October 5, 2010

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

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

Re: <u>Request for IRS investigation to determine whether "Crossroads GPS" is</u> <u>operating in violation of tax status</u>

Dear Commissioner Shulman and Director Lerner:

Democracy 21 and the Campaign Legal Center call on the IRS to conduct an investigation into whether Crossroads GPS, a tax exempt group organized under section 501(c)(4) of the Internal Revenue Code, 26 U.S.C. § 501(c)(4), is operating in violation of its tax status because it has a primary purpose of participating in political campaigns in support of, or in opposition to, candidates for public office.

We urge the IRS to conduct its investigation and make its determination about whether the tax laws are being violated as expeditiously as possible, consistent with IRS procedures.

The status of Crossroads GPS as a section 501(c)(4) entity allows its donors to evade the public disclosure requirements that would apply if the organization was registered as a section 527 political organization. Section 527 groups are organizations that are "primarily organized and operated" to engage in political activities. By contrast, Section 501(c)(4) organizations are not permitted to be "primarily engaged" in activities to influence elections. They are not required to disclose their donors.

If, in fact, Crossroads GPS is impermissibly operating as a section 501(c)(4) organization in order to conceal its donors from the American people, the IRS has an obligation to take steps to protect the integrity of our tax laws and to make clear that such abuses will not be permitted in future elections.

Absent timely and appropriate action by the IRS, such abuses will become common place in the 2012 presidential and congressional races, at the expense of the credibility of the tax laws and of the right of the American people to know the identity of the donors who are providing the money to influence their votes and the amounts they are giving.

The IRS applies a "facts and circumstances" test to determine whether a group like Crossroads GPS is in compliance with the requirements of its tax status under section 501(c)(4).

The known facts and circumstances surrounding the creation, operations and activities of Crossroads GPS in 2010 strongly warrant an IRS investigation to determine whether it is in violation of its tax status.

According to published reports, Crossroads GPS is the brainchild of leading Republican Party political operatives and is operated by former Republican Party operatives. Published reports indicate that Crossroads GPS was formed in order to support Republican candidates in the 2010 congressional races and that it is engaged primarily, if not exclusively, in activities to promote and support Republican candidates and to oppose and attack Democratic candidates in the 2010 congressional elections.

Under applicable IRS standards, there is no requirement that an organization's activities and communications contain express advocacy or the functional equivalent of express advocacy in order to determine that the organization is engaged in "direct or indirect participation or intervention in political campaigns on behalf of or in opposition to any candidate for public office."

If, in fact, Crossroads GPS is primarily engaged in political campaign activity under applicable IRS standards, it does not qualify for section 501(c)(4) status. By cloaking itself in the status of a section 501(c)(4) social welfare organization, Crossroads GPS is avoiding the public disclosure obligations that the law imposes on nonprofit entities organized and operated primarily for the purpose of influencing elections.

The New York Times recently quoted Marcus S. Owens, former head of the IRS division that oversees section 501(c)(4) groups, as saying with regard to the new 501(c)(4)s being formed this year:

"These groups are popping up like mushrooms after a rain right now, and many of them will be out of business by late November," Mr. Owens said. "Technically, they would have until January, 2012 at the earliest to file anything with the I.R.S. It's a farce."¹

This "farce" harms both the American people's right to transparency regarding the financing of federal elections, and the integrity and credibility of the nation's tax law.

Past experience shows that such groups often organize during an election year and claim tax status under section 501(c)(4). During the election year, the groups raise huge amounts in unlimited contributions from corporations, wealthy individuals and labor unions that are spent on

¹ M. Luo and S. Strom, "Donors' Names Kept Secret as They Influence the Midterms," *The New York Times* (Sept. 21, 2010).

election activities, with no disclosure of the names of their donors and the amounts they gave. Thus, under cover of their section 501(c)(4) tax status, these groups spend millions or tens of millions of dollars on ads to influence the election, while at the same time hiding from the public information about the sources of the funds being used for these expenditures.

After the election, such 501(c)(4) groups either disband, lay dormant or shift to other activities. This practice is contrary to the letter, spirit and intent of the tax laws, which requires non-profit entities "organized and operated primarily" for election-influencing activities to operate as a 527 group and, thereby, to be subject to a comprehensive public disclosure regime. 26 U.S.C. § 527(j).

The IRS needs to determine whether Crossroads GPS has violated its section 501(c)(4) status by failing to comply with the requirements applicable to such groups, and whether the organization should instead be registered as a section 527 political organization subject to disclosure of its donations and disbursements, or whether it should be treated as a for-profit entity subject to the tax laws that apply to for-profit corporations.

More generally, the IRS needs to address the problem of whether section 501(c)(4) groups are being improperly used as vehicles for groups to spend money to influence federal elections while hiding the identities of the funders of these activities. This matter must be resolved on a timely basis because it will have a direct bearing on whether continuing widespread abuse of the tax laws will allow secret contributions to influence the 2012 elections.

The IRS has a responsibility and obligation to the public to protect the integrity and credibility of the nation's tax laws. It is the job of the IRS to ensure that the nation's tax laws are not being improperly used by political operatives and political activists to hide campaign finance information which citizens and voters have a right to know, as the Supreme Court affirmed in its decision in *Citizens United v.* FEC, 130 S.Ct. 876 (2010).

I. Crossroads GPS

Crossroads GPS was organized in July, 2010 as a "non-profit social action organization" under section 501(c)(4) of the IRC. ("GPS" stands for "Grassroots Policy Strategies.")

Crossroads GPS is affiliated with American Crossroads, a non-profit political organization registered under section 527 of the IRC. American Crossroads is registered with the Federal Election Commission as a political committee under the Federal Election Campaign Act. As such, the major purpose of American Crossroads is to raise and spend money to influence federal campaigns. As a registered political committee, American Crossroads must report all of its contributions and expenditures to the FEC under federal campaign finance laws.

According to a report in *Time*, "American Crossroads was the brainchild of a group of top Republican insiders, including two of George W. Bush's closest White House political advisers, Karl Rove and Ed Gillespie, both of whom remain informal advisers."² Another published

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M. Crowley, "The New GOP Money Stampede," Time (Sept. 16, 2010).

report referred to American Crossroads and Crossroads GPS as "a political outfit conceived by Republican operatives Karl Rove and Ed Gillespie."³ According to the *Los Angeles Times*, both groups "receive advice and fundraising support from Rove."⁴

American Crossroads and Crossroads GPS are, in turn, part of a larger network of Republican-groups that are working together to influence the 2010 congressional elections. According to one published report, four separate groups, including American Crossroads and Crossroads GPS "are collectively planning to spend at least \$70 million to help Republicans win back control of Congress this November."⁵

According to this report:

While dozens of former GOP lawmakers and seasoned Republican strategists are involved, the effort largely springs from the work of two former Bush aides: Ed Gillespie, the former Republican National Committee chairman who later served as White House counselor, and Karl Rove, the man Bush once described as the "architect" of his presidency.

Id. The article notes that "[a]ll of the organizations were founded separately and organized as individual groups. But each is working closely in concert – they share the same office space with the New York Ave. building. . . . They identify each other as 'sister' groups, even though officials involved in the effort are cagey about exactly how closely they are coordinating their efforts and message." *Id.*

According to one published report, the organizers of American Crossroads and Crossroads GPS intend "to raise a combined total of 'approximately \$50 million' to attack Democrats and boost Republicans heading into the 2010 midterm elections." ⁶

According to another published report, "Mike Duncan, chairman of American Crossroads, told *The Washington Times* that his group and [American] Crossroads Grassroots Policy Strategies (sic) plan to plow more than \$49 million of it into 11 Senate races in anticipation that the Republican Party is within reach of a Senate majority."⁷

⁶ K. Vogel, *supra*.

⁷ R. Hallow, "Pro-GOP Nonprofits Kick in Millions; Cash to target 11 Senate races," *The Washington Times* (Aug. 19, 2010).

³ K. Vogel, "Rove-tied group raises \$2 million," *Politico* (Aug. 21, 2010).

⁴ M. Reston and A. York, "Karl Rove-linked group launches new hit against Boxer," *The Los Angeles Times* (Aug. 25, 2010).

⁵ H. Bailey, "A guide to the 'shadow GOP': the groups that may defined the 2010 and 2012 elections," *Yahoo News* (Aug. 5, 2010).

We note that former RNC Chairman Duncan is not quoted as saying the two groups plan to spend more than \$49 million to promote lower taxes or reduced government spending, but rather to plow into 11 Senate races.

American Crossroads, functioning as a 527 political organization and registered as a federal political committee, is running broadcast ads that promote Republican candidates or attack Democratic candidates. According to a press report, for example, American Crossroads in late August, 2010 began running ads in Nevada and Missouri that "are designed to defeat Senate Majority Leader Harry Reid in Nevada and Democratic Senate candidate Robin Carnahan in Missouri. American Crossroads has already spent some \$600,000 on ads in Nevada attacking Reid on different issues."⁸ According to this same press report:

The group will be stepping up its ad spending in other states this month to boost GOP Senate candidates, [spokesman Steven] Law said, and it expects to begin running ads to help a dozen or two House candidates in September. In coming weeks American Crossroads will also finalize plans for an ambitious get-out-the-vote effort aimed at bringing Republicans and conservative-leaning independents to the polls in November.

Id.

Just as American Crossroads is spending large sums for campaign ads to influence the 2010 congressional elections, so also is Crossroads GPS, its 501(c)(4) affiliate. According to a story in USA Today published on August 25, 2010:

Crossroads GPS, a Republican nonprofit group that does not have to publicly disclose its donors, has pumped more than \$2 million into another round of TV ads targeting Democrats.

This brings to roughly \$5 million the amount Crossroads GPS and an affiliated organization, American Crossroads, announced spending in the last week alone to influence November's midterm elections.

This round of spending goes after Sen. Barbara Boxer of California; Rep. Joe Sestak, running for the Senate in Pennsylvania and Jack Conway, the party's Senate nominee in Kentucky.⁹

One published report describes a "concept paper" distributed to potential donors prior to the formation of Crossroads GPS as stating that Crossroads GPS intends "to deploy advertising and other issue information in August/September in key markets," right before the 2010

⁸ P. Stone, "American Crossroads Spin-off Launches New Ads in Missouri, Nevada," *The Center for Public Integrity* (Aug. 20, 2010).

⁹ F. Schouten, "Karl Rove-affiliated nonprofit unleashes more ads in three races," *USA Today* (Aug. 25, 2010).

congressional elections. *Id.* According to this concept paper, a "micro-targeting effort" also to be conducted by the group "is focused on seven states – Colorado, Florida, Missouri, New Hampshire, Nevada, Ohio and Washington," all states that have key contested Senate races in 2010.¹⁰

The ads themselves that have been run by Crossroads GPS leave little doubt that they are intended to influence the 2010 congressional elections and will have the effect of doing so. The organization is sponsoring ads in the weeks prior to the 2010 election which are highly critical of Democratic Senatorial candidates and attack those candidates on their positions. For instance, Crossroad GPS reports that the follow advertisement began running in California in the last week of August 2010:

California seniors are worried. Barbara Boxer voted to cut spending on Medicare benefits by \$500 billion. Cuts so costly to hospitals and nursing homes that they could stop taking Medicare altogether. Boxer's cuts would sharply reduce benefits for some and could jeopardize access to care for millions of others. And millions of Americans won't be able keep the plan or doctor they already have. Check the facts and take action. Call Boxer. Stop the Medicare cuts.¹¹

Another ad run in Pennsylvania which started in the last week of August, 2010 attacks Democratic Senatorial candidate Joe Sestak:

We're hurting, but what are they doing in Washington? Congressman Joe Sestak voted for Obama's big government health care scheme, billions in job-killing taxes, and higher insurance premiums for hard-hit families. Even worse, Sestak voted to gut Medicare, a \$500 billion cut. Reduced benefits for 850,000 Pennsylvania seniors. Higher taxes and premiums, fewer jobs, Medicare cuts. The Sestak-Obama plan costs us too much. Tell Congressman Sestak stop the Medicare cuts.¹²

A second ad attacking Joe Sestak states:

Over half a million Pennsylvanians unemployed. And what's Congressman Joe Sestak done? He voted to gut Medicare, slashing benefits for Pennsylvania seniors. The Obama-Sestak scheme could jeopardize access to care for millions. Sestak even voted to raise taxes over \$525 billion, devastating small businesses, killing jobs, gutting Medicare, hurting seniors, killing jobs. Pennsylvania can't

¹⁰ K. Vogel, *supra*.

¹¹ See Crossroads GPS launches new issue ads in Pennsylvania, California and Kentucky, Crossroads GPS (Aug. 25, 2010) at <u>http://www.crossroadsgps.org/news/crossroads-gps-launches-new-issue-ads-pennsylvania-california-and-kentucky</u> (last visited Sept. 30, 2010); see also Crossroads GPS website, at <u>http://www.crossroadsgps.org/video/worried</u>.

¹² See Crossroads GPS launches new issue ads in Pennsylvania, California and Kentucky, supra.

afford Joe Sestak. Crossroads GPS is responsible for the contents of this advertising. 13

According to published reports, Crossroad GPS began running the following ad in Kentucky beginning on August 31, 2010:

Obamacare is the wrong way for Kentucky. And Jack Conway is going the wrong way too. Obamacare means \$525 billion in job killing taxes. It means higher insurance premiums. \$500 billion cut from Medicare. Reduced benefits for 113,000 Kentucky seniors. And intrusive big-government government mandates. It's the wrong way, Conway. Crossroads GPS is responsible for the contents of this advertising.¹⁴

With regard to the Colorado Senate race, it was reported on August 17, 2010 that Crossroads GPS was broadcasting the following ad attacking Democratic candidate Michael Bennet:

Michael Bennet's spending spree. Since his appointment, Bennett 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 Bennett's spending spree. Call Senator Bennet, stop the spending.¹⁵

With regard to the Missouri Senate race, Crossroads GPS began running the following ad in mid-August 2010 attacking Democratic candidate Robin Carnahan:

Male announcer: The message is clear. Seventy-one percent of Missouri voters don't want government mandated health care. We want to make our own health care decisions.

Female announcer: But Robin Carnahan disagrees, while seventy-one percent of us voted no, Carnahan sided with lobbyists, big unions, and Washington insiders to force Obamacare on us.

Male announcer: Missouri's Lieutenant Governor is suing the federal government so we can keep our health care.

¹³ Crossroads GPS website, *at* <u>http://www.crossroadsgps.org/</u> (left sidebar) (last visited Sept. 30, 2010).

¹⁴ Jeremy P. Jacobs, *Crossroads GPS Targets Obama in KY*, Hotline on Call (Aug. 31, 2010) *at* <u>http://hotlineoncall.nationaljournal.com/archives/2010/08/american_crossr_1.php</u>.

¹⁵ Jeremy P. Jacobs, *American Crossroads Airs Ads in OH, CO*, Hotline on Call, (August 17, 2010), at <u>http://hotlineoncall.nationaljournal.com/archives/2010/08/american_crossr.php</u>; *see also* Crossroads GPS website, *at* <u>http://www.crossroadsgps.org/video/bennet-calendar</u> (last visited Sept. 30, 2010).

Female announcer: Tell Carnahan to get in touch with Missourians and support the health care challenge.¹⁶

And in another closely contested Senate race, Crossroads GPS began running an ad attacking Democratic candidate Senator Harry Reid beginning in mid-August 2010:

Obamacare is bad for healthcare in America. And worse for Nevada. Because when Senator Harry Reid needed votes to push Obamacare, he cut sweet deals across the country – to help Nebraska, to help Louisiana, to even help Florida. What has Nevada gotten from Senator Reid? Record foreclosures and the highest unemployment rate in the nation. And Reid's still pushing for even more government control of your healthcare. Really, Harry? How 'bout some help for Nevada.¹⁷

Although both American Crossroads and Crossroads GPS are closely affiliated organizations headed by the same person and both are the brainchild of Rove and Gillespie, and although both organizations are running ads promoting Republican candidates or attacking Democratic candidates in the 2010 congressional races, there is one very important difference between the two groups when it comes to the American people's right to know basic campaign finance information.

As a federal registered political committee, American Crossroads is required to make timely disclosure of its contributors to the Federal Election Commission. 2 U.S.C. § 434. But as a group claiming section 501(c)(4) status, Crossroads GPS has no obligation to disclose its donors to the public and is not doing so. Indeed, on its website, Crossroads GPS touts the fact that its "policy" is to shield its donors from public disclosure:

Any person or entity that contributes more than 5,000 to a 501(c)(4) organization must be disclosed to the Internal Revenue Service on Form 990. However, the IRS does not make these donor disclosures available to the general public. Crossroads GPS's policy is to not provide the names of its donors to the general public.¹⁸

Indeed, it appears that the Crossroads GPS 501(c)(4) group was created in order to provide anonymity for donors providing money for campaign expenditures who otherwise might

¹⁶ See Peter H. Stone, American Crossroads Spin-off Launches New Ads in Missouri, Nevada Center for Public Integrity (August 20, 2010), at <u>http://www.publicintegrity.org/blog/entry/2359/</u> (last visited Sept. 30, 2010); see also Crossroads GPS website, at <u>http://www.crossroadsgps.org/video/issue-ad-robin-carnahan</u> (last visited Sept. 30, 2010).

¹⁷ See American Crossroads Spin-off Launches New Ads in Missouri, Nevada, supra; see also Crossroads GPS website, at <u>http://www.crossroadsgps.org/video/thanks-harry</u> (last visited Sept. 30, 2010).

¹⁸ https://www.icontribute.us/crossroadsgps.

resist making donations to the American Crossroads 527 group because donations to the 527 group would be subject to public disclosure.

As one published report states:

A new political organization conceived by Republican operatives Karl Rove and Ed Gillespie formed a spin-off group last month that – thanks in part to its ability to promise donors anonymity – has brought in more money in its first month than the parent organization has raised since it started in March.¹⁹

The same article quotes Steven Law, the head of both American Crossroads and Crossroads GPS as saying that "the anonymity of the new 501(c)(4) GPS group was appealing for some donors." *Id.* Law said, "We're not inclined to get into much detail about the 501(c)(4) on the financial side given its different report status." *Id.* The article also states:

[A] veteran GOP operative familiar with the group's fundraising activities said the spin-off was formed largely because donors were reluctant to see their names publicly associated with giving to a 527 group, least of all one associate with Rove, who Democrats still revile for his role in running former President George W. Bush's political operation.

In another article, Law stated, "I wouldn't want to discount the value of confidentiality to some donors." 20

Another published report calls Crossroads GPS a "spinoff of American Crossroads" and states that "this 501-c-4 group can keep its donor list private – a major selling point for individuals and corporations who want to anonymously influence elections."²¹

II. An Organization Which Primarily Engages in Political Campaign Activity Does Not Qualify for Section 501(c)(4) Tax-Exempt Status

A. General rule.

Section 501(c)(4) of the Internal Revenue Code establishes tax-exempt status for "[c]ivic leagues or organizations not organized for profit but <u>operated exclusively</u> for the promotion of social welfare...." 26 U.S.C. § 501(c)(4) (emphasis added).

According to IRS regulations, "An organization is operated exclusively for the promotion of social welfare if it is <u>primarily engaged</u> in promoting in some way the common good and general welfare of the people of the community." 26 C.F.R. 1.501(c)(4)-1(a)(2)(i) (emphasis added).

¹⁹ K. Vogel, *supra*.

²⁰ K. Vogel, "Crossroads hauls in \$8.5M in June," *Politico* (June 30, 2010).

²¹ H. Bailey, *supra*.

Political activity – spending to influence campaigns – does not constitute promoting the social welfare. Section 1.501(c)(4)-l(a)(2)(ii) of the regulations provides that political campaign activities do not promote social welfare as defined in section 501(c)(4). The regulation states, "The promotion of social welfare does not include <u>direct or indirect participation or intervention in political campaigns</u> on behalf of or in opposition to any candidate for public office." 26 C.F.R. § 1.501(c)(4)–1(a)(2)(ii) (emphasis added).

In other words, an organization primarily engaged in political campaign activity is <u>not</u> primarily engaged in the promotion of the social welfare of the community and, therefore, is <u>not</u> eligible for tax-exempt status under section 501(c)(4). For example, "[a]n organization whose primary activity is rating candidates for public office is not exempt from Federal income tax under section 501(c)(4) of the Internal Revenue Code of 1954 because such activity does not constitute 'promotion of the social welfare.'" Rev. Rul. 67–368, 1967–2 C.B. 194.

Although the promotion of social welfare does not include political campaign activities, IRS 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) <u>as long as it is primarily engaged in activities that promote social welfare[,]</u>" in other words, as long as it is not primarily engaged in political activities. Rev. Rul. 81–95, 1981–1 C.B. 332 (emphasis added).

B. Political campaign activity under the Internal Revenue Code.

IRS rules make clear that "direct or indirect participation or intervention in political campaigns on behalf of or in opposition to any candidate for public office" is not limited to activities or communications which contain express advocacy or the functional equivalent of express advocacy.

Section 527(e)(2) of the Internal Revenue Code describes what constitutes political campaign (*i.e.*, "exempt function") activity for purposes of the tax code:

The term "exempt function" means the function of influencing or attempting to influence the selection, nomination, election, or appointment of any individual to any Federal, State, or local public office or office in a political organization, or the election of Presidential or Vice Presidential electors, whether or not such individual or electors are selected, nominated, elected or appointed.

26 U.S.C. § 527(e)(2).

Revenue Ruling 2004–6, 2004–4 I.R.B. 328, provides a detailed explanation of what constitutes "exempt function" political campaign activity—illuminating the line between the political activities that may not be the primary activities of 501(c)(4) organizations, and those which may. The IRS there states:

Section 1.527-2(c)(1) provides that the term "exempt function" includes all activities that are directly related to and support the process of influencing or attempting to influence the selection, nomination, election, or appointment of any individual to public office or office in a political organization. Whether an expenditure is for an exempt function depends on all the facts and circumstances.

Id. (emphasis added)

Revenue Ruling 2004-6 explains that, because section 501(c)(4) public policy advocacy "may involve discussion of the positions of public officials who are candidates for public office, a public policy advocacy communication may constitute an exempt function (a political activity) within the meaning of § 527(e)(2)." Rev. Rul. 2004-6 at 1. The Ruling further states:

All the facts and circumstances must be considered to determine whether an expenditure for an advocacy communication relating to a public policy issue is for an exempt function under § 527(e)(2). When an advocacy communication explicitly advocates the election or defeat of an individual to public office, the expenditure clearly is for an exempt function under § 527(e)(2). However, when an advocacy communication relating to a public policy issue does not explicitly advocate the election or defeat of a candidate, all the facts and circumstances need to be considered to determine whether the expenditure is for an exempt function under § 527(e)(2).

Id. (emphasis added)

Thus, regardless of whether an "issue ad" contains express advocacy, it may nonetheless be treated as "exempt function" electioneering activity under IRS regulations, depending on the "facts and circumstances."

Even if an ad discusses an "issue," and even if the ad does not contain express advocacy or the functional equivalent of express advocacy, it can still be treated as "direct or indirect participation or intervention in political campaigns" under IRS standards for purposes of determining whether a 501(c)(4) organization is "primarily engaged" in activities to influence elections.

Rev. Rul. 2004-6 lists six factors that "tend to show" that an advertisement is "exempt function" political campaign activity, and five competing factors that "tend to show" that an advertisement is not. Rev. Rul. 2004-6 at 3-4. The "factors that tend to show that an advocacy communication on a public policy issue is for an exempt function (political activity) under § 527(e)(2)" include 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.

Rev. Rul. 2004-6 at 3.

The "factors that tend to show that an advocacy communication on a public policy issue is not for an exempt function under 527(e)(2)" include the following:

- a) The absence of any one or more of the factors listed in a) through f) above;
- b) The communication identifies specific legislation, or a specific event outside the control of the organization, that the organization hopes to influence;
- c) The timing of the communication coincides with a specific event outside the control of the organization that the organization hopes to influence, such as a legislative vote or other major legislative action (for example, a hearing before a legislative committee on the issue that is the subject of the communication);
- d) The communication identifies the candidate solely as a government official who is in a position to act on the public policy issue in connection with the specific event (such as a legislator who is eligible to vote on the legislation); and
- e) The communication identifies the candidate solely in the list of key or principal sponsors of the legislation that is the subject of the communication.

Id.

Under this multi-part test, the "facts and circumstances" here certainly indicate that the ads and activities of Crossroads GPS involve "exempt function" activity that constitutes "participation or intervention in political campaigns."

First, the organization was created just months before the 2010 congressional elections, was conceived, organized and staffed by leading political party strategists and operatives, self-defined its activities as spending money in Senate races and is closely affiliated with other organizations similarly committed to spending large sums to influence the 2010 congressional races.

Second, the activities of the organization are targeted to battleground states involving key Senate races, and to supporting Republican candidates in those elections.

Third, the ads run by the organization identify candidates by name, discuss the candidates' position on issues in the midst of a campaign and do so in ways that criticize the positions of the Democratic candidates opposed by Crossroads GPS.

Fourth, the timing of the group's activities do not correspond with external events outside the group's control, such as a legislative vote on an issue, but rather correspond with congressional election campaigns.

C. Primary purpose. There is little question that Crossroads GPS is engaged in activities which constitute "exempt function" political intervention under the IRS standards. Although the organization can engage in some political participation or intervention under IRS regulations, it cannot be <u>primarily</u> engaged in such activity, consistent with its tax status under section 501(c)(4).

In a 2008 Letter Ruling, the IRS found an organization did not qualify for tax exempt status under section 501(c)(4) because it was primarily engaged in political intervention. The IRS said:

Whether an organization is "primarily engaged" in promoting social welfare is a facts and circumstances determination. Relevant factors include the manner in which the organization's activities are conducted; resources used in conducting such activities, such as buildings and equipment; the time devoted to activities (by volunteers as well as employees); the purposes furthered by various activities; and the amount of funds received from and devoted to particular activities.

2008 TNT 160-33 (May 20, 2008) (emphasis added). The Letter Ruling continued:

In Rev. Rul. 81-95, 1981-1 C.B. 332, we concluded that "an organization may carry on lawful political activities and remain exempt under section 501(c)(4) of the Code as long as it is primarily engaged in activities that promote social welfare." The corollary to this is that if an organization's primary activities do not promote social welfare but are direct or indirect political intervention, the organization is not exempt under section 501(c)(4). The key is to determine the character of the organization's primary activities by looking at all of the facts and circumstances.

Id. (emphasis added).

In the Letter Ruling, the IRS considered the organization's claim that it was primarily engaged in lobbying, not campaign intervention. The Letter Ruling states:

A facts and circumstances test is to be used in determining whether an organization's activities primarily constitute political intervention or whether

those activities constitute lobbying or educational activities. After reviewing all of the facts and circumstances presented in the administrative file as discussed above, we have concluded that your primary emphasis and primary activities constituted direct and indirect political intervention. While you engage in extensive lobbying activities, they are by no means your primary activity. <u>Your first and primary emphasis is on getting people elected to public office</u>.

Id. (emphasis added). The IRS thus concluded:

The emphasis throughout your materials is on electing to office * * * people in order to impact legislation and policy as insiders. The overwhelming majority of the evidence in the administrative record, and thus the facts and circumstances in this case, denotes an organization that is intent upon intervening in political campaigns. . . .While lobbying is usually mentioned, and we recognize that lobbying activities are being pursued, those activities are not your primary activity. An analysis of all of the facts and circumstances contained in the administrative file leads us to the conclusion that your primary activity constitutes political intervention.

Id. (emphasis added).

Therefore, the organization did not qualify for tax exemption under section 501(c)(4):

Based upon the materials submitted in connection with your application, we have concluded that your activities primarily constitute direct and indirect participation or intervention in political campaigns on behalf of or in opposition to candidates for public office. Therefore, you are not primarily engaged in activities that promote social welfare and do not qualify for recognition of exemption under section 501(c)(4) of the Code.

Similarly, the IRS needs to investigate in this case whether the "facts and circumstances" show that Crossroads GPS is primarily engaged in activities which constitute political participation or intervention in political campaigns under IRS regulations, and if it is, to find that the organization is a violation of its section 501(c)(4) status.

The "primarily engaged" test should be applied on the basis of the activities undertaken by Crossroads GPS during calendar year 2010. If a section 501(c)(4) group is found to have primarily engaged in campaign-related activities during an election year, it should not be permitted to dilute that finding by engaging in non-election related activities in subsequent years.²²

For example, the IRC uses a "taxable year" analysis – in other words, a calendar year analysis – to determine whether a section 501(c)(3) charitable group has complied with the limit on the amount of lobbying expenditures the group is permitted to engage in, consistent with its charitable status. 26 U.S.C. § 501(h).

Although we do not have access to the contribution and expenditure data that Crossroads GPS is required to file with the IRS, published reports indicate that the organization is primarily engaged in activities to influence the 2010 congressional elections. As part of its investigation, the IRS needs to examine the organization's financial data.

If the IRS examination of the facts and circumstances surrounding Crossroads GPS's formation and activities confirm that the organization is primarily engaged in section 527 "exempt function" political campaign activity in 2010, the IRS should find that Crossroads GPS is in violation of its tax status under section 501(c)(4).

III. Conclusion.

Crossroads GPS was organized under section 501(c)(4) of the Internal Revenue Code. Based on the discussion of the published reports set forth above, the facts and circumstances surrounding the formation and activities of Crossroads GPS show that the group was organized to participate and intervene in the 2010 congressional races while providing donors to the organization with a safe haven for hiding their role in funding expenditures to influence the 2010 congressional races.

For the reasons set forth above, the IRS should investigate whether Crossroads GPS has a primary purpose of "participation or intervention in political campaigns on behalf of or in opposition to" candidates for public office, which is <u>not</u> a permissible primary purpose for a section 501(c)(4) organization. *See* 26 C.F.R. § 1.501(c)(4)-1(a)(2).

If the IRS investigation establishes that the facts and circumstances show that Crossroads GPS is primarily engaged in participating or intervening in political campaigns, appropriate penalties should be imposed on the organization, including penalties that take into account the need to deter similar widespread violations from occurring in future elections. The penalties should apply to the organization's misuse of the nonprofit tax laws to improperly claim section 501(c)(4) tax status and its failure to operate as a nonprofit 527 group required to disclose its contributions and expenditures.

Sincerely,

/s/ Gerald Hebert

J. Gerald Hebert Executive Director Campaign Legal Center /s/ Fred Wertheimer

Fred Wertheimer President Democracy 21