taxanalysts special report

The Effect of *Citizens United* on Tax and Campaign Laws Governing Tax-Exempt Organizations

by B. Holly Schadler and Laurence E. Gold

B. Holly Schadler *Laurence E. Gold*

B. Holly Schadler is a partner at Lichtman Trister & Ross PLLC. Laurence E. Gold is of counsel to the firm.

* * * * *

The Supreme Court's recent ruling in *Citizens United v. Federal Election Commission*[1] permits corporations to spend directly on broadcast and other public communications that explicitly endorse and oppose candidates for public office. While the ruling has been reported as sending "shock waves" through the American political system, the actual effect on how tax-exempt organizations engage in the electoral process remains unclear in important respects. In large measure this uncertainty arises because the tax rules for exempt organizations remain unchanged and continue to impose limitations on and disincentives against the types of activities and amount of political involvement in which such organizations may engage. The full effect of *Citizens United*, along with other recent developments, will not be understood for months while the Federal Election Commission (FEC) and state campaign finance agencies revise their regulations and policies to reflect the holding. Congress may pass legislation addressing some of the changes, and numerous state legislatures are likely to do so. Finally, pending and future litigation promises to bring more changes.[2]

The Ruling in *Citizens United*

In a 5-4 decision, the Supreme Court held that the First Amendment prohibits governmental restrictions on corporations, including nonprofit organizations, spending general treasury funds for independent public communications that "expressly advocate" the election or defeat of clearly identified federal candidates.[3] By implication, the ruling affects labor organizations in the same manner. And, because *Citizens United* is a First Amendment decision, state restrictions on independent corporate and union political speech are no longer enforceable as well.[4]

Prior to this decision, virtually all corporations were prohibited under federal law from engaging in express advocacy.[5] While corporations and unions could spend

[1]No. 08-205, 558 U.S. ___ (2010).

[2]*See, for example*, *Speechnow.org v. FEC*, Nos. 08-5223(L) and 09-5342 (D.C. Cir.) (decision pending); *Thalheimer v. San Diego*, No. 09-CV-2862 (S.D. Cal.).

[3]At issue in the case was the attempt by Citizens United, a nonprofit corporation exempt as an organization described under section 501(c)(4), to make its documentary film "Hillary: The Movie," already screened in public theaters, available for home consumption through a video-on-demand provider via cable and satellite television technology. Citizens United also wanted to promote the film in television advertisements. Unlike theatrical and Internet distribution, the proposed televising of the film and the ads implicated the electioneering communications provisions of the Bipartisan Campaign Reform Act (BCRA), which prohibit corporate (and union) expenditures for certain broadcast communications that "refer" to a federal candidate and run within 30 days of a primary or 60 days of a general election. *See* 2 U.S.C. section 441b(b)(2) and (c). The majority found that the film was the "functional equivalent of express advocacy" because there was "no reasonable interpretation" other than that it was an appeal to vote against Hillary Clinton for the office of president. Accordingly, BCRA prohibited the televising of the film. *See Citizens United v. FEC*, slip op. at 7-8; *FEC v. Wisconsin Right to Life, Inc.*, 551 U.S. 449 (2007)(Court ruled that an ad may be prohibited during the blackout period only if it is the "functional equivalent" of express advocacy, defined as being "susceptible of no reasonable interpretation other than as an appeal to vote for or against a specific candidate.")

[4]Many states permitted unlimited corporate and union treasury spending on express advocacy and other independent electoral speech to the general public prior to *Citizens United*. *See* http://www.ncsl.org/default.aspx?tabid=19607. Restrictions on such independent speech in the other states are now invalid. Virtually all state campaign finance laws will be affected by the decision in some manner.

[5]*See* 2 U.S.C. section 441b(a). The Supreme Court's decision, *Federal Election Commission v. Massachusetts Citizens for Life, Inc.*, 479 U.S. 238 (1986), created an exception for so-called MCFLs or qualified nonprofit corporations (QNCs), which are permitted to make independent expenditures and electioneering communications using their own corporate treasury funds. To qualify as a QNC, an incorporated section 501(c)(4) group must meet

(Footnote continued on next page.)

treasury funds for independent public communications with election-related messages, they could not use phrases that urge the election or defeat of a clearly identified candidate, such as ''vote for,'' ''defeat,'' or ''support your Democratic Senate nominee.'' In addition, prior to *Citizens United*, corporations and unions were prohibited from paying for ''electioneering communications'' — broadcast communications 30 days before a federal primary and 60 days before a general election that refer to federal candidates if the ads were the ''functional equivalent of express advocacy,'' that is, they were ''susceptible of no reasonable interpretation other than as an appeal to vote for or against a specific candidate.''[6] *Citizens United* invalidated these restrictions on political speech.

The Court took a decidedly different view of the related public information requirements of the Federal Election Campaign Act (FECA). The Court upheld by an 8-1 margin both FECA's ''disclaimer'' requirements that such communications clearly identify who paid for the communication and its disclosure requirement that the sponsor file reports with the FEC itemizing its expenditures as well as certain donations received by the sponsor.[7]

The *Citizens United* decision does not affect the prohibition on corporations, unions, and advocacy groups making *contributions* to federal candidates and national political parties. While many states currently permit contributions from these sources to state and local candidates and the nonfederal accounts of state and local political party committees, and may continue to do so, federal and state laws that either prohibit or limit corporate and labor contributions remain unchanged. Similar restrictions on contributions to and by federally registered political committees (federal PACs) that contribute to candidates and parties are also unaffected by *Citizens United*. Nor does the decision affect the funding and spending prerogatives of federal PACs that undertake only independent expenditures, although those matters are at issue in a pending and closely-watched lower court case, *Speechnow.org v. FEC*.

Federal Tax Rules and *Citizens United*

Notwithstanding the Court's ruling in *Citizens United*, the federal tax rules impose significant restrictions on exempt organizations' political activities. This article examines the federal tax and campaign finance laws governing political activities of section 501(c) organizations.[8]

- **Public Charities and Private Foundations**

Citizens United does not change the tax rules that prohibit section 501(c)(3) organizations from engaging in any partisan political activity. While private foundations and public charities may support or engage in certain nonpartisan voter education and engagement activities, they may 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.''[9]

The consequences are severe for a public charity that engages in even a *de minimis* amount of political intervention. If a public charity makes a prohibited political campaign expenditure, the IRS may impose an initial excise tax on the organization in an amount equal to 10 percent of the expenditure and a similar tax of 2.5 percent on certain managers. If the expenditure is not corrected within a prescribed period, an additional tax may be imposed on both the organization and the managers. The charity also risks losing its tax exemption.[10] Similarly, private foundations are subject to excise tax on any political expenditures.[11]

While the *Citizens United* ruling may spur a legal challenge to the ''facts and circumstances'' test employed by the IRS to define nonpartisanship, it is clear that the restrictions on electoral activity by section 501(c)(3) organizations remain. They rest on a legal footing distinct from the constitutional justifications that, prior to *Citizens United*, the Supreme Court had recognized as sufficient to uphold proscriptions against corporate or union treasury-funded independent expenditures and electioneering communications.[12] In *Regan v. Taxation With Representation of Washington* (*TWR*), the Supreme Court held that Congress was not required to subsidize with tax deductibility and a tax exemption an organization's lobbying activities, which, like the political campaign activities discussed here, are generally protected by the First Amendment.[13] The Court emphasized that individuals associated with exempt organizations were not denied the right to engage in lobbying activities because they had the option of establishing both a section 501(c)(3) organization to receive tax-deductible contributions and conduct limited lobbying activities and a section 501(c)(4) affiliate to conduct unlimited lobbying activities.

Similarly, in *Branch Ministries v. Rossotti*, a federal appellate court upheld the denial of exemption under section 501(c)(3) to a church that had published an advertisement urging the public to vote against Bill

---

stringent criteria, including not accepting business or labor union contributions. *See* 11 C.F.R. section 114.10. The *Citizens United* decision likely renders this status obsolete because the use of business or union funds for public electoral communications are no longer prohibited.

[6]*FEC v. Wisconsin Right to Life, Inc.*, *supra see also* 11 C.F.R. section 114.15.

[7]*Citizens United v. FEC*, slip op. at 50-56.

[8]All references to section 501(c) are to the Internal Revenue Code.

[9]Section 501(c)(3). The IRS has permitted certain nonpartisan election-related activities such as publishing legislative scorecards; preparing candidate questionnaires; sponsoring candidate debates; and conducting nonpartisan get-out-the-vote, voter registration, and education drives. *See, for example,* IRS 2002 EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION TEXT, *Election Year Issues* 2002 CPE TEXT.

[10]Section 4955.

[11]Section 4945.

[12]*See McConnell v. FEC*, 540 U.S. 93, 203-09 (2003); *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990).

[13]461 U.S. 540 (1983).

Clinton for President in the 1992 general election.[14] In rejecting the church's free exercise challenge to the IRS's determination, the court of appeals applied the Supreme Court's reasoning in *TWR*, noting that the church could form a related organization that would be free to participate in political campaign activities. The court stressed, however, that any such related organization would have to be separately incorporated and "must maintain records that will demonstrate that tax-deductible contributions to the Church have not been used to support the political activities conducted by the section 501(c)(4) organization's political action arm."[15]

Therefore, while there may be future challenges to the restrictions on public charities, the current rules prohibiting their political activity remain in place, and it does not necessarily follow from *Citizens United* that those restrictions are legally vulnerable.

- **Other Section 501(c) Organizations: Social Welfare Organizations, Labor Unions, and Trade Associations**

Although *Citizens United* now permits corporations and unions to make independent expenditures, section 501(c) organizations nevertheless remain constrained by the tax laws in the amount of political activities they may conduct. The Court's ruling does not address or alter these restrictions. Therefore, a 501(c)(4) social welfare organization may carry out political activities without jeopardizing its tax-exempt status as long as it is engaged primarily in non-electoral activities that promote social welfare. Education and lobbying on social and economic issues qualify as social welfare activities, but participation in partisan political campaigns does not. Unions (501(c)(5) entities) and trade associations (501(c)(6) entities) similarly must primarily pursue their respective non-electoral activities for which they enjoy tax exemption.

Primary Purpose. There is no clear test for determining when political activity becomes an organization's primary purpose. While one approach is to analyze a group's spending, the IRS may also consider other factors such as: staff and other organizational resources devoted to conducting the organization's social welfare versus political activities; the profile of the activities conducted; and the time of both volunteers and staff devoted to political activities. If an organization's annual partisan political expenditures are relatively small compared to its overall budget, the organization's tax-exempt status is generally safe.[16]

Even determining whether or not certain activities are "political" (or, in the terminology of the code, "exempt function")[17] is frequently difficult in light of the facts and circumstances test applied by the IRS. An activity is considered political if it is conducted to influence the election, selection, nomination, or appointment of any individual to a federal, state, or local public office; to an office in a political organization; or as a delegate or elector for president or vice president.[18] Despite the generally subjective nature of this test, the express advocacy communications permitted under *Citizens United* will definitely be treated as political activity because their partisan nature is inarguable. Therefore, if a 501(c) organization now chooses to undertake express advocacy, in order to preserve its tax-exempt status it will have to limit these communications (as well as other partisan activity) to a decidedly secondary portion of its overall activities.

Section 527(f) Tax. In addition, a section 501(c) organization may be subject to a tax on all or a portion of its spending of general treasury funds for exempt function activities. Under section 527(f), the tax is imposed at the highest corporate rate (currently, 35 percent) on the lesser of: (1) the organization's annual net investment income (income from interest, dividends, rents, and royalties, and the gains from sale or exchange of assets, minus the losses for such assets, investment-management expenses and other costs incurred in producing that income); or (2) the aggregate amount expended on political activities during that year. Therefore, if a section 501(c) organization has investment income, undertaking political activities will likely give rise to a tax liability.[19]

No tax currently results if a section 501(c) group pays for certain expenses explicitly permitted by FECA or "similar" state election laws, such as partisan engagement with the group's own members and establishing, administering, and fundraising for a PAC.[20] The regulations provide that these are expenditures for an exempt function only to the extent provided in the regulations. The specific regulation covering these expenses, however, is "reserved" and no final decision has ever been made on their treatment.[21] In any event, partisan spending that is not subject to 527 tax nonetheless counts in determining the organization's primary purpose.

The tax treatment of "indirect expenses" is similarly reserved in the final regulations.[22] IRS regulations provide for two types of exempt function expenditures —

[14]211 F. 3d 137, 143 (D.C. Cir. 2000).

[15]*Id.*

[16]*See* Rev. Rul. 81-95, 1981-1 C.B. 332; IRS 2003 EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION TEXT, *POLITICAL CAMPAIGN AND LOBBYING ACTIVITIES OF 501(c)(4), 501(c)(5) AND 501(c)(6) ORGANIZATIONS* AT L-3. Section 501(c) organizations are also subject to the FEC's "major purpose test" to the extent that they are engaging in activities to influence federal elections. See discussion of the "major purpose test" under the "Impact of *Citizens United* on Political Organizations" below.

[17]Section 527(e)(2).

[18]*Id.*

[19]A 501(c) organization is required to file an IRS Form 1120-POL if it has $100 or more in both net investment income and exempt function expenditures

[20]Reg. section 1.527-6(b)(3); *see* 2 U.S.C. section 441b(b).

[21]*Id.* Particularly in light of *Citizens United*, there is some question about the breadth of the "reserved" portions of this regulation. It is unclear why expenditures for member communications and PAC sponsorship are currently not subject to the 527(f) tax but other legally permissible partisan political activities may not be. The IRS has never provided a cogent explanation of where it draws the 527(f) line. *See, for example*, 2002 CPE Text at 435.

[22]Reg. section1.527-6(b)(2).

''directly related expenses'' and ''indirect expenses.''[23] ''Directly related expenses'' include expenditures made for activities that are directly related to and support the process of influencing or attempting to influence the election process. ''Indirect expenses'' are expenses that are not directly related to influencing or attempting to influence the election process, but are necessary to support the directly related activities of a political organization. The regulations specifically identify such support functions as overhead, recordkeeping, administrative, and fundraising as indirect expenses.[24]

Based on IRS private letter rulings, however, indirect expenses may also cover some programmatic costs, including ''acquisition and enhancement of voter lists to target distribution of materials,'' candidate research, polling and focus groups.[25] Engagement with other organizations that does not comprise voter contact also appears to fall in the ''indirect'' category. The IRS's guidance states that a ''501(c) organization currently may make any indirect exempt function expenditures and will not be subject to tax with respect to such expenditures under section 527.''[26] If the IRS changes this position it will be effective only on a prospective basis.[27]

In addition, there continues to be a range of nonpartisan, but election-related, activities that are not considered political activities under the code, and, so long as they relate to a section 501(c) group's primary purpose, they neither activate the section 527(f) tax nor undermine the group's tax-exempt status. These activities include voter education and engagement activity such as candidate questionnaires and debates, issue education projects, get-out-the-vote programs, and voter registration — again, so long as they are conducted in a nonpartisan manner.[28]

Section 162(e) Proxy Tax. Other tax rules could affect particularly the ability of some section 501(c)(4) and 501(c)(6) organizations to raise funds for political activity.[29] While certain members of these groups may, in some circumstances, deduct their dues as an ordinary and necessary business expense, the portion of dues that funds lobbying and political expenditures is not tax deductible.[30] These organizations are required to alert members about the percentage of dues (and similar amounts), if any, allocated to lobbying and political expenditures.[31] If the organization fails to give this notice, or if it provides a notification that underestimates the percentage of dues used for these purposes, the IRS may impose a tax on the organization equal to 35 percent of its lobbying and political expenditures.[32]

A section 501(c)(4) organization is exempt from this notice requirement if: (1) more than 90 percent of all dues or similar amounts are received from persons or entities paying $101 or less or (2) 90 percent or more of the membership dues to the organization come from nonbusiness sources (such as section 501(c)(3) organizations and state and local governments) and are, therefore, nondeductible in any event.[33] An exception similar to (2) above applies to section 501(c)(6) organizations. If, however, a greater percentage of dues is raised from corporations and others that deduct ordinary and necessary business expenses, then this tax provision is likely to have more of an impact.

Gift Tax. Another issue that may affect a section 501(c)(4) or (c)(6) organization's fundraising activities is the gift tax. While donations to such a group are not tax-deductible, they may subject the donor to gift tax. (In contrast, donations to section 527 and 501(c)(3) organizations are specifically excluded from the gift tax provisions, and section 501(c)(5) unions ordinarily rely upon non-donation sources of revenue, principally membership dues.) An individual donor may give up to $13,000 ($26,000 per married couple) per organization each year without the risk of incurring gift tax.[34]

Federal Campaign Finance Rules and *Citizens United*

- **Contributions to Candidates and Coordination**

As noted earlier, the Supreme Court's ruling in *Citizens United* does not alter federal and various state law prohibitions on corporations and labor unions using their regular treasury funds to make contributions to candidates and political parties.[35] FECA prohibits corporations, including nonprofit corporations, and unions from making any such contributions to federal candidates, federal PACs, national political parties, and the federal accounts of state and local parties.[36] Contributions include direct and indirect payments (including distributions, loans, advances, deposits, or gifts) of money, services, or anything of value to any such political recipient.[37]

Under this general rule, a nonprofit corporation such as a 501(c)(4) may not: contribute funds; make in-kind contributions by providing goods or services at no charge or at less than fair market value, such as turning over a mailing, membership, or donor list, assigning paid staff

[23] *See* reg. section 1.527-2(c)(1) and (c)(2).

[24] *Id.*

[25] *See, for example*, LTR 9652026, LTR 9808037 and LTR 9725036.

[26] 2002 CPE Text at 437; *see also* T.D. 7744, 1981-1 C.B. 360, 361.

[27] *Id.*

[28] *See for example*, Rev. Rul. 2007-41, 2007-25 I.R.B. (June 18, 2007).

[29] Section 501(c)(4) veterans organizations and 501(c)(5) labor organizations are entirely excepted from these requirements. Rev. Proc. 98-19, 1998-1 C.B. 547.

[30] Section 162(e)(3).

[31] Section 6033(e)(1)(A)(ii).

[32] Section 6033(e)(2).

[33] *See* Rev. Proc. 98-1; Rev. Proc. 2009-50.

[34] *See* section 2501 *et seq*.

[35] In light of the ruling in *Citizens United*, future litigation challenging the restrictions on corporate and union contributions is likely.

[36] *See* 2 U.S.C. section 441b(a). ''General treasury funds'' (or simply ''corporate funds'') are funds received in the ordinary course variously as dues, investments, or other income, as distinct from separate voluntary individual contributions from members or shareholders that are earmarked for electoral use by the organization.

[37] *See* 2 U.S.C. section 431(8).

to a campaign, or picking up the costs of a candidate's radio or television ads; or pay for coordinated communications. Expenditures that are made in concert or cooperation with a candidate or a political party continue to be treated as in-kind contributions and remain subject to the prohibitions and limitations of FECA; therefore, the rules defining and governing coordination have become increasingly important.[38]

Given the greater opportunities for corporate and union spending on election-related messages, there is likely to be enhanced focus on whether and how groups interact with candidates and parties, and whether the communications can be regulated as ''coordinated'' spending. While the current rules on coordinated communications remain in effect, numerous provisions have been rejected by the U.S Court of Appeals for the District of Columbia and are the subject of an ongoing FEC rulemaking.[39]

- **Communications to Members and the "Restricted Class"**

Even before *Citizens United*, a section 501(c) organization (other than a 501(c)(3)) was permitted to expressly advocate the election or defeat of clearly identified federal candidates in communications directed to its members, executive and administrative personnel, and their families (together referred to as a group's ''restricted class''). These communications remain important tools for political advocacy because an organization has a naturally greater affinity with these individuals than it has with the public at large. Also, unlike the public electoral communications that are now permissible under *Citizens United*, restricted class communications may be coordinated with candidates and political parties, so even their intrinsically superior effectiveness may be enhanced further by collaboration on their timing, content, and other aspects.[40] In addition, as discussed earlier, a group's spending for these communications is exempt from the 527(f) tax.

So, for example, a section 501(c)(4) organization may invite a federal candidate, a candidate's representatives, and political party representatives to address its membership.[41] There is no requirement to invite all candidates in a race; rather, the organization may invite only the candidate it supports or the representative of one political party and exclude all others, announce its support for the candidate or party, and urge its members to contribute to that candidate or party (so long as the group does not facilitate the contributions further by collecting and transmitting them). And, the candidate or representative may solicit and accept contributions for the campaign or political party before, during, or after the event.[42]

By contrast, FEC rules governing communications involving candidate appearances before the general public likely remain in effect in the wake of *Citizens United*. For example, a section 501(c)(4) group may conduct federal candidate debates that are open to the public only if the organization does not endorse, support, or oppose

[38]FEC regulations set out a three-part test to determine if a particular communication is ''coordinated.'' First, the communication must be paid for, in whole or in part, by someone other than a candidate, a candidate's authorized committee, or their agents, or a political party or its agents. 11 C.F.R. section 109.21(a)(1).

Second, the communication must be: (a) an electioneering communication; (b) a ''public communication'' that includes, in whole or in part, campaign materials prepared by a candidate, the candidate's authorized committee, or any agent of either; (c) a ''public communication'' that expressly advocates the election or defeat of a clearly identified candidate; or (d) a ''public communication'' that refers to a political party or a clearly identified federal candidate, is publicly distributed within 120 days (for a presidential candidate) or 90 days (for a congressional candidate) before a general, special, or runoff election or a primary, convention, or caucus, and is directed to voters in the jurisdiction of the clearly identified candidate or to voters in a jurisdiction in which one or more candidates of the political party appear on the ballot. 11 C.F.R. section 109.21(c).

Third, the communication must be either: (a) made at the request or suggestion of a candidate; (b) made with a candidate, authorized committee, political party, or agent of any of them ''materially involved'' in the decisions regarding the communication's content, intended audience, means, mode, media outlet, timing, frequency, size, prominence, or duration of the communication; (c) made after ''substantial discussion'' about the communication between the spender and the candidate identified in the communication, his or her authorized committee, his or her opponent's authorized committee, a political party, or agents of any of them; or (d) made after receiving non-public information about a candidate's or political party's campaign plans, projects, activities, or needs, and that information is ''material'' to the creation, production, or distribution of the communication.

Finally, the coordination may occur if a communication is created, produced, or distributed with the assistance of: (a) a vendor who has provided services to a candidate, his authorized committee, his opponent's committee, or a political party within the previous 120 days or (2) an individual who was an employee or independent contractor of a candidate, authorized committee, or political party committee within the previous 120 days. The vendor, former employee, or independent contractor must either use, or convey to the person making the communication, information about the identified candidate's (or his opponent's) plans, projects, activities, or needs, and that information must be material to the creation, production, or distribution of the communication. 11 C.F.R. section 109.21(d).

[39]*Shays v. FEC*, 528 F. 3d 914 (D.C. Cir. 2008); *see* 74 Fed. Reg. 53893 (Oct. 21, 2009); 75 Fed. Reg. 6590 (Feb. 10, 2010).

[40]A section 501(c) group must report all of its regular-treasury spending for membership communications that expressly advocate the election or defeat of a clearly identified federal candidate if the aggregate costs exceed $2,000 per election. Quarterly reports (FEC Form 7, ''Report of Communication Costs by Corporations and Membership Organizations'') are filed with the FEC. Costs are aggregated for each election; consequently, there is a separate limit for primary, general, and special elections. The report requires an organization to identify the candidate(s) that the communication supported or opposed. If a communication identifies more than one candidate, the total costs may be allocated among the candidates. *See generally* 11 C.F.R. section 104.6.

[41]11 C.F.R. section 114.3(c)(2).

[42]*Id.*

any candidate or political party, and a corporation or labor union may only donate funds to support such a debate.[43]

- **Independent Communications**

Before the *Citizens United* ruling, among corporations only qualified nonprofit corporations (QNCs)[44] were permitted to make express advocacy communications to the general public.[45] Other section 501(c) organizations could lawfully communicate with the general public about federal candidates only if they did not use express advocacy, and no corporation could coordinate certain types of communications, including express advocacy, with federal candidates, political parties, and their agents. Extensive and detailed standards set out in section 114 of the FEC's regulations apply to these independent activities. As a consequence of the Court's ruling, the FEC is reviewing those rules, and it has already confirmed that it will no longer enforce the regulations prohibiting corporations and unions from making independent expenditures.[46] Therefore, subject to the tax rules discussed above, a corporation or union may use its treasury funds to publish and distribute voter guides and candidate questionnaires, and to conduct voter registration and get-out-the-vote drives, in connection with federal elections that include express advocacy and are directed to the general public.

Reporting. Post-*Citizens United*, corporations and unions that make independent expenditures from their general treasury accounts are now subject to longstanding FEC reporting requirements that previously applied, as a practical matter, only to those who previously could lawfully make them, mainly individuals, QNCs, and federal PACs, as well as certain groups that could but did so relatively infrequently, namely, unincorporated associations and partnerships.

Under current rules, a non-PAC independent expender must file FEC Form 5 (''Report of Independent Expenditures Made and Contributions Received'') in order to disclose any donor who contributed an aggregate amount above $200 specifically for independent expenditures. (The organization need not list other donors, regardless of timing and amount.). The Form 5 must also list every individual and entity that the filer paid more than $200 during a calendar year in connection with independent expenditures.[47] In addition to these periodic reports, corporations and unions must now file 48-hour and 24-hour reports disclosing expenditures above certain thresholds and at certain intervals preceding an election. Form 5 calculations and reporting pertain to each election for each particular office.

Disclaimers. FECA also requires that independent expenditure public communications include a statement (commonly referred to as a ''disclaimer'') identifying who financed and authorized the communication.[48] Disclaimers for independent expenditures must state the sponsor's full name and either permanent street address, telephone number, or web address, and the fact that the communication is not authorized by any candidate or campaign. There are special requirements for televised ads so that disclaimers have both audio and visual components.[49]

Electioneering Communications

Although the Supreme Court in *Citizens United* invalidated the remaining restrictions on corporations and unions paying for broadcast electioneering communications, the disclaimer and reporting requirements applicable to those messages also continue to apply. Currently, if a group spends an aggregate of $10,000 to produce and air electioneering communications, it must file FEC Form 9 (''24-Hour Notice of Disbursements/Obligations for Electioneering Communications'') within 24 hours of the advertisement's first airing. Whenever a group aggregates another $10,000 in electioneering communication spending (or commitments) during a calendar year and airs the message, it must file another such report within 24 hours.[50]

The Impact of *Citizens United* on Political Organizations

While the *Citizens United* ruling does not address the status of political organizations, they are at least indirectly affected in important ways. A political organization is generally exempt from taxation to the extent that it spends its funds on political and related activities, meaning, again, 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.[51]

Political organizations generally fall into one of three categories: (1) federal PACs that register with and report to the FEC but not with the IRS, and which, if they engage in state-election activities, also may have to register with and report to one or more state election agencies; (2) state PACs that seek to influence the election of state and local candidates and must register with and report to state election agencies, and usually must also register with, if not report to, the IRS; and (3) other section 527 organizations whose activities do not require

[43]11 C.F.R. sections 110.13(a), 114.4(f).

[44]*See* footnote 5, *supra*.

[45]*See generally* 11 C.F.R. section 114.10.

[46]*See* FEC News Release, ''FEC Statement on the Supreme Court's Decision in *Citizens United v. FEC*'' (Feb. 5, 2010), available at http://www.fec.gov/press/press2010/20100205CitizensUnited.shtml.

[47]FEC Form 5 Instructions, available at http://www.fec.gov/pdf/forms/fecfrm5i.pdf; 11 C.F.R. section 109.10.

[48]A ''public communication'' includes any communication by means of broadcast, cable, or satellite; newspaper or magazine ad; billboard or mass mailing; phone bank to the general public; or other form of general public political advertising. ''General public political advertising'' does not include communications over the Internet other than communications placed for a fee (such as pop-up and other types of ads) on another person's Web site. 11 C.F.R. section 100.26.

[49]11 C.F.R. section 110.11(c)(4).

[50]11 C.F.R sections 104.20(a) and 114.10(e)(1)(ii).

[51]Section 527(e)(2).

them to register with and report to any governmental campaign finance agency, and that, in most cases, both register with and report to the IRS.

Federal PACs are largely untouched by *Citizens United*. They remain subject to the same source restrictions and contribution limits as before, so they essentially remain dependent upon contributions from individuals and other federal committees. Federal PACs may make both in-kind and direct contributions to federal candidates and, in doing so, coordinate with them. Therefore, they remain specially and directly valuable sources of support for federal candidates, as well as national political parties. State PACs retain similar value with respect to state and local candidates and state parties.

Other political organizations — what are popularly if over-inclusively called ''527 groups'' — that are not registered with the FEC or any state election agency may now make federal independent expenditures and electioneering communications regardless of their sources of funds and, as before, they may receive unlimited donations from corporations and labor unions.

There remains a risk under FECA, however, that a section 527 group (or a section 501(c) group discussed earlier) will make independent expenditures and electioneering communications to a degree that will cause it to be treated as a federal PAC subject to the usual source restrictions and contribution limits. This risk arises because a federal PAC is any entity that receives contributions or makes expenditures in excess of $1,000 and whose ''major purpose'' is to influence federal elections.[52] The ''major purpose'' requirement is judicially constructed to avoid the statutory definition of a ''political committee'' capturing primarily non-political entities.[53] The FEC has not elaborated on that construction by regulation, but it has formally explained that it will look at a variety of contextual and behavioral factors beyond the making of contributions and express-advocacy communications in order to determine whether a particular group's conduct merits political committee status, such as a group's other kinds of spending that influences federal elections, solicitations of donations, its governing documents, descriptions of its mission and purposes, and other public statements.[54]

The *EMILY's List v. FEC* Decision and Political Organizations

In a decision that was somewhat overshadowed by *Citizens United*, a key federal appeals court last September invalidated FEC regulations adopted in 2005 that severely restricted the ability of ''non-connected'' federal PACs — that is, those not sponsored by a business or tax-exempt corporation or union, but instead formed and operated by individuals — and their nonfederal accounts to raise and spend money.[55] Even so, the decision's rationale also appears to eliminate similar constraints, to the extent they were applicable, on separate segregated funds.[56] The court also struck down restrictions on the ability of groups to raise funds with appeals that refer to specific federal candidates and elections.[57]

The 2005 rules required certain ''allocations'' of expenditures forcing federal PACs with nonfederal accounts to spend federal (''hard,'' or individually sourced and dollar-limited) funds rather than nonfederal (''soft,'' or unlimited and any-source) funds for public communications that mention a federal candidate, and for generic voter mobilization and routine administrative expenses. Specifically, the *EMILY's List* decision:

> Invalidated the 50 percent federal PAC minimum payment for generic voter drives, including voter registration, voter identification, and get-out-the-vote activities or other activities that urge the public to register, vote, or support candidates of a particular political party or associated with a particular issue, without even mentioning a candidate. Until the FEC adopts new rules, a nonfederal account may pay 100 percent of these costs.
>
> Invalidated the 100 percent federal PAC payment for communications that ''refer'' to federal candidates and do not contain express advocacy. Therefore, a nonfederal account may pay 100 percent of those costs.
>
> Invalidated the 50 percent federal PAC minimum payment for administrative costs that are common to both the federal and nonfederal accounts. Although the court recognized the FEC's authority to require some allocation of these costs, until the FEC adopts new rules it appears that the nonfederal account may pay 100 percent of those costs.

Emily's List and the FEC's recent advisory opinion are significant because the allocation rules particularly disadvantaged section 501(c) organizations that established separate segregated funds; if applicable, they forced these groups to finance a portion of these activities using limited federal PAC funds. Alternatively, if a group chose to pay for these expenses through its 501(c) accounts, it was potentially subject to tax under the section 527(f) tax discussed above.

---

[52]2 U.S.C. section 431(4)(A); *see also* Supplemental Explanation and Justification, ''Political Committee Status,'' 72 F.R. 5595, 5602 (Feb. 7, 2007) (''Supp. E & J'').

[53]*Buckley v. Valeo*, 424 U.S. 1, 79 (1976).

[54]*See, for example*, Supp. E & J, 72 F.R. at 5605.

[55]*Emily's List v. FEC*, 581 F.3d.1 (D.C. Cir. 2009).

[56]FEC Advisory Opinion 2009-23. The FEC advised that the allocation regulations under 11 C.F.R. Part 106 (that require certain entities that make disbursements in connection with federal and nonfederal elections to allocate expenses) do not apply to Sierra Club's Virginia PAC or Voter Education Fund, both separate segregated funds, because neither entity is a federal political committee.

[57]11 C.F.R. section 100.57. The 2005 rules restricted organizations, including section 501(c) and nonfederal section 527 organizations, in making fundraising solicitation messages. The regulations required all funds to be treated as federal ''contributions'' — that is, subject to FECA's contribution limits and source restrictions — if they were received as a result of a communication that ''indicates that any portion of the funds received will be used to support or oppose the election of a clearly identified Federal candidate.'' The *EMILY's List* decision invalidated these fundraising restrictions.

Conclusion

The full effect of *Citizens United* will become known during the next months and possibly years as the FEC and comparable state agencies address the Court's ruling. At the time of publication of this article, many bills had already been introduced in Congress to address the perceived effects of the ruling, and the FEC had begun to announce that it would cease enforcement of various newly invalid regulations and began to undertake rulemakings to consider how to conform other regulations to the new legal environment. Also, agencies in various states had initiated processes to review and adjust their own campaign finance laws.

But at publication there was no indication that the IRS would seek to clarify any of its regulations implementing sections 501(c) and 527 in order to provide greater certainty and predictability concerning the functionally interrelated federal campaign finance and federal tax legal regimes.