

March 3, 2016

John Koskinen
Commissioner
Internal Revenue Service
1111 Constitution Avenue NW
Washington, DC 20224

Re: IRS decision to grant recognition to Crossroads GPS as a social welfare organization under section 501(c)(4).

Dear Commissioner Koskinen:

The Internal Revenue Service, without public explanation, has granted recognition to Crossroads GPS as a “social welfare” organization under section 501(c)(4) of the Internal Revenue Code. This recognition came in the form of a two-page form letter to Crossroads GPS dated November 4, 2015, but that was not disclosed to the public until recently, when the Center for Responsive Politics obtained, analyzed and released the documents in this case.

The IRS Exempt Organizations staff reached a decision in 2013 to deny social welfare status to Crossroads GPS because, the staff found, Crossroads GPS had engaged in campaign activities that constituted 54 percent of its spending in an earlier year. This level of campaign-related spending exceeded the 49 percent rule that you have often stated sets the limit of campaign activities that a section 501(c)(4) organization is permitted to undertake.

Without explanation, an IRS appeals officer reversed the staff ruling and has granted recognition to Crossroads GPS as an exempt social welfare organization. This decision, made without any explanation after the Exempt Organization staff had concluded that Crossroads GPS should not receive section 501(c)(4) tax status, is inexplicable and indefensible. It represents a fundamental failure by the IRS to rationally and properly administer the tax laws.

As you know, the question of whether Crossroads GPS qualifies as a social welfare organization under the tax laws has been a contentious public matter because it goes directly to the use of undisclosed “dark money” contributions in federal elections. Since the Supreme Court’s 2010 decision in the *Citizens United* case, section 501(c) non-profit groups have spent more than \$500 million in secret contributions to influence federal elections.

Since its founding in 2010, Crossroads GPS itself has reported to the Federal Election Commission spending more than \$100 million on campaign activities. But it has not disclosed the sources of the funds it has used for this spending.

Federal tax law does not require section 501(c)(4) social welfare organizations to publicly disclose their donors—unlike political organizations under section 527, which do have such disclosure obligations. The IRS recognition of Crossroads GPS as a social welfare organization means that the group can continue to hide from public scrutiny the identity of the donors who are financing their expenditures to influence federal campaigns.

More broadly, the grant of social welfare tax status to Crossroads GPS signals to the public that the IRS has abandoned any meaningful effort to enforce the provisions of the tax code that limit the amount of campaign activities that can be engaged in by social welfare groups.

As *The Washington Post* said in a recent editorial (February 19, 2016), the agency’s decision on Crossroads GPS sends the message that the IRS “has thrown in the towel” with regard to policing the misuse of social welfare organizations as vehicles for laundering undisclosed dark money into federal elections.

The same point was noted in a recent article about the Crossroads GPS decision in *Tax Notes*: “If perception is reality, the new reality for nonprofit ‘social welfare’ organizations is that they can emphasize politics as much as they want and not worry in the slightest about losing their tax exemptions.” P. Barton, “No Stopping Political Nonprofits Now, Some Say,” *Tax Notes* (Feb. 25, 2016).

The IRS decision is very likely to have ramifications that will be severely detrimental to the interests of the American people. The use of social welfare organizations to spend undisclosed money in federal elections is now likely to proliferate in light of the agency’s unexplained decision to acquiesce to Crossroads GPS’s claim that it is entitled to tax status as a social welfare organization, notwithstanding its extensive campaign activities. The IRS’s abdication of its responsibility to enforce the law will be responsible for further erosion of the right of citizens to know the identity of the big donors providing money to influence their votes, thereby undermining a bedrock principle of our democracy.

The law says that a social welfare organization must be operated “exclusively” for the promotion of social welfare. 26 U.S.C. § 501(c)(4). The IRS has long recognized that the “promotion of social welfare” does not include “direct or indirect participation or intervention in political campaigns on behalf of or in opposition to any candidate for public office.” Treas. Reg. § 1.501(c)(4)-1(a)(2)(ii).

Given these two propositions of law as the starting point, the decision in this case should have been simple. Because Crossroads GPS has reported to the FEC spending an overall total of more than \$100 million on campaign activity, it is not “exclusively” devoted to social welfare, and should have been denied recognition as a social welfare organization.

However, as we have pointed out in earlier letters to the agency on this matter, the IRS has previously misinterpreted the law by creating, without statutory authority, a “primarily engaged” gloss on the “operated exclusively” language in the statute. The IRS has compounded this error by informally interpreting this regulatory gloss to mean that a social welfare organization can devote up to 49 percent of its spending on political activities and still qualify for non-profit status under section 501(c)(4).

Even in applying this legally erroneous standard, however, the Exempt Organizations staff on its initial review of the Crossroads GPS application still reached a proposed determination to deny social welfare status because it found that a majority of the activities of Crossroads GPS involved political intervention.

In a 15-page, single-spaced proposed adverse determination letter dated September 6, 2013, IRS staff carefully analyzed the spending and political activities of Crossroads GPS and concluded that “you are not operated exclusively for the promotion of social welfare within the meaning of § 501(c)(4) and the regulations thereunder.” Proposed Determination Letter at 12. The letter continued:

Television advertisements accounted for the majority of your Fiscal Year expenditures. All but one of your Fiscal Year television advertisements aired during the 11 weeks before the [2010] general election, identified a candidate for public office, and expressed approval or disapproval of that candidate. You aired all of these pre-election TV ads in targeted areas where the candidate mentioned in the advertisement was running for public office. . . .

Thus, we conclude that all of your pre-election TV ads, and all but one of your Fiscal Year television advertisements, constituted political campaign intervention and did not promote social welfare. The pre-election TV ads accounted for a majority (51.5%) of your [\$40,365,792] in total Fiscal Year expenditures. . . .

Id. at 12. The IRS staff also found that an additional 2.5 percent of Crossroads GPS’s spending in the same year was for direct mail and phone calls that were “also communications that targeted voters, during the period leading up to the [2010] general election, which expressed approval or disapproval of specific, identified candidates for public office” and therefore “also constituted political campaign intervention and did not promote social welfare.” *Id.* at 13.

Thus, the IRS staff found that a total of 54 percent of Crossroads GPS expenditures during the period were campaign expenditures.

Crossroads GPS appealed the proposed adverse determination, protesting that it “was replete with factual, legal and procedural errors. . . .” (September 22, 2015 email). The appeal was eventually heard and decided by the IRS Appeals Office in Fresno, California. The administrative appeals process extended over more than a year, and was apparently conducted with great informality. The record, as made public, reflects a flow of telephone calls and emails from counsel for Crossroads GPS to Theron C. Wing, the IRS appeals officer hearing the case. Crossroads GPS raised a multitude of legal and factual issues in its appeal. But at the heart of the

case was the question of whether the advertisements run by Crossroads should be treated as political campaign intervention or not, under IRS standards.

For instance, one ad in question was run by Crossroads GPS on August 17, 2010, in Colorado and referred to Senator Michael Bennet, who was a candidate for re-election that year. The audio of the ad said:

Michael Bennet's spending spree. Since his appointment, Bennet has voted to spend \$2.5 billion every single day. Spending billions of your tax dollars on everything—from the failed stimulus, billions in government pork, even cash-for-clunkers. And to pay for some of it, Bennet voted twice in 35 days to increase the national debt. Bennet's way? Spend more, borrow more, and then raise our taxes. Michael Bennet's spending spree. Call Senator Bennet. Stop the spending.¹

In its appeal papers, Crossroads GPS contended that this ad had been “misclassified” by the Exempt Organization staff as campaign intervention. It said that this advertisement (and similar ones) were “issue” ads. This ad, it said, was intended to urge Senator Bennet to vote “no” on Senate Amendment 4594, “which would have increased the Fiscal Year 2011 deficit by \$85.38 billion and would have caused a net increase in the deficit over the next decade.” Crossroad GPS Protest (Nov. 8, 2013) at 50. According to Crossroads, at the time the advertisement aired, Senate Amendment 4594 was scheduled for a vote on the Senate floor on September 14, 2010. Crossroads pointed out that the advertisement closed with an on-screen message: “Tell Senator Bennet/Stop the Spending/Vote No on S. Amdt. 4594/Call: (866) 455-9866.” *Id.* at 49.

In discussing the advertisements run by Crossroads GPS, the Exempt Organization staff in its Proposed Adverse Determination said:

You identified nearly two-thirds of your pre-election TV ads as independent expenditures reported to the FEC. Of the remaining one-third of pre-election TV ads, a few contained text at the end of the advertisement that listed a bill number, and a vote on that bill was scheduled close to the time the advertisements were aired. However, these advertisements focused primarily on criticizing the identified candidate and provided no information about the legislation other than the bill number, which was provided as text (but not audio) at the very end of the advertisement. . . . Accordingly, the facts and circumstances indicate that these advertisements were political campaign intervention and did not promote social welfare. . . .

Proposed Adverse Determination at 12 (emphasis added). In its appeal, Crossroads GPS contested this characterization.

The record suggests that Mr. Wing had a surprising lack of familiarity with the applicable law relating to the tests for social welfare status and political intervention. At one point, Mr.

¹ See Letter of October 5, 2010 from Democracy 21 and Campaign Legal Center to Commissioner Douglas H. Shulman, at 7.

Wing apparently suggested to counsel for Crossroads GPS that social welfare communications “must have an element of education and/or logical discussion,” a test nowhere found in prior IRS rulings. Counsel for Crossroads GPS sought to disabuse Mr. Wing of this view, arguing that a social welfare group could “do nothing but distribute seven-word bumper stickers wholly devoid of educational or logical content and maintain its tax-exempt status.” (Emails of August 27 and September 30, 2015).

At another point, Mr. Wing in a telephone conversation with counsel for Crossroads apparently described a novel methodology he was devising to determine if the television ads in contention did or did not meet the test for political intervention. As described by Crossroads counsel, Mr. Wing was “construct[ing] a chart” with “eighteen boxes” that reflected various factors set forth in earlier IRS rulings on political intervention. Counsel further described Mr. Wing’s proposed methodology:

You then reviewed each TV ad and placed either a “Yes” or a “No” in each box; “Yes” meaning that the factor implies that the TV ad is political and “No” meaning that the factor implies that the TV ad is social welfare. You told me that because the two rulings do not weigh the factors, you assigned equal weight to each factor.

Then you counted. If there were more “Yesses” than “Noes,” you deemed the TV ad political. If there were more “Noes” than “Yesses,” you deemed the TV ad social welfare. As you said to me, “This made it easy.”

(Email of August 17, 2015). Counsel for Crossroads GPS argued that this methodology was both unprecedented and flawed. *Id.*

Ultimately, the Appeals Office made a decision to reverse the adverse determination that had been made by the Exempt Organizations staff, and to grant recognition to Crossroads GPS as a section 501(c)(4) social welfare organization. There is no explanation whatsoever in the record as to the basis for this decision to reverse the staff determination.

Instead, the decision was formalized by only a two-page form letter to Crossroads GPS dated November 4, 2015. Mr. Wing informed counsel for Crossroads GPS of the favorable decision in advance. (Email of October 26, 2015). Counsel for Crossroads thanked Mr. Wing for the advance notice and remarked that “the hard work and hard thinking that you put into this case is greatly appreciated.” (Email of October 26, 2015). Mr. Wing responded to Crossroads counsel that “it was truly a pleasure to work with you” and concluded his email with a smiley-face emoticon. (Email of October 26, 2015).

As pleasant as this process may have been for the participants, it is utterly unsatisfactory from the point of view of the American people. Among other apparent flaws, the record does not reflect that anyone in the IRS was given the opportunity to defend the staff’s proposed adverse determination against the barrage of attacks on it by counsel for Crossroads GPS. The arguments made to Mr. Wing by counsel for Crossroads GPS appear to have been entirely un rebutted. Given Mr. Wing’s own apparent unfamiliarity with the relevant background law, counsel for

Crossroads GPS was able to present an essentially one-sided argument, with no contrary view to challenge his assertions, and then to lobby Mr. Wing in a series of private telephone calls and emails.

The record provided by the IRS does not reflect that anyone other than Mr. Wing was involved in making the decision to grant the appeal by Crossroads GPS. Indeed, in an email to Mr. Wing, counsel for Crossroads GPS said that “you stated and repeatedly confirmed that you – and no one else – would be the decision maker. . . .” (Email of September 22, 2015).

But according to the same email, which was written about a month before the final decision on the appeal, Mr. Wing made comments that “cast severe doubts on my understanding of what the procedure would be” by stating that, “contrary to my earlier understanding, you might not be the ultimate decision maker and that your ‘Manager’ might choose to overrule whatever you decided.” *Id.* Counsel for Crossroads GPS complained that he was left “a bit concerned and confused” by this (and other procedural issues). There is, however, no indication in the public documents released on this matter that anyone other than Mr. Wing was substantively involved in making the decision on this appeal.

Even more troubling is the complete lack of explanation as to the basis for the final IRS determination to grant social welfare status to Crossroad GPS. Mr. Wing may have accepted the erroneous Crossroads position that particular ads identified by the staff as constituting political intervention—such as the Bennet ad, above—were instead just “issue” ads, as Crossroads GPS contended. If so, there is no explanation for why Mr. Wing accepted this proposition as opposed to the staff position. Or Mr. Wing may have accepted the Crossroads argument that the IRS test for political campaign intervention set forth in prior revenue rulings is unconstitutionally vague and cannot be used. If so, there is again no explanation for why he accepted this argument and, if he did, what test he applied instead.

It also appears that it was procedurally easier for Mr. Wing to make a decision in favor of Crossroads GPS than against. As counsel for Crossroads GPS explained in an email to Mr. Wing following a telephone conversation with him:

[Y]ou indicated that if you reached an adverse conclusion, that conclusion would be explained in a detailed written adverse determination letter. . . . Indeed, I even discussed with you about how a favorable ruling would require you to write only a single sentence, while an unfavorable ruling would require a lengthy explanation that would be compelled to deal with the errors contained in the Proposed Adverse Letter that GPS has identified in written submissions.

(Email of Sept. 22, 2015). Ultimately, the appeal was decided exactly this way—by sending Crossroads GPS a two-page form letter with a favorable decision granting recognition as a social welfare organization, but with no explanation for the basis of the decision, or for why the IRS Exempt Organizations staff was being overruled in reaching the decision.

The fact that there has been no explanation, and no rationale, offered for the decision to reverse the Exempt Organizations staff and recognize an exemption for Crossroads GPS does a

grave disservice to the American public. This unexplained and wrongful ruling leaves the law in chaos, and the IRS's ability to properly administer the law crippled.

Given the high public stakes involved—whether purported social welfare organizations can misuse the tax laws to inject hundreds of millions of dollars of secret contributions into federal elections—the agency has an obligation to the American people to do its job responsibly.

This has not occurred in the Crossroads GPS case. The agency owes the public an explanation for its otherwise inexplicable decision to treat Crossroads GPS as a social welfare organization, summarily reversing without explanation a staff opinion to the contrary.

Step by step over the years, the IRS has progressively eroded the congressional mandate that social welfare organizations must be operated “exclusively” for social welfare purposes, which do not include any activities to influence elections.

With this latest ruling, the IRS appears to have abandoned this statutory requirement altogether. This has resulted in the IRS issuing what amounts to a blanket invitation to section 501(c)(4) groups to violate the tax laws with impunity, and thereby acquiescing to the unfettered spending of secret money in federal elections by social welfare organizations.

The country deserves better from the IRS.

Sincerely,

/s/ J. Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21