benefit individual actors but undermine social norms; the net cost is positive (i.e., favors rules) for the individual, but negative for society. This insight echoes Professor Weisbach’s argument above about the discontinuity of rules.\textsuperscript{168}

A low enforcement rate is not itself a legal error or misaligned penalty, but it can create negative incentives for those looking to “handicap” the probability that their violation of the law will result in a penalty. This is true whether the legal command is a rule or a standard, although as noted, the discontinuities in rules can offer additional assurances to the loophole-seeker that are not desirable from the vantage of social norms.\textsuperscript{169}

When it comes to the campaign activity of social welfare groups, however, the enforcement process is further misaligned in two significant ways. First, the worst sanction with which the IRS can threaten a social welfare organization is a tax penalty or loss of tax-exempt status.\textsuperscript{170} Whereas a 501(c)(3) charitable organization that violates the political activity ban loses its status and is prohibited from reorganizing as a 501(c)(4) group,\textsuperscript{171} organizations that lose their 501(c)(4) exempt status due to campaign intervention can always reconstruct themselves as a 527 group (or the individuals behind it can formally form a new 501(c)(4) organization).\textsuperscript{172} Moreover, as a mat-

\begin{itemize}
\item[166] See, e.g., Potter & Morgan, supra note 57, at 469 (“Until it becomes apparent that the IRS is auditing 501(c)(4) political activities or until the IRS announces an enforcement program to police such activities, very politically active 501(c)(4) organizations can reasonably believe they have a green light to spend hundreds of millions to influence federal elections, without any apparent risk of immediate scrutiny or action by the IRS.”).
\item[167] Kaplow, supra note 21, at 603.
\item[168] See Weisbach, supra note 140, at 872.
\item[169] See generally Lawsky, supra note 159.
\item[171] See I.R.C. §§ 501(c)(3), 504(a) (2012).
\end{itemize}
of consequence there is little incentive to refrain from campaign intervention; there is no forced disclosure of donors, and no way to “take back” the campaign activity that has already occurred. Indeed, unlike 501(c)(3) charities, social welfare groups need not apply for status recognition before they begin operating; they are invited to act first and ask (or assert) later.

Second and relatedly, the long delay before a 501(c)(4) organization must report any political activity to the IRS limits the bite of the legal command. For example, as the “Tea Party scandal” played out in the summer of 2013, political watchdog groups were still waiting for most social welfare groups to file their Form 990s for Tax Year 2012, the most recent federal election cycle. For groups treating the calendar year as their tax year and requesting a six-month extension in filing, as is typical, details of their activity during the months leading up to the 2012 presidential election were not filed until September 2013, at which point analysts still had to sort through thousands of pages of filings in order to extract data. (For groups organized with a different tax year [e.g., July-June] reports of spending in the 2012 elections were not due until spring of 2014.) This delay between activity and oversight provides room for considerable gamesmanship. Indeed, several “social welfare” groups that spent money in the 2012 elections were reported to have already closed up shop just months later.

The key observation here is that replacing the “primary activity” inquiry with a rule rather than standard would most benefit those who seek to circumvent the law rather than the social values the standard is meant to safeguard: the preservation of the social welfare exemption for groups that


173 See TIGTA REPORT, supra note 12, at 2. The IRS may ask a 501(c)(3) to pay back the money it spent on campaign intervention, and it presumably could ask the same of a 501(c)(4) group. See, e.g., 2006 PACI REPORT, supra note 70, at 7. This merely closes the proverbial barn door, however; the endorsement or other intervention has already occurred.

174 TIGTA REPORT, supra note 12, at 1. Section 501(c)(3) groups are required to apply for recognition.

175 See INTERNAL REVENUE SERV., supra note 60; see also infra note 176; I.R.C. § 6033.

176 See, e.g., Robert Maguire & Viveca Novak, Shadow Money Magic: Five Easy Steps That Let You Play Big in Politics, Hide Your Donors and Game the IRS—Step 4, OPENSECRETS.ORG (Apr. 18, 2013), http://www.opensecrets.org/news/2013/04/shadow-money-magic-five-easy-steps-3.html (“All in all, a nonprofit has up to eleven months after the end of its fiscal year to file its report with the IRS.”).

177 See INTERNAL REVENUE SERV., supra note 60.

178 Id.

“bring[] about civic betterments and social improvements.” While the enforcement issues outlined above are problematic for both rules and standards, the difficulty in determining in advance how a standard will apply makes it more difficult for individuals to identify and exploit loopholes. An adjudicator retains some flexibility with a standard.

The discussion above also demonstrates the limits of rules where the culture of circumvention is high and enforcement is low. In situations like this, rules cannot accurately map the full contours of a legal command. The most they can do is provide a safe harbor.

Consider again the paradigmatic fifty-five miles per hour speed limit. What is notable about this example is not how often it is used to distinguish a rule from a standard, but how poorly it actually constrains behavior. Most drivers exceed the speed limit on a regular basis. We slow down only where we know we might get caught—for example, if there are speed cameras monitoring. The posted limit only constrains behavior if one is in a high-enforcement area; otherwise, the most it does is provide a zone of safety for the risk-adverse.

In this regard, the speed limit, campaign finance regulation, and the Internal Revenue Code all share something in common: there is a widespread sense that it is acceptable to circumvent each of these regimes so long as you can avoid getting caught. The system does not have the capacity to catch all of the speeders, or tax cheats, or excessive campaign contributors. I make this point not to equate the culpability of the person driving at ninety-five miles per hour and the person wishing to run inflammatory campaign ads without disclosing his identity, but to demonstrate that a low enforcement rate, coupled with a high level of incidence, creates negative incentives to learn the contours of the law so that one may avoid detection yet fails to create positive incentives to comport with the legal command at issue.

4. Political Realities and Unworkable Assumptions

The analysis above proceeds largely in the realm of theory. We should also consider operable facts. Applying Professor Kaplow’s calculus to find that rules should be promulgated to regulate the permissible level of political campaign activities of social welfare groups would require making three assumptions that do not hold in this case.

180 INTERNAL REVENUE SERV., supra note 40, at 1.
181 See Tara Parker-Pope, No Respect for Speed Limits, N.Y. TIMES (Nov. 10, 2008, 10:40 AM), http://well.blogs.nytimes.com/2008/11/10/no-respect-for-speed-limits/?_r=0 (citing that researchers at Purdue University found that many drivers believed that they could drive safely while speeding).
First, Professor Kaplow assumes that the appropriate content of rules can be determined ex ante through legislative or regulatory fact-finding; he acknowledges that where “information will be easier to acquire at the time individuals act or cases are adjudicated,” standards are preferable.\(^\text{183}\) As demonstrated in the brief history of campaign finance reform below, it is impossible to predict in advance all of the ways in which groups will organize to impact elections.\(^\text{184}\) For example, when the Bipartisan Campaign Reform Act (“BCRA”) was enacted in 2002, its definition of “public communication”—those communications covered by the law’s restrictions—did not include internet communications,\(^\text{185}\) and the law certainly did not anticipate the degree of participation in elections now allowed for corporations and unions. Any IRS rules in this area would face similar issues.

Second, Professor Kaplow assumes that it is possible to promulgate rules; for him, the key question in choosing between rules and standards is how often a situation will be adjudicated, not the political viability of either regime.\(^\text{186}\) In the current political climate, however, arriving at either a statute or regulation setting a bright-line rule would require a level of agreement that is unlikely to be achieved.\(^\text{187}\) Moreover, because one of the features of a rule is that an adjudicator’s discretion is limited, the public rhetoric in favor of a rulemaking (whether legislative or administrative) is likely to emphasize the risk of allowing the IRS discretion in these cases.\(^\text{188}\) Such

\(^{183}\) Kaplow, supra note 21, at 585-86.

\(^{184}\) Taken to its logical conclusion, Professor Kaplow’s entire methodology arguably breaks down here. Even if one were to assume that legislators and regulators decide between a rule and standard based on cost effectiveness, the amount of fact-finding that would be required in order to evaluate which system would be the most efficient would quickly land the legislature “in the snares of the infinite regress.” Eric A. Posner, Standards, Rules, and Social Norms, 21 HARV. J.L. & PUB. POL’Y 101, 105-06 (1997).

\(^{185}\) See 2 U.S.C. § 431(22) (2012) (defining “public communication” under FECA). See also 11 C.F.R. § 100.26 (2014) (“The term general public political advertising shall not include communications over the Internet, except for communications placed for a fee on another person’s Web site.”).

\(^{186}\) See generally Kaplow, supra note 21, at 621.

\(^{187}\) See, e.g., THOMAS E. MANN & NORMAN J. ORNSTEIN, IT’S EVEN WORSE THAN IT LOOKS 31 (2012).

\(^{188}\) A leading Republican talking point throughout the “Tea Party scandal” has been the risks of agency discretion. See Stephen Ohlemacher, Tax Overhaul: IRS Scandal Could Lead to Changes, ASSOCIATED PRESS (May 29, 2013), http://news.yahoo.com/tax-overhaul-irs-scandal-could-lead-changes-070447634.html (quoting Rep. David Camp (R-MI), chairman of the House Ways and Means Committee as saying, “I think giving the IRS less discretion is going to be important, and that’s what a simplified code would do.” (internal quotation marks omitted)). However, these same lawmakers have also introduced legislation to block the IRS’s attempt to clarify its approach in this area, see supra note 16, raising the question of whether the political benefits of the “scandal” outweigh the harm any IRS action actually caused. See also Scott Clement, The IRS’ Approval Ratings Are Free Fallin’, WASH. POST (May 28, 2013), http://www.washingtonpost.com/blogs/the-fix/wp/2013/05/28/the-irs-approval-
a discourse would further harm the reputation of IRS administrators, the authority of the agency, and the morale of those who work there—all of which may, in turn, harm the quality of any future adjudication and the respect that any resulting law or regulation commands.

Third, Professor Kaplow’s analysis suggests that the benefit of a rule is that it lessens the costs of enforcement actions, both because it encourages individuals to learn the law and adjust their behavior accordingly, and because each individual adjudication is less costly due to the fact that the contours of the underlying norm have already been defined. In the case of politically active 501(c)(4) groups, however, it is improbable that enforcement actions would come less frequently or more cheaply; the arguments would simply be restated and the terms redefined. This, too, is readily apparent when one considers the speed limit example. While we may want to know ex ante how fast we can go, this will not prevent many of us from arguing that a speeding ticket was issued unfairly in our particular case because, for example, the method of speed detection was unreliable. This is why we have traffic court.

C. Considering the Case for Rules

While the above analysis finds that bright-line rules would be costly and unworkable in regulating 501(c)(4) political activity, arguments do exist in favor of rules. Many of these are cogently laid out by Professor Ellen Aprill in her recent article that applies Professor Kaplow’s calculus to the 501(c)(3) ban on campaign activity. She concludes that instead of taking a facts-and-circumstances approach to evaluating whether charities have engaged in prohibited political activity, “the IRS should invest the time to develop a set of rules.”

189 See, e.g., Tony Schwartz & Christine Porath, Why You Hate Work, N.Y. TIMES (May 30, 2014), http://www.nytimes.com/2014/06/01/opinion/sunday/why-you-hate-work.html?module=Search&refbias%3Ar&.r=0 (summarizing numerous studies showing that lower levels of employee engagement and satisfaction yield worse business results across several metrics).

190 See, e.g., 1 TAXPAYER ADVOCATE SERV., 2013 ANNUAL REPORT TO CONGRESS xii (2013), available at http://www.taxpayeradvocate.irs.gov/userfiles/file/2013FullReport/Volume-1.pdf (“The classic economic model of compliance—that compliance depends upon the risk (or perception of risk) of being caught and the cost (punishment) if caught—does not fully explain the high compliance rate in our tax system. Research shows that other factors, such as taxpayers’ attitudes about government and their perception that they are being treated fairly by the tax system, also influence taxpayer compliance decisions.”).

191 Kaplow, supra note 21, at 606-07 n.132.

192 Aprill, supra note 23, at 647.

193 Id. Professor Aprill herself proposed a set of “safe harbors” for charitable political activity in a 2005 letter to the IRS. See Letter from Ellen Aprill, Professor of Law, Loyola Law Sch., to Eric Solo-
Although Professor Aprill focuses on charities rather than social welfare groups, the considerations that she (and Professor Kaplow) cite—"the low level of enforcement, the large number of affected parties, and the number of affected parties unlikely to seek legal advice"—are equally implicated in the 501(c)(4) context. In the case of social welfare groups, however, these factors do not counsel for a rules-based regime.

Professor Aprill acknowledges that a low level of enforcement activity actually weighs in favor of standards. However, she notes that recent IRS investigations of prohibited political campaign activities by 501(c)(3) entities “suggest that violations fall into clear and relatively few categories” and proposes that these few categories could be easily addressed by a few bright-line rules. Even if this is true for 501(c)(3) groups (and it is a debatable point), it does not appear to be the case for social welfare groups. Indeed, in the investigation that led to the 2013 TIGTA report, a highly ranked official explained that much of the delay in processing requests for 501(c)(4) status recognition was due to the variety of activities the IRS was being asked to consider.

Professor Aprill’s contention that rules are preferable where there is a high number of affected entities, many of which have limited resources, assumes that (a) most of these entities will have an organizational interest in learning the detailed content of the prohibition, and (b) that a rule would be more cost-effective than a standard. Neither is a safe assumption for social welfare groups. Under Professor Kaplow’s framework, individuals (or, here, entities) only seek to become informed about the content of a law when it provides them with some self-benefit. The facts suggest, however, that despite outcries from a vocal minority, most organizations can understand and comply with the IRS’s political activity restrictions.

For example, in the case of 501(c)(3) organizations, we know from the investigations that the IRS conducted over the decade that far fewer than 1 percent of the roughly one million 501(c)(3) groups were actually investigated for illegal political activity, and only a fraction of those groups were...
found to have violated the law. Thus, it appears that the vast majority of groups find the political activity ban sufficiently clear.

This evidence may well be circumstantial, but it is supported by other indicia. Consider the restriction that 501(c)(3) groups cannot engage in “substantial” amounts of lobbying. As Professor Aprill notes, in response to concerns that the “substantial” standard did not provide charitable groups sufficient certainty as to the amount of permissible lobbying, Congress created the “Section 501(h)” safe harbor. Organizations that elect the “safe harbor” can ascertain with mathematical precision whether their lobbying activities jeopardize their tax-exempt status. Yet fewer than 2 percent of all 501(c)(3) groups have chosen to do so. While this low adoption rate of a fairly straightforward safe harbor could indicate a high number of scofflaws in the charitable community, it more likely demonstrates that a “vague” standard can provide sufficiently clear guidance for the majority of organizations; most people do, in fact, “know it when they see it.” If the uncertainty is at the margins, perhaps that is where it should be.

It is also worth remembering that, for reasons explored above, a complex rule would be required to define political intervention and set the appropriate permissible level of campaign activity. Thus, the real cost savings to an entity that decides it is beneficial to learn about either a complex law or standard would not come in the transmission of content—it is likely to be voluminous either way—but rather in the peace of mind that a group could achieve through a rule as opposed to having to guess how a standard would be applied after the fact. In this regard, there is a certainty advantage to

200 See supra note 164.
201 See generally 2006 PACI REPORT, supra note 70, at 3. While we do not know the percentage of 501(c)(4) organizations that are seeking to toe the political activity line, it is likely that at a minimum the majority of the groups in existence prior to the Citizens United decision in 2010—139,129—were formed for a non-political primary purpose and not in effort to circumvent campaign finance laws. See INTERNAL REVENUE SERV., supra note 81, at 56.
202 Aprill, supra note 23, at 681; see also I.R.C. § 510(c)(3) (2012) (allowing exemption under this subsection, inter alia, only so long as “no substantial part of the activities [of the organization] is carrying on propaganda, or otherwise attempting, to influence legislation”).
203 Aprill, supra note 23, at 681 (“It is difficult to know why such is the case. It may derive from their length or their complexity. . . . If the complexity of the applicable set of rules is discouraging the adoption of the lobbying expenditure election, that reaction cautions against adopting a complex set of rules to define campaign intervention.”).
204 Jacobellis v. Ohio, 378 U.S. 184, 197 (1964) (Stewart, J., concurring) (famously opining, of obscenity, “I know it when I see it”).
205 See, e.g., Lawsky, supra note 159, at 1073.
206 While Professor Aprill considers Professor Weisbach’s arguments about the risks of complexity in the context of tax law, she dismisses them as being concerned with the problematic interaction among various sections of the code when one section is changed, and thus not relevant to the campaign intervention prohibition. Aprill, supra note 23, at 678. However, for Professor Weisbach interaction only emerges as an additional problem when overly complex rules are adopted instead of a standard. For him, the hallmark of complexity—and why it causes the problems described above—is that “the more com-
rules. However, there is an alternative: an anxious 501(c)(3) leader can avoid a potentially costly information-gathering exercise by forming an affiliated 501(c)(4) entity, which can then, if necessary, form a 527 political committee. Social welfare groups can simply form a political committee without the intervening step and campaign to their hearts’ content.

Professor Aprill’s most provocative argument is not Professor Kaplow’s but her own: that rules are preferable to standards where there is a disagreement as to the underlying norm. Where a self-serving bias or disagreement with the underlying legal proposition exists, she posits that there is a heightened value in ex ante guidance because “standards will not accurately constrain behavior.”207 In other words, an “I know it when I see it” approach is not appropriate where beauty (so to speak) is in the eye of the beholder.

This return to background norms and the question of how best to regulate conduct is an important one. Professor Aprill points to several factors that may indicate rules are preferable given certain background parameters, but these are not conclusive.208 For example, while research does show that we have a self-serving bias that makes us more likely to assume that our actions will pass muster,209 we also have a well-documented risk aversion that often compels inaction in the face of uncertainty.210 Similarly, disagreeing with the First Amendment implications of a law is not indicative of a failure to understand the law. On the contrary, the past century of campaign finance litigation suggests that opponents of FECA and its predecessors have been well versed in both rules and standards regulating their conduct.211 As this history shows, disagreement with the underlying norm is likely to lead to challenges regardless of whether the legal command is a rule or standard, which suggests that spending the time and effort to define a rule in advance is not cost effective. As in the case of a low enforcement

plex the law, the more accurately it distinguishes between different individuals or transactions.”

Weisbach, supra note 140, at 867. This is precisely the challenge in implementing the legislative commands on 501(c)(3) organizations. As both Revenue Ruling 2007-41 and Professor Aprill’s proposed “safe harbors” suggest, the scope of regulated conduct is very wide, and the risk of circumvention high. Aprill, supra note 23, at 678. In such situation, Professor Weisbach (and, indeed, Professor Kaplow) would argue that standards are preferable. See generally Weisbach, supra note 140, Kaplow, supra note 21.

207 Aprill, supra note 23, at 676.
208 Id. at 682-83.
210 See, e.g., DANIEL KAHNEMAN, THINKING, FAST AND SLOW 283-84 (1st ed. 2011).
level above, the most a rule governing a contentious social norm can do is provide a safe harbor; it cannot by itself change behavior.212

A focus on background norms also suggests an entirely different set of criteria for the “rules versus standards” debate. While the discussion above sought to weigh relatively objective standards, such as cost and efficiency, another line of inquiry might ask, as an empirical matter, which regime—rules or standards—better incentivizes individuals to adjust their behavior to the desired social and legal norm. Scholars are divided and, it must be said, nuanced in their assessment of this question.213

When it comes to assessing the impact of rules on groups interested in engaging in campaign activity, we do not need to dwell in the realm of theory and hypothesis. Over the past several decades, campaign finance law has been characterized by an increasingly strong reliance on bright-line rules. As demonstrated in the analysis below, rules in campaign finance law have largely served as signposts to those looking for loopholes. We may be able to say even more than that. Recent history suggests that it was the fragility of rules that brought us to the present point. As a consequence of these events, the long-standing IRS standard regulating the permissible level of political activity by social welfare groups has become one of the last remaining barriers to the flow of unrestricted funds into federal elections from undisclosed sources.

III. RULES IN PRACTICE: THE CASE OF CAMPAIGN FINANCE REFORM

As Oliver Wendell Holmes noted in a tax case nearly a century ago, “a page of history is worth a volume of logic.”214 Sufficient data exist in the parallel world of FECA enactments and enforcements to demonstrate the futility of a rules-based legal regime in the case of campaign activity. A brief review of the history of campaign finance reform efforts shows the fallibility of bright-line rules in this area. As more than one commentator has noted, money has flowed like water around rules that seek to create a firewall between legislators and those who would influence them.215

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A. Circumvention and Complexity

In their current form, federal campaign finance laws are complex in their details, but their aim is straightforward. From the words of “sober-minded Elihu Root” long before the 1907 passage of the Tillman Act\(^\text{216}\) to testimony offered in support BCRA in 2002,\(^\text{217}\) lawmakers have expressed a desire to preserve the public’s faith in the federal government by reducing the corruption, or the appearance of corruption, that comes from private interests funneling piles of cash to elected officials or candidates and thereby influencing legislative or regulatory action (or inaction).

Campaign finance laws work through four main levers, the first three of which are designed to inoculate a candidate against the corrupting influence of large donors and/or donations. First, there are strict dollar and source limitations on contributions to candidates, political parties, and “non-super” PACs—committees organized by a candidate or that coordinate their campaign activities directly with a candidate.\(^\text{218}\) Second, the law restricts the ability of candidates, PACs, and parties to solicit anything other than “federal” or “hard” dollars (money subject to amount, source, and disclosure restrictions).\(^\text{219}\) Third, “coordination” of expenditures between these “hard money” entities (which the law presumes to be closest to the candidate) and organizations making so-called “independent expenditures,” which are not subject to the same source and amount restrictions, is prohibited.\(^\text{220}\)

The fourth lever is disclosure. As described above, it is here that “dodger donors” are most effectively exploiting gaps between campaign finance and tax laws. Disclosure was the one area of campaign finance reg-

\(^{216}\) McConnell, 540 U.S. at 115 (quoting United States v. UAW-CIO, 352 U.S. 567, 571 (1957)) (internal quotation marks omitted); Tillman Act of 1907, ch. 420, 34 Stat. 864. Elihu Root was a former U.S. Senator and Cabinet member who advocated for legislation to “prevent the . . . great aggregations of wealth, from using their corporate funds . . . [to elect legislators who would vote] for their protection and the advancement of their interests as against those of the public.” See ELIHU ROOT, ADDRESSES ON GOVERNMENT AND CITIZENSHIP 143 (Robert Bacon & James Brown Scott eds., 1916).


\(^{218}\) See 2 U.S.C. § 441a(a) (2012). In McCutcheon v. FEC, the Supreme Court struck down aggregate limits—a cap on the total amount a donor can give in an election cycle—but did not alter the caps on donations to individual candidates and campaign-related entities. 134 S. Ct. 1440, 1443 (2014).

\(^{219}\) See 2 U.S.C. § 441i(a) (2012).

\(^{220}\) See id. § 441a(d)(4)(C).
ulation that the Supreme Court considered in *Citizens United* and upheld.\(^{221}\) For those subject to FECA’s “hard money” limitations, disclosure is triggered by a contribution or expenditure in excess of $200.\(^{222}\) For those operating “independently” (for example, a 527 Super PAC, 501(c)(4) social welfare group, 501(c)(5) union, or 501(c)(6) trade association), disclosure under FECA is triggered by expenditures on “electioneering communications”\(^{223}\) or “independent expenditures.”\(^{224}\)

To the extent that those who enacted FECA and BCRA hoped to limit the role of money in politics, it has not worked; watchdog groups estimate that more than $6 billion was spent on the 2012 election season.\(^{225}\) According to the Center for Responsive Politics, the average House winner spent $407,556 in 1990 compared to $1.6 million in 2012.\(^{226}\) Moreover, virtually all of the legal commands outlined above are governed by bright-line rules, and all have been carefully circumvented by members and supporters of both major political parties.\(^{227}\) The following sections chart the flow of money around campaign finance rules and describe how campaign finance opponents have successfully manipulated the rules/standards dichotomy to create a legal regime in which the process often seems to undermine the purpose. This history also illustrates how rules can be circumvented by skilled advocates and underscores the importance of calling a standard a standard.


\(^{223}\) Id. § 434(f)(3). As enacted in BCRA, “electioneering communications” are advertisements run within a certain amount of time before an election or primary that show a candidate’s name or likeness. This provision of BCRA was intended to target so-called “issue ads,” which consumed significant amounts of unregulated “soft money” in the years leading up to the law’s passage. Craig Holman & Joan Claybrook, *Outside Groups in the New Campaign Finance Environment: The Meaning of BCRA and the McConnell Decision*, 22 YALE L. & POL’Y REV. 235, 243 (2004). In *Wisconsin Right to Life*, however, the Supreme Court narrowed the definition of electioneering communications to return, in essence, to the previous standard set out in *Buckley v. Valeo*. FEC v. Wis. Right To Life, 551 U.S. 449, 451 (2007) (“[A] court should find that an ad is the functional equivalent of express advocacy only if the ad is susceptible of no reasonable interpretation other than as an appeal to vote for or against a specific candidate.”); Buckley v. Valeo, 424 U.S. 1, 44 (1976) (per curiam); see also infra notes 242–55 and accompanying text. The definition was briefly given new life in the NPRM as a factor in determining whether an organization has engaged in candidate-related political activity, but it remains to be seen whether that language will survive into the final regulation.

\(^{224}\) 2 U.S.C. § 434(f) (2012). Independent expenditures are any communication expressly advocating the election or defeat of a candidate that is funded by a person or group not related to a candidate or political party and not coordinated with the candidate or party. See id. § 431(17).


\(^{227}\) See, e.g., *McConnell v. FEC*, 540 U.S. 93, 126 (2003) (noting that parties and candidates were able to circumvent the FECA by transferring and using soft money).
1. Follow the Money

Following the tributaries of campaign finance regulation, a student of history comes across many rules that were meant to operate as a dam but instead just redirected the flow of money in whatever direction offered the most favorable combination of rules (or lack thereof) governing donor disclosure, permissible purpose, and tax consequences. Former FEC Chairman Trevor Potter notes that during the 1972 elections, gift taxes could be triggered by contributions of more than $3,000. As a result, “Nixon had 220 separate campaign committees for the 1972 presidential election, and on the Democratic side . . . 785 separate committees [were] created just for General Motors heir Stewart Mott.”

Similarly, prior to enactment of BCRA in 2002, state parties were allowed to spend a higher ratio of unregulated “soft” money to “hard” money on activities such as get-out-the-vote efforts, voter registration drives, and “issue advertisements” than national parties, and so transfers from the national parties to state parties skyrocketed. After BCRA eliminated national parties’ ability to raise soft money and restricted the amount of soft money a state party could raise for an election in which a federal official was running, transfers between the national and state parties dropped sharply. Transfers from the Republican national party went from $112 million in 2000 to $56 million in 2004; Democratic transfers fell from $111 million to $72 million in the same cycles. At the same time, reported outside spending, exclusive of party committees, went from $51.6 million to $193.1 million; this figure would top $1 billion in 2012.

More recently, after Citizens United substantially broadened the universe of those who could make independent expenditures, disclosure of outside spending plummeted, from 96.5 percent in 2004 to an estimated 40.8 percent in 2012. Long-overlooked FEC regulations severely limit disclosure requirements when it comes to donors whose contributions are

228 Potter & Morgan, supra note 57, at 414. Political contributions to 527 groups are now excluded from the gift tax. I.R.C. § 2501(a)(4) (2012); see also Oosterhouse, supra note 35, at 265.

229 Potter & Morgan, supra note 57, at 414.


231 See id.

232 Id. Democratic transfers in 2008 rebounded to approximately their 2000 levels, largely because of the national “50 state” strategy set out by Democratic Party Chairman Howard Dean, but Republican transfers fell even lower, to $46 million. Id. at 80-81. The overall amount spent on the 2008 election was roughly $5.3 billion, compared to $3.1 billion in 2000. The Money Behind the Elections, OPENSECRETS.ORG, http://www.opensecrets.org/bigpicture/ (last visited Feb. 5, 2014).


234 See Potter & Morgan, supra note 57, at 384.
intended to fund express “independent expenditures”; only donors who clearly indicate they intend that their funds be used for such advertising must be disclosed. Paradoxically, this narrow disclosure provision (which is far more restrictive than the text of FECA) has incentivized even social welfare groups, who ostensibly do not have campaign intervention as their primary activity, to run “independent expenditures” expressly calling for the election or defeat of a candidate rather than issue-oriented “electioneering communications,” because the FEC and courts are still determining groups’ obligation to disclose the donors behind the latter set of ads.

These examples illustrate many of the issues that were anticipated in the earlier discussion: the problem with rules where there is a tendency for fraud or an emphasis on the form of the transaction, the use of rules to exploit discontinuities and circumvent rather than uphold the underlying legal norm, and the recursively complex and reactive nature of rules when there is a culture of avoidance rather than compliance. Consider too that the original drafters of FECA wrote the law blissfully ignorant of terms such as “issue ad,” “soft money,” or “bundler”—all phenomena developed to avoid seemingly clear legal prohibitions in campaign finance rules.

The result is a legal regime that bears little resemblance to the goal set out by Congress; indeed, some members of Congress have challenged the rules in court and in agency actions for exactly this reason.

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235 See id. at 420-25.
236 See id.
237 See id. at 457; Ctr. for Individual Freedom v. Van Hollen, 694 F.3d 108, 111 (D.C. Cir. 2012) (reversing the lower court’s ruling that every person who funds “electioneering communications” must disclose all contributors to FEC).
238 An issue ad is a broadcast communication that identifies a candidate for office in the weeks leading up to an election but instead of directly exhorting the voter to “vote for” or “vote against” the candidate, it expresses views on a policy issue with which the candidate is associated. See, e.g., FEC v. Wis. Right to Life, Inc., 551 U.S. 449, 451 (2007). These ads allowed campaigns to avoid the spending and donor source restrictions of FECA.
239 “Soft money” refers to money donated to a political party that is not subject to source restrictions and donation limits. Although largely halted now by BCRA, for decades soft money allowed donors to circumvent the source and contribution limits of campaign finance law. See McConnell v. FEC, 540 U.S. 93, 93 (2003).
240 A “bundler” is a donor who seeks out additional donors to convince them to donate up to the hard money limits allowed by FECA. See, e.g., United States v. Hsu, 669 F.3d 112, 115 (2d Cir. 2012) (describing how a wealthy donor convinced his friends to channel their funds to support the election of a political candidate). This allows donors to be credited for bringing in much larger amounts than allowed under FECA.
241 See, e.g., Shays v. FEC, 337 F. Supp. 2d 28, 35 (D.D.C. 2004), aff’d, 414 F.3d 76 (D.C. Cir. 2005); see also supra notes 12 (discussing a 2013 lawsuit challenging the IRS’s political activity regulations) and 57 (discussing 2012 lawsuit challenging FEC regulations limiting disclosure of donors for independent expenditures).
2. “Magic Words” and Manipulation of Rules and Standards

The history of campaign finance reform also reveals something about the continued vitality of the rule/standard dialectic and the importance of defining which approach is intended. Even if we assume that the use of rules to administer FECA has reduced the number of lawsuits from those seeking to apply the law, it has certainly not reduced the number of challenges to the law itself. The technique used by those challengers has exploited not just the discontinuities within the rules, but the discontinuities between rules and standards: where they do not like a rule, they argue that the First Amendment requires a more flexible standard, and where they do not like a standard, they argue that the First Amendment requires a strict rule. Conversely, where they do like a rule, they argue that the court does not have the discretion to change it, and when they do like a standard, they argue that it should be converted into a rule. The net result is an emphasis on rules and a sacrifice of function to form.

Consider, for example, the case of the “magic words.” When FECA was revised in 1974, it limited expenditures made relative “to a clearly identified candidate for Federal office.” Almost immediately, however, this standard was replaced by the rule set out in *Buckley v. Valeo*: expenditures could only be restricted to the extent they went to “communications containing express words of advocacy of election or defeat, such as ‘vote for,’ ‘elect,’ ‘support,’ ‘cast your ballot for,’ ‘Smith for Congress,’ ‘vote against,’ ‘defeat,’ [and] ‘reject.’” The rule created by the Court would direct the course of campaign spending for the next several decades, with most courts treating the rule in the footnote as a “bright-line test.”

242 See, e.g., Citizens United v. FEC, 558 U.S. 310 (2010); Cal. Med. Ass’n v. FEC, 453 U.S. 182, 186 (1981) (challenging the constitutionality of the statutory contribution limitations of the FECA); Mariani v. United States, 212 F.3d 761, 765 (3d Cir. 2000) (challenging the FECA on First Amendment grounds); see also Court Case Alphabetical Index, FED. ELECTION COMM’N, http://www.fec.gov/law/litigation_CCA_Alpha.shtml (last visited Feb. 16, 2014) (providing an alphabetical list of 431 lawsuits in which the FEC is or has been a party).


244 See *Buckley v. Valeo*, 424 U.S. 1, 44 & n.52 (1976) (per curiam); see also id. at 80 (applying express advocacy test to disclosure requirements as well).

245 *Kansans for Life, Inc. v. Gaede*, 38 F. Supp. 2d 928 (D. Kan. 1999). For example, in *Kansans for Life, Inc. v. Gaede*, 38 F. Supp. 2d 928 (D. Kan. 1999), the court was asked to find that the following ad, which ran during a primary election, was express advocacy and should be funded by regulated “hard” money:

Have you ever had someone try to trick you? You know, twist the truth to make you think one thing instead of another? Children are quite good at this. Unfortunately, Governor Bill Graves is trying to do the same thing, telling you he is pro-life when, in fact, he is a strong supporter of legal abortion in Kansas. During his last campaign, Gov. Bill Graves held a rally for his supporters—Dr. George Tiller, the infamous late-term abortionist was in attendance to support Bill Graves. We know Bill Graves props up the abortion industry because we are Kansans For Life—it’s our job to know who is pro-life and who is pro-abortion. Yet there are political ads, which this radio station is required by law to run, by Bill Graves trying to
Once parties and campaigns realized that the rules allowed them to raise unlimited funds from unregulated sources and spend them on any political advertisement so long as it did not contain “express” advocacy, “issue ads” were born. These advertisements, which proliferated in the 1990s and early 2000s, typically ran in the period leading up to an election, mentioned a candidate, and even expressed a point of view on the candidate, but avoided the “magic words.” Along with issue ads, unregulated soft money donations skyrocketed, from 11 percent of national party spending in 1988 to 42 percent in 2000.

To stem the flow of soft money and stop the use of the “magic words” rule to circumvent the purpose of FECA, Congress enacted BCRA in 2002. The law sought to answer rules with rules. It took the national parties out of the soft money game and created a new category of ads subject to expenditure and disclosure limits—“electioneering communications.” These are ads running in certain media for a particular amount of time before an election that include the candidate’s name or likeness. This new rule was meant to better capture the underlying goal of restricting the influence of unregulated and undisclosed funds to influence federal elections, and at first the Supreme Court, taking a functional approach, agreed that it did so.

In its 2007 decision in *FEC v. Wisconsin Right to Life*, however, the Court reversed course and reanimated the magic words test, holding, in an as-applied challenge to BCRA’s ban on the use of corporate or union treasury funds for electioneering communications, that “a court should find that an ad is the functional equivalent of express advocacy only if the ad is susceptible of no reasonable interpretation other than as an appeal to vote for or against a specific candidate.” As *Buckley* had rejected a standard for deceive you. The truth is David Miller, who is challenging Bill Graves for Governor, is pro-life. David Miller has always been pro-life. David Miller will not change or try to fool you just because it is an election. Now you know the truth!

Paid for by Kansans For Life.

Kansas for Life, 38 F. Supp. 2d at 929-30 (internal quotation marks omitted). The court rejected the request, explaining that the “ad at issue in this case contains none of the buzz words or phrases which the Supreme Court or the Kansas Legislature have listed as trademarks of express advocacy.” Id. at 936.

246 See, e.g., supra note 245.


250 See McConnell, 540 U.S. at 193 (“[T]he unmistakable lesson from the record in this litigation, as all three judges on the District Court agreed, is that Buckley’s magic-words requirement is functionally meaningless.”).

251 FEC v. Wis. Right to Life, Inc., 551 U.S. 449, 451 (2007); see also id. at 495 (Scalia, J., concurring) (“If a permissible test short of the magic-words test existed, Buckley would surely have adopted it.”).
what advocates turned into a bright-line rule, Wisconsin Right to Life rejected a bright-line rule for an ostensible standard that functions, commentators noted, as a return to the rule.252

This history is relevant to current discussions about how to best revise IRS guidance for reviewing applications and activities of 501(c)(4) groups. There is an intuitive appeal, in the face of complaints about a vague standard, to proposing an up-front, bright-line rule as a solution. Indeed, this is the title of Public Citizen’s working document recommending changes to “clarify the IRS regulations governing nonprofit organizations’ political activities.”253

Even a casual observer will quickly spot the problem with this approach, however. Public Citizen’s Bright Lines Project proposal runs five pages with fifteen footnotes; the explanation of the proposal runs thirty-three pages and contains thirty-five separate examples.254 It outlines six principles for evaluating an organization’s activities; the last is titled “facts and circumstances.”255 The “bright-line rule” is, in fact, a clarified standard.

Why quibble over terminology? Because sometimes it is important to call a standard a standard, if only to eliminate the risk of gamesmanship that can come with a rule. As shown above, where complexity is given and circumvention the norm, a rule provides opportunities for arbitrage that a standard does not. A rule also can hamstring an adjudicator, particularly where novel issues are arising regularly. The IRS standard does need revision, but its emphasis on “facts and circumstances” should remain.

B. Back to the Beginning: Explaining the IRS “Scandal” as a Failure of Rules

It is easy to read the TIGTA report and news coverage of the resulting congressional hearings and assume that the genesis of the “Tea Party scandal” lay in the fact that the IRS was trying to administer a nebulous stand-

252 Compare Buckley v. Valeo, 424 U.S. 1, 44 (1976) (per curiam) (concluding that the test for express advocacy turns on whether or not the ad uses words such as “election” or “defeat”), with Wisconsin Right to Life, 551 U.S. at 451 (holding that an issue advertisement is not express advocacy because “it may reasonably be interpreted” as something other than an “express advocacy” for a particular candidate).

253 Pub. Citizen, supra note 12, at 1 (italics omitted).

254 See, e.g., id. at 12-15 (enumerating the different applications of the general speech rule that go beyond express advocacy); see also id. at 15-24 (relaying over twenty examples of the proposed safe harbor threshold). Although the rule seeks to limit use of facts and circumstances by indicating an organization can only rely on these considerations in its defense, it is unclear that this would in fact reduce the instances of an adjudicator being asked to weigh the facts and circumstances.

255 See id. at 29-33 (considering, inter alia, timing, range of issues discussed, disclaimers and disclosures, and the history of organization to determine when a group has engaged in improper campaign activity).
ard rather than a clear rule. While there are steps the IRS should take to improve its administration of the political activity limitation—suggestions in this regard are made below—moving from a standard to a rule is not one of them. In fact, it was the failure of a rules-based system that the IRS is not tasked with administering, and the inherent limitations of rules, that led to the problems outlined in the TIGTA report.

The buildup in requests for recognition from 501(c)(4) groups can be traced to three fairly recent developments. The first development demonstrates the difficulty of using rules to enforce legal commands where the background norm is circumvention. In 2000, Congress began requiring disclosure reports from almost all Section 527 political organizations. This rule change was meant to close a loophole in a previous rule: when Section 527 was first enacted in 1974, all political campaign committees were required under the newly reinvigorated FECA to file disclosure reports with the FEC, and so the Internal Revenue Code did not duplicate the requirement. After the Buckley decision and subsequent rulings by the FEC, however, only groups engaged in “express advocacy” were required to file disclosure reports with the FEC. The results were predictable: “[a]dvocates found ample room to design programs to influence election outcomes without express advocacy of any candidate’s election or defeat . . . and [to] conduct those programs free of regulation under any election law, using a 527 political organization.” The 2000 change to the Code eventually closed this loophole, but in doing so it increased the appeal of organizing under Section 501(c)(4), which offered the tax advantage without disclosure requirements.

The second development demonstrates not only the disconnect between rules and the norms they are supposed to capture, but also the fragility of the former. The Supreme Court’s decision in Citizens United struck

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256 TIGTA REPORT, supra note 12, at 8-9; see also IRS Tax-Exempt Investigation: Hearing Before the H. Comm. on Ways & Means, 113th Cong. (2013) (statement of Steve Miller, Acting Comm’r, Internal Revenue Serv.) (admitting that the determination of whether an organization is primarily engaged in social welfare is “intensely fact-specific” and that “[t]here are no bright-line tests for what constitutes political campaign intervention”).

257 I.R.C. § 527(i)(5)-(6) (2012). Section 527 organizations do not have to register with the FEC unless their primary purpose is intervening in a federal campaign. Id. § 527(e)(5). Their obligations to the IRS turn on their status under FECA: if they already are required to register with and report to the FEC as a Super PAC or Federal PAC, 527 groups do not have to file registration documents (Form 8871) or political activity reports (Form 8872) with the IRS. Id. § 527(i)(6). They also do not have to register with the IRS if they reasonably anticipate that their gross receipts will be less than $25,000. Id. § 527(i)(5).

258 See, e.g., 146 CONG. REC. E1149 (June 29, 2000) (statement of Rep. Michael Castle) (advocating for an amendment to Section 527 because of the torrent of political advertising by groups that exploit the tax and campaign finance loopholes).

259 Rosemary E. Fei, The Uses of Section 527 Political Organizations, in 1 STRUCTURING THE INQUIRY INTO ADVOCACY 23, 28 (Elizabeth J. Reid ed., 2000), quoted in Kindell & Reilly, supra note 95, at 461.
down a long-standing rule that prohibited corporations—including many 501(c)(4) groups—from using general treasury funds on campaign spending. The decision marked a major change in bright-line campaign finance rules.261 Previously, these expenditures by corporations had to be funded through PACs, which were subject to strict contribution and disclosure rules.262

Taken together with the Court’s earlier decision in *Wisconsin Right to Life*, which substantially dismantled Congress’s attempt in BCRA to reign in sham “issue ads,” *Citizens United* significantly changed the potential scope of a 501(c)(4) organization’s campaign activity just as 527 groups were becoming less attractive for some. Groups that had been disinclined to organize under 527 because of the new disclosure requirements now had a possible work-around: file as a 501(c)(4) and engage only in the broad set of political activities that does not require public disclosure of individual donors.263 (Although the Supreme Court did, by 8-1, uphold FECA’s disclosure provisions, the Court apparently failed to realize the limitations of these provisions, particularly as applied to 501(c) groups.)264

The impact was immediate. “Outside groups that didn’t make their donors’ names publicly available, together with groups that received a substantial portion of their contributions from such nondisclosing groups accounted for nearly 44 percent of outside spending in the 2010 election cycle.”265 Estimated political spending by 501(c)(4) groups grew from $3.2 million in the 2004 election to $256.3 million in 2012; the latter exceeded

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260 *Citizens United* v. FEC, 558 U.S. 310, 372 (2010). Certain corporations that were strictly issue-oriented and did not accept funds from for-profit organizations were already allowed to run issue ads thanks to the “MCFL” exception. *See supra* note 48.

261 *See Tobin, supra* note 110, at 444 (noting that as a result of *Citizens United*, the use of non-profit organizations as political vehicles is “even more tempting”).

262 *Citizens United*, 558 U.S. at 338.

263 Organizations filing a Form 990 or 990-EZ must report donors on Schedule B; however, this list is not available to the public. I.R.C. § 6104(d)(3)(A) (2012); Treas. Reg. § 301.6104(d)(1) (2000).

264 *Citizens United*, 558 U.S. at 366-70. *See Potter & Morgan, supra* note 57, at 425, 459 (suggesting that the Supreme Court did not understand the FEC’s existing disclosure regulations when it decided *MCFL* and *Citizens United*). This may provide further evidence that rules and complexity do not mix well.

265 *Outside Spending by Disclosure, Excluding Party Committees, supra* note 62.
the $255.4 million spent by the parties themselves. Applications requesting recognition as a social welfare group soared, burdening the IRS.

The third development is gridlock. The FEC, the agency that is supposed to administer and enforce campaign finance laws, has reached a point of political impasse that is singular even in light of its own anemic record. The agency was hobbled from the start by a series of structural impediments, rules that have prevented it from functioning effectively. Four of its six commissioners—no more than three of whom can be from the same political party—must agree before a decision can be issued or enforcement action taken, even if the agency’s own general counsel recommends, for example, sanctions. Its budget is relatively small, and its enforcement powers weak. However, since 2007, the number of deadlocked decisions has dramatically increased. From 2003 to 2007, the agency voted on 2,600 enforcement actions and deadlocked on 1 percent of them. In the four years after that, the agency voted on only 760 enforcement actions and its deadlock rate soared to over 13 percent. Similarly, in 2005, the agency voted on sixty-one audits and deadlocked on one; in 2011, it voted on only twenty and deadlocked on seven. The anemia extends to the appointment


\[271\] See id.

process itself; until two new commissioners were nominated and confirmed in late 2013, the entire panel was serving expired terms. Unfortunately, as one of the new commissioners reported, the new blood has not altered the level of “paralysis.”

The jammed FEC enforcement mechanism has yielded results that would be comical if not for the lasting harm to institutional authority. For example, in 2011, American Crossroads, the Karl Rove-backed Super PAC that poured hundreds of millions of dollars into Republican campaigns in 2012 (much of it raised by its associated 501(c)(4) American Crossroads GPS), wrote to ask the FEC to agree that a set of television ads that were admittedly “fully coordinated” with a candidate were neither “coordinated communications” under the FEC nor an in-kind contribution to the candidate. If the ads were found to be either coordinated expenditures or contributions, they would be subject to “hard money” limitations and could neither be generated from corporate treasury funds nor funded by a Super PAC.) American Crossroads noted that the FEC had already deadlocked on a nearly identical question in a 2009 action brought against a Democratic candidate. Although the letter was so absurd on its face that it was parodied by television satirist Stephen Colbert, the FEC commissioners could not reach an agreement on the request. Americans Crossroads proceeded with apparent impunity.


Ann M. Ravel, How Not to Enforce Campaign Laws, N.Y. TIMES (Apr. 2, 2014), http://nyti.ms/l13bQzf (warning that “[i]f the courts continue to defer to the F.E.C.’s inaction, groups like Crossroads GPS will continue to operate with impunity. Money from anonymous donors will continue to pour into elections. And voters will again be barraged with political advertising from unknown sources, making it difficult for them to make informed decisions. If we continue on this path, we will be betraying the public and putting our democracy in jeopardy”).


Josefiak & Bayes, supra note 211.


See Josefiak & Bayes, supra note 211, at 2 (noting that the Commission did not clearly address the issue).


See, e.g., S.V. Date, Crossroads GPS Redefines ‘Social Welfare’ Political Action, NAT’L PUB. RADIO (Nov. 5, 2012), http://www.npr.org/blogs/itsallpolitics/2012/11/05/164364802/crossroads-gps-
These developments show that the increased use of 501(c) organizations as a way to fund federal campaigns is a consequence of the gaps created by a change in campaign finance rules and the failure of the FEC to enforce the rules that do exist. Campaign finance reform opponents have now turned their attention to converting the standard set out in the IRS regulations for social welfare groups to a rule. Much discussion, for example, has circled around the exact contours of the words “exclusively” and “primarily.” The debate is illustrative of how rules have been wielded in campaign finance debates. In 2013, partially in response to the TIGTA report, the IRS proposed a “safe harbor” that would fast-track recognition of exempt status to any organization that agreed to keep its level of campaign activity below 40 percent. A number of groups refused to agree, arguing that they should be allowed to devote up to 49 percent of their resources to campaign activities.

IV. TOWARDS A MORE ROBUST STANDARD: SUGGESTED REFORMS

Notwithstanding this full-throated defense of “facts-and-circumstances” standards in this area, something needs to change. The bureaucratic failures revealed by the TIGTA report and subsequent congressional investigations are less important to the current inquiry than the cracks the investigation exposed in the underlying regulatory architecture. These cracks resulted from too great a load being placed on too inadequate a foundation. They did not result, despite what some suggest, from improper building methods: a facts-and-circumstances approach to policing the excessive political activity line was, and is, appropriate, and discretion to make appropriate calls at the margin should remain with the IRS as the ultimate adjudicator.

281 While I have focused on the substantive impact of the FEC deadlock, the example also demonstrates the impact of rules on process; rules and standards are only as effective as the agencies that administer them. This in turn raises important questions about the legitimacy of the entities that promulgate laws and enforce them, as well as practical considerations about the comparative efficacy of Congress, the IRS, and the FEC. See, e.g., Oosterhouse, supra note 35, at 291-92. I hope to fully consider these issues in a future article, but for now it suffices to note that given structural impediments constraining both Congress and the FEC, the IRS is likely in the best position to promulgate either rules or standards in this area.


The foundation, on the other hand, is out of date and underdeveloped. As noted above, the most recent guidance from the IRS defining political campaign activity has focused far more on 501(c)(3) charities and churches and 527 political organizations than 510(c)(4) groups.\(^{284}\) Indeed, many of the IRS’s key revenue rulings and private letter rulings related to 501(c)(4) status and political activities date to the 1960s, 1970s, and early 1980s.\(^{285}\)

By contrast, in the 2004, 2006, and 2008 election cycles the IRS undertook an exhaustive review of political activity by 501(c)(3) organizations, and in 2007, it issued a lengthy revenue ruling describing when certain activities amount to political campaign intervention.\(^{286}\) The IRS has since applied this 501(c)(3) revenue ruling to evaluate the activities of 501(c)(4) social welfare organizations, even though the fit is far from perfect.\(^{287}\) Most critically, even if the definition of political campaign intervention provided in Revenue Ruling 2007-41 applies equally in the 501(c)(4) context—and one can make an argument that it should not—the ruling is silent on the question of what is an appropriate level of political activity.\(^{288}\) This is understandable; the question is not relevant to 501(c)(3) organizations because they are completely barred from any intervention. It is less understandable why, in its 2013 Notice of Proposed Rulemaking regarding the political activity of 501(c)(4) groups, the IRS did not propose a definition of “primary”; it merely asked for feedback on the question.\(^{289}\)

The IRS should make several substantive and procedural revisions to its process for approving applications for tax-exempt status from non-501(c)(3) groups. As evidenced by the more than 150,000 comments received by the agency in response to its November 2013 NPRM, this Article is not alone in offering the IRS advice. From its own watchdog arms at TIGTA and the Taxpayer Advocate Service to the very smart lawyers working on the Bright Lines Project, the IRS has a wealth of suggestions to consider.\(^{290}\) My own unique additions to this cornucopia come from observations drawn from the discussion above.

\(^{284}\) Compare, e.g., Rev. Rul. 2007-41, 2007 C.B. 1421 (enumerating prohibited types of advocacy for charities), with Rev. Rul. 81-95, 1981-1 C.B. 332 (discussing the types of advocacy in which social welfare groups can engage).


\(^{287}\) I.R.S. Priv. Let. Rul. 2010-200-21 (May 21, 2010). Interestingly, in its proposed rulemaking the IRS declines to adopt the same test for political campaign intervention for charities and social welfare organizations. See NPRM, supra note 13, at 71,537.

\(^{288}\) See NPRM, supra note 13, at 71,535.

\(^{289}\) Id. at 71,541.

\(^{290}\) Particularly commendable is the National Taxpayer Advocate’s exhortation for Congress to restore funding to the agency, especially resources for agent training, and for the IRS to increase its audit rate for social welfare groups. See, e.g., TAXPAYER ADVOCATE SERV., SPECIAL REPORT TO
First, nuance and standards in fact function best where a certain level of clarity exists. Professor Sarah Lawsky notes that although a certain level of uncertainty appears to discourage potential tax cheats, greater uncertainty does not result in greater compliance with the Internal Revenue Code. The IRS should develop a robust set of guidelines for 501(c)(4) organizations to better describe the line between activity that intervenes in campaigns and activity that does not. The suggestions from the Bright Lines Project, with its six principles and thirty-five examples, and Revenue Ruling 2007-41, which provided twenty-one examples of permitted and prohibited political activities, can both serve as helpful templates.

Second, the IRS should recognize the limits of rules in situations where the ability to enforce is low and the incentive to circumvent is high. At most, rules can provide safe harbors to assure anxious actors, be they social welfare groups or motorists, that they are “legal.” The safe harbor provision of Section 501(h), which specifies the percentage of a charitable organization’s expenditures that can “safely” go to direct and grassroots lobbying, may also be a model, with two significant caveats. As an initial matter, any test that proposes a defined percentage spending cap will be open to circumvention as a rule. Therefore, I would join the voices urging that any safe harbor be set well below the 49 percent some currently propose. I also join with those calling for greater disclosure of donors. For all social welfare groups—especially those that insist that they do not qualify as 527 organizations but eschew a safe harbor—more rigorous disclosure requirements would help discourage abuse of this section of the Internal Revenue Code by those whose true interests are not in the greater social welfare.

In addition, the safe harbor offers an opportunity to recommit to the concept of social welfare as something that promotes a common good. This may mean that a strict percentage test does not accurately reflect the organization’s purpose or impact. Consider, for example, an organization the size of the Gates Foundation, which in 2010 had income of more than $50 bil-
Ten percent of this budget would come close to the total amount spent in the last election cycle. Would this be acceptable?

My last recommendation addresses the lengthy delay in processing some 501(c)(4) applications. It is here that the real scandal lay in the matter. The Taxpayer Advocate recommends providing 501(c)(4) applicants the same opportunity presently offered to 501(c)(3) applicants: an appeal by right after 270 days if a decision has not been reached. A robust appeals process is needed, but the fact that 501(c)(4) groups are not required to apply for status complicates the matter. A penalty should be added if an application has been pending more than 270 days that prevents the IRS from challenging an organization’s tax-exempt status until a decision is reached. This would create an incentive for organizations to register with the IRS (not necessary, but helpful) and for the IRS to act promptly on applications.

CONCLUSION

In recent years, the fissures in the regulatory framework have created opportunities for a form of campaign finance arbitrage in which groups have been able to take advantage of the clear lines set out by the FEC’s rules and the IRS’s lack of resources and agency expertise in administering the campaign activity limitations in order to achieve the results Congress intended to foreclose: namely, the substantial flow of unregulated and undisclosed funds into federal elections. The solution, however, is not more rules. Indeed, it was the fragility of rules that brought us to the present point.

The level of complexity, the risk of circumvention, and the practical limits on enforcement actions in the areas of both taxation and campaign finance counsel for the continued implementation of standards to safeguard the use of social welfare organizations by those working for the social welfare as Congress and the IRS have defined it. Notwithstanding the current rulemaking and views to the contrary, advocates would best use their resources and serve the spirit of campaign finance law and Section 501 if they instead committed themselves to reinvigorating the political activity standard and the agency that administers it.

296 See TIGTA REPORT, supra note 12, at 16 (remarking that some charitable organizations are able to sue for declaratory judgments if the IRS does not approve or deny a request within 270 calendar days).