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Comments on the New York Attorney General's Proposed Regulations Regarding the Contents of Annual Financial Reports Filed with the Attorney General by Certain Nonprofits

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My name is Tara Malloy and I am a Senior Counsel at the Campaign Legal Center, a Washington D.C.–based nonprofit, nonpartisan organization that focuses on strengthening and defending campaign finance and political disclosure laws.

I submit this testimony in support of the New York Attorney General's proposed regulations that would require certain non-profits registered with the Attorney General's Charities Bureau to disclose information about their expenditures relating to New York state and local elections, including the sources of their funding.

The Campaign Legal Center believes that the proposed regulations are constitutional and are crucial to ensuring that voters can make informed decisions in elections and to preventing corruption in the political system. This transparency is also essential because it protects the integrity of the tax laws and deters abuse of federal and state laws granting tax-exempt status. The Legal Center urges adoption of the proposed regulations.

I. The Proposed Regulations Are Constitutional.

In response to every attempt to promote transparency in political spending, opponents of campaign finance laws invariably claim that such political disclosure is unconstitutional. The inevitability of these attacks, however, in no way reflects their merit. For almost a century, the Supreme Court has consistently upheld laws requiring political transparency, and emphasized that "public disclosure of political contributions . . . tend[s] to prevent the corrupt use of money to affect elections."[1]

[1] *Burroughs v. U.S.*, 290 U.S. 534, 548 (1934).

In its seminal case on campaign finance, *Buckley v. Valeo*,[2] the Court recognized an array of governmental interests served by political disclosure. First, "disclosure provides the electorate with information as to where political campaign money comes from and how it is spent by the candidate in order to aid the voters in evaluating those who seek federal office."[3] In addition to this informational interest, the Court also found that "disclosure requirements deter actual corruption and avoid the appearance of corruption by exposing large contributions and expenditures to the light of publicity."[4] Finally, disclosure serves an enforcement purpose: "disclosure requirements are an essential means of gathering the data necessary to detect violations" of the federal campaign finance laws.[5]

More recently, in *Citizens United*,[6] the Supreme Court relied upon *Buckley* to uphold, in an 8-1 opinion, the federal electioneering communications disclosure requirements, which require disclosure from any person or group spending $10,000 or more on television or radio communications that mention a specific federal candidate shortly before a primary or general election.[7] Eight Justices explained that this disclosure served the state's informational interest, by providing that "voters are fully informed about the person or group who is speaking," and ensuring that citizens are "able to evaluate the arguments to which they are being subjected."[8]

The regulations proposed by Attorney General Schneiderman fall squarely within this judicial precedent and are justified by the vital governmental interests recognized in *Buckley* and reiterated in *Citizens United*.

The proposed regulations require certain nonprofit and charitable organizations registered with the Attorney General's to disclose their donors if they spend $10,000 or more in a year on New York election-related communications, including advertisements that expressly advocate for the election or defeat of a candidate, referendum or political party, as well as communications made within 180 days of an election that identify a particular candidate, referendum, or party.[9]

By requiring groups to disclose the sources funding their election-related expenditures, the regulations would serve the government's informational interest by ensuring that individual citizens can make informed choices in the political marketplace. They would serve the

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[2] 424 U.S. 1 (1976).

[3] *Id*. at 66-67 (internal quotations and footnotes omitted).

[4] *Id*. at 67.

[5] *Id*. at 67-68.

[6] 558 U.S. 310, 130 S. Ct. 876 (2010).

[7] 2 U.S.C. § 434(f), 441d.

[8] 130 S. Ct. at 915 (internal quotations and citations omitted).

[9] N.Y. Comp. Codes R. & Regs. tit. 13, §§ 91.6(a)(5), (a)(6), (c) (proposed).

government's anti-corruption interest by exposing whether elected officials are "in the pocket" of moneyed interests and enabling voters to hold them accountable.

Furthermore, in structure, the proposed regulations are analogous to the federal electioneering communications disclosure requirements upheld in *Citizens United*. The federal statute requires a group making more than $10,000 in electioneering communications to either disclose all donors over a certain threshold to the group, or alternatively, to use a segregated fund for their electioneering communications and disclose only the donors to this fund.[10] Similarly, the new disclosure regulations would require a covered organization that makes over $10,000 in election-related communications to either disclose all of the donors of over $100 to the organization, or establish a segregated bank account for its electioneering activities and disclose the donors to this segregated account.[11] Both laws are thus carefully tailored to require the disclosure of donors seeking to influence elections while allowing donors whose funds are not used for election-related expenditures to maintain their privacy.

A. The Proposed Regulations Are Not Overbroad.

Critics of political disclosure may attempt to distinguish the proposed regulations from the electioneering communications disclosure law sustained in *Citizens United* by highlighting that the former cover not only advocacy relating to candidates, but also communications that mention political parties, and constitutional amendments, propositions and referenda.[12] Such critics frequently argue that disclosure is only permissible in connection to communications that "expressly advocate" the election or defeat of a candidate.

But in upholding the federal disclosure requirements applicable to "electioneering communications," the Supreme Court in *Citizens United* specifically rejected the contention that "disclosure requirements must be limited to speech that is the functional equivalent of express advocacy."[13] Indeed, eight Justices noted that the Court had in the past endorsed disclosure laws applicable to issue speech, citing the case *U.S. v. Harriss*,[14] which approved a federal law requiring disclosure of expenditures for lobbying.

Furthermore, the Supreme Court has also spoken approvingly of statutes requiring the disclosure of funds spent to support or defeat ballot measures. In *First Nat'l Bank of Boston v. Bellotti*,[15] the Supreme Court recognized the importance of disclosure in the ballot initiative

[10] 2 U.S.C. § 434(f)(2)(E), (F).

[11] N.Y. Comp. Codes R. & Regs. tit. 13, § 91.6(c)(2) (proposed).

[12] N.Y. Comp. Codes R. & Regs. tit. 13 § 91.6(a)(7) (proposed).

[13] 130 S. Ct. at 915.

[14] 347 U.S. 612, 625 (1954).

[15] 435 U.S. 765 (1978)

context, noting that "identification of the source of [ballot initiative] advertising may be required as a means of disclosure so that the people will be able to evaluate the arguments to which they are being subjected."[16] The Court again recognized this state "informational interest" in *Citizens Against Rent Control v. City of Berkeley*,[17] where it considered a challenge to Berkeley's ordinance limiting contributions to committees formed to support or oppose ballot measures. Although the Court struck down the contribution limit, it based this holding in part on the availability of disclosure regarding these committees, stating that "there is no risk that the Berkeley voters will be in doubt as to the identity of those whose money supports or opposes a given ballot measure since contributors must make their identities known under [a different section] of the ordinance, which requires publication of lists of contributors in advance of the voting."[18]

These precedents provide ample confirmation for the proposition that the proposed regulations are not overbroad simply because they extends beyond express advocacy to cover communications that mention candidates, political parties and ballot referenda.

B. Disclosure Need Not Be Limited to Groups Whose Major Purpose Relates to the Nomination or Election of Candidates.

Opponents of political disclosure also attempt to limit the reach of disclosure laws by arguing that disclosure requirements must be restricted to "major purpose" groups. But the "major purpose" test, insofar as it is relevant to disclosure at all, relates only to the legal requirements imposed on "political committees" (or "PACs") under federal campaign finance law. It has no application to a one-time annual reporting requirement, such as the measure proposed by the Attorney General here.

The Supreme Court first formulated the "major purpose" test in *Buckley* to address the constitutional concern that the federal law definition of "political committee" was vague and overbroad. Federal law defines a "political committee" as a group that "receives contributions" or "makes expenditures" "aggregating in excess of $1,000 during a calendar year."[19] At the time of *Buckley*, "political committees" were subject to contribution limits,[20] and restrictions on

[16] *Id*. at 792, n.32.

[17] 454 U.S. 290 (1981).

[18] *Id.* at 298. *See also Buckley v. Am. Constitutional Law Found*., 525 U.S. 182, 205 (1999) (invalidating several Colorado regulations concerning the state's ballot petition process but upholding the regulation requiring "sponsors of ballot initiatives to disclose who pays petition circulators, and how much" because this requirement informed voters of "the source and amount of money spent by proponents to get a measure on the ballot").

[19] 2 U.S.C. § 431(4)(A).

[20] 2 U.S.C. §§ 441a(a)(1), (a)(2).

corporate and union contributions.[21] Political committees were also subject to comprehensive disclosure and organizational requirements, including that they register with the Federal Election Commission; appoint a treasurer; file regular reports disclosing all receipts and disbursements; maintain records for all disbursements for three years; and follow a formal dissolution process when terminating the committee.[22] In light of the battery of regulations applicable to committees, the *Buckley* Court was concerned that the "political committee" definition would "reach groups engaged purely in issue discussion."[23]

To resolve its concerns, the *Buckley* Court narrowed the definition of "political committee to encompass only "organizations that are under the control of a candidate *or the major purpose of which is the nomination or election of a candidate.*"[24] The major purpose test was thus formulated to correct the specific deficiencies of the federal statute, and in light of the extensive regulations that attended federal political committee status.

Here, by contrast, PAC status is simply not at issue. The proposed regulations do not require a covered group to form a political committee or become a political committee itself. Nor do the proposed regulations impose requirements tantamount to the federal political committee regulatory regime at issue in *Buckley*, which entailed contribution restrictions as well as disclosure and organizational obligations. The proposed regulations simply require covered groups to include a schedule disclosing their contributors along with the annual financial report that they are already required to file under existing New York law.[25]

This one-time annual reporting requirement most closely resembles the federal electioneering communications disclosure requirements upheld in *Citizens United*—requirements that were not limited to "major purpose" groups. Indeed, the electioneering communications disclosure requirements are substantially more burdensome than the proposed regulations because they require a group to file a new report each time it spends more than $10,000 on electioneering communications, potentially obligating the group to file numerous reports in a single election year.[26] In addition, federal law requires a group to include on the face of its electioneering communications a disclaimer listing its name, address and telephone number or

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[21] 2 U.S.C. § 441b(a).

[22] 2 U.S.C. §§ 432, 433, 434(a)(4).

[23] 424 U.S. at 79. In particular, the Court was concerned that the definition of "political committee" was vague to the extent it relied upon the statutory definition of "expenditure." Federal law defined "expenditure" as any spending "for the purpose of influencing any election for Federal office." 2 U.S.C. § 431(9)(A)(i). Because the Court found that this expansive definition of "expenditure" was unconstitutionally vague, it feared that the "political committee" definition which incorporated the term "expenditure," "could raise similar vagueness problems." 424 U.S. at 79.

[24] 424 U.S. at 79 (emphasis added).

[25] *See* N.Y. Comp. Codes R. & Regs. tit. 13 §§ 91.5, 91.7.

[26] 2 U.S.C. § 434(f).

website address.[27] If the federal electioneering communications disclosure requirements can be applied to non-major purpose groups, then so too can the proposed regulations be thus applied.

Furthermore, even if the proposed regulations imposed burdens more closely resembling federal PAC requirements, it is still unlikely that the "major purpose" test would apply. As the First Circuit has noted, "[t]he [Supreme] Court has never applied a 'major purpose' test to a *state*'s regulation of PACs."[28] Following *Citizens United*, most lower courts have found that the "major purpose" test formulated by *Buckley* was meant to cure the defects of a particular federal statute, and is not applicable to a state's regulation of political committees, at least insofar as the state law imposes only disclosure requirements, not contribution restrictions.[29] These lower courts have based that judgment on the recognition that "*Buckley*'s limiting construction was drawn for the statute before it"[30] and in light of the fact that "[w]hen *Buckley* was decided, political committees faced much greater burdens under FECA's 1974 amendments,"[31] than they do under a state PAC disclosure law. Thus, these courts have found that the "major purpose" test is inapplicable to disclosure laws far more extensive than the proposed regulations.

As the authority above demonstrates, the "major purpose" test is not relevant to the simple reporting requirement created by the proposed regulations.

C. The Proposed Regulations Do Not Unconstitutionally Chill Speech.

Finally, campaign finance opponents often fall back on speculative claims that campaign finance laws "chill" the speech of those who fear public disclosure.

But the Supreme Court has already considered and rejected this argument as a general basis for invalidating disclosure requirements. In *Buckley*, the Court acknowledged that "compelled disclosure has the potential for substantially infringing the exercise of First Amendment rights," but found "that there are governmental interests sufficiently important to outweigh the possibility of infringement, particularly when the 'free functioning of our national institutions' is involved."[32] Otherwise expressed, the Supreme Court is well aware of the claim

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[27] *See* 2 U.S.C. § 441d(a)(3).

[28] *Nat'l Org. for Marriage v. McKee*, 649 F.3d 34, 59 (1st Cir. 2011) (emphasis added).

[29] *Ctr. for Individual Freedom v. Madigan*, 697 F.3d 464 (7th Cir. 2012), *petition for reh'g en banc denied* (7th Cir. Nov. 6, 2012); *Nat'l Org. for Marriage v. Roberts*, 753 F. Supp. 2d 1217 (N.D. Fla. 2010), *aff'd per curiam*, No. 11-1493, 2012 WL 1758607 (11th Cir. 2012); *McKee*, 649 F.3d at 59; *Human Life of Washington v. Brumsickle*, 624 F.3d 990 (9th Cir. 2010). *But see New Mexico Youth Organized v. Herrera*, 611 F.3d 669 (10th Cir. 2010).

[30] *Madigan*, 697 F.3d at487-88.

[31] *Id*. at 488.

[32] *Id.* at 66 (quoting *Communist Party v. Subversive Activities Control Bd*., 367 U.S. 1, 97 (1961)).

that disclosure is chilling, but has repeatedly found that the public benefit of transparency offsets any harm.

Furthermore, the proposed regulations incorporate the as-applied exemption from disclosure created by the Supreme Court for groups with a *demonstrated* and *specific* concern about the harassment of their donors. In *Buckley*, the Court held that a group could request an as-applied exemption to a disclosure law if it presented evidence showing "a reasonable probability that the compelled disclosure of [its] contributors' names will subject them to threats, harassment, or reprisals from either Government officials or private parties."[33] As the basis for the exemption, it highlighted the 1958 case, *NAACP v. Alabama ex rel. Patterson*, where an attempt to compel disclosure from the Alabama branch of the NAACP was found unconstitutional in light of the NAACP's "uncontroverted showing that on past occasions revelation of the identity of its rank-and-file members has exposed these members to economic reprisal, loss of employment, threat of physical coercion, and other manifestations of public hostility."[34] In accordance with this guidance, the proposed regulations provide an exemption from public disclosure for those covered organizations that show by clear and convincing evidence that disclosure will cause undue harm, threats or harassment to any person or organization.[35]

But it is important to note that *Buckley* resoundingly rejected the proposition that general allegations of potential harassment would render a campaign disclosure law facially unconstitutional. In the words of the *Buckley* Court, "*NAACP v. Alabama* is inapposite where, as here, any serious infringement on First Amendment rights brought about by the compelled disclosure of contributors is highly speculative."[36] It is thus appropriate that the exemption set forth in the proposed regulations requires "clear and convincing evidence" of potential harassment and does not permit groups to evade disclosure through mere speculation about threats.

The proposed regulations also incorporate further protections for contributors to covered groups who do not fund election-related expenditures and wish to stay out of public view. In a manner similar to the federal electioneering communications disclosure requirements, the regulations allow covered organizations to establish a segregated fund for their electioneering, and to disclose only those contributors who finance this fund.[37] This mechanism enables donors concerned about privacy to take steps to ensure that their identity is not disclosed to the public.

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[33] 424 U.S. at 74.

[34] 357 U.S. 449, 462 (1958).

[35] *See* N.Y. Comp. Codes R. & Regs. tit. 13, § 91.6(h) (proposed).

[36] 424 U.S. at 69-70.

[37] N.Y. Comp. Codes R. & Regs. tit. 13, § 91.6(c)(2) (proposed).

II. The Proposed Regulations Protect the Integrity of the Tax Laws.

In addition to advancing the informational and anti-corruption interests identified in *Buckley*, the proposed regulations also promote an enforcement interest by preventing the abuse of federal and state laws governing tax-exempt status.

Following the *Citizens United* decision, the Campaign Legal Center has been troubled by the manipulation of federal tax law by certain tax-exempt groups active in elections, in particular section 501(c)(4) groups,[38] for the purpose of shielding their donors from disclosure. In particular, we have been concerned that an increasing number of groups that are primarily – or even exclusively – involved in election-related advocacy are claiming 501(c) status as a means to avoid the comprehensive disclosure required of political organizations under section 527 of the Internal Revenue Code (IRC).[39]

The proposed regulations, by requiring donor disclosure from all covered groups spending in New York elections, reduce the incentive for such groups to improperly seek 501(c) status, and eliminate at the state level the anonymity that such status has afforded groups that are active in federal elections.

A. Limitations of Federal Tax Law

Federal tax law permits several types of groups organized under section 501(c) of the IRC to engage in some campaign-related activity[40] provided it is not their "primary activity."[41] These groups include "social welfare organizations" organized under section 501(c)(4), labor organizations organized under section 501(c)(5), and trade associations organized under section 501(c)(6).[42] Although these 501(c) groups are permitted to be engaged in a significant amount of campaign-related advocacy, they are not required to disclose their donors to the public.[43]

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[38] 26 U.S.C. § 501(c)(4).

[39] 26 U.S.C. § 527.

[40] Campaign-related activity is "participation or intervention in political campaigns on behalf of or in opposition to any candidate for public office." *See* Treas. Reg. § 1.501(c)(4)-1(a)(2)(ii) (1990).

[41] *See* Treas. Reg. § 1.501(c)(4)-1(a)(2)(i) (1960); Rev. Rul. 81–95, 1981–1 C.B. 332 ("Although the promotion of social welfare within the meaning of section 501(c)(4)-1 of the regulations does not include political campaign activities, the regulations do not impose a complete ban on such activities for section 501(c)(4) organizations. Thus, an organization may carry on lawful political activities and remain exempt under section 501(c)(4) as long as it is engaged primarily in activities that promote social welfare.").

[42] 26 U.S.C. § 501(c)(4)-(6).

[43] Tax-exempt organizations generally are required to file an IRS Form 990, an annual information return with the IRS. *See* 26 U.S.C. § 6033. Section 501(c)(4), (c)(5), and (c)(6) organizations must report the names and addresses of significant donors, but this information is not publicly disclosed. *See* IRS Form 990, Sched. B, Schedule of Contributors (OMB No. 1545-0047).

By contrast, a group seeking tax-exempt status that wishes to engage primarily in campaign-related spending is required to organize under a different section of the federal tax code, section 527.[44] Section 527 organizations are required to file regular reports to the IRS disclosing all donors of over $200.[45]

The IRS's overly permissive regulations and its lax enforcement of the law has allowed groups in large part devoted to election advocacy to avoid organizing under section 527 and instead to organize under section 501(c)(4) and thereby evade disclosure.

First, although section 501(c)(4) of the IRC establishes tax-exempt status for organizations "operated *exclusively* for the promotion of social welfare,"[46] the IRS has interpreted this language broadly to allow 501(c)(4)s to engage in substantial amounts of non-social welfare activities such as electoral advocacy. Essentially, the IRS has construed the term "exclusively" to mean only that these groups' non-exempt activity may not be their "primary" activity.[47] The Campaign Legal Center believes this "primary activity" standard has no legal basis and invites abuse of the 501(c) tax status.[48]

Second, the IRS thus far has failed to enforce even its permissive "primary activity" standard. The Campaign Legal Center and Democracy 21 have filed complaints with the IRS to challenge improper claims for section 501(c)(4) status from groups across the political spectrum, including Crossroads GPS, founded by Republican Party operative Karl Rove, whose primary purpose is to support Republican candidates; and Priorities USA, formed by former Obama White House officials by all appearances for the sole purpose of supporting President Obama's reelection.[49]

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[44] *See* 26 U.S.C. § 527.

[45] *See id.* § 527(j).

[46] 26 U.S.C. § 501(c)(4) (emphasis added).

[47] *See* Treas. Reg. § 1.501(c)(4)-1(a)(2)(i).

[48] In 2011, the Legal Center and Democracy 21 filed a rulemaking petition with the IRS urging amendment of its regulations to make clear that 501(c)(4) groups may not engage in more than an "insubstantial" amount of campaign-related spending. *See* Petition for Rulemaking On Campaign Activities by Section 501(c)(4) Organizations, *available at* http://www.campaignlegalcenter.org/attachments/IRS_PETITION.FINAL.7-27-2011.pdf.

[49] *See*, *e.g.*, Application for section 501(c)(4) status by American Tradition Partnership (Jan. 16, 2013), *available at* http://www.campaignlegalcenter.org/images/IRS_LETTER_WESTERN_TRADITION_PARTNERSHIP_1-16-13.pdf; Request for IRS investigation into whether certain organizations are ineligible for tax exempt status under section 501(c)(4) (Sept. 28, 2011), *available at* http://www.campaignlegalcenter.org/attachments/Letter_to_the_IRS_from_Democracy_21_and_Campaign_Legal_Center_9_28_2011.pdf; Request for IRS investigation to determine whether "Crossroads GPS" is operating in violation of tax status (Oct. 5, 2010), *available at* http://www.campaignlegalcenter.org/attachments/IRS_Crossroads_GPS_Letter_10-5-10.pdf.

Because of overly permissive IRS regulations and the agency's unwillingness to enforce the law, an increasingly large share of the electioneering activity at the federal level is now conducted through 501(c) groups that provide no disclosure, instead of the proper vehicle for campaign advocacy, namely transparent 527 organizations. Over $300 million in secret contributions was laundered into the 2012 elections through section 501(c) organizations, according to the Center for Responsive Politics.[50] The Legal Center expects this trend to only worsen in future election cycles absent changes in the law or increased enforcement efforts by the IRS.

B. Effect of the Proposed Regulations

The proposed regulations, by requiring donor disclosure from 501(c) groups active in New York elections, would serve as a check on these problems in federal tax law – or at least would avoid importing the problems into New York.

Under New York law, the exemption for non-profit organizations from state tax is in some circumstances based on the organizations' federal tax-exempt status.[51] Thus, absent the proposed regulations, New York in some circumstances would be granting tax-exempt status to non-profit organizations that were abusing federal tax law. Furthermore, because federal law does not reliably provide information about the funding of non-profit organizations spending in elections, absent the regulations, New York would be granting charitable and tax-exempt status to groups that provided no information to New York citizens about their efforts to influence state elections.

The proposed regulations, however, would serve the state's enforcement interests by ensuring that New York is not granting a state tax subsidy to groups that are exploiting federal tax law to avoid disclosing the donors funding their electoral spending. Section 501(c) groups that wish to keep their donor lists secret will have to refrain from making expenditures in state elections. And if groups do choose to comply with the regulations, then the information they disclose will enable the public to confirm the nature and scope of the group's electoral activities and to ascertain whether it is complying with federal and state tax laws.

Adoption of the proposed regulations thus not only safeguards the integrity of elections, but also guards against the grant of a state tax exemption to groups that are undermining federal tax law and the public's right to meaningful disclosure of election-related spending.

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[50] *See* Outside Spending, By Group *at* http://www.opensecrets.org/outsidespending/summ.php?cycle=2012&disp=O&type=P&chrt=D (last visited Feb. 15, 2013).

[51] *See* N.Y. Comp. Codes R. & Regs. tit. 20, § 1-3.4(b); N.Y. Comp. Codes R. & Regs. tit. 13 § 90.2(a)(3), (4).