

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: Request for IRS investigation to determine whether “Crossroads GPS” is
operating in violation of tax status

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

² 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

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).

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).

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

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 <http://www.crossroadsgps.org/> (left sidebar) (last visited Sept. 30, 2010).

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

¹⁵ Jeremy P. Jacobs, *American Crossroads Airs Ads in OH, CO*, Hotline on Call, (August 17, 2010), at http://hotlineoncall.nationaljournal.com/archives/2010/08/american_crossr.php; see also Crossroads GPS website, at <http://www.crossroadsgps.org/video/bennet-calendar> (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 <http://www.publicintegrity.org/blog/entry/2359/> (last visited Sept. 30, 2010); see also Crossroads GPS website, at <http://www.crossroadsgps.org/video/issue-ad-robin-carnahan> (last visited Sept. 30, 2010).

¹⁷ See *American Crossroads Spin-off Launches New Ads in Missouri, Nevada*, *supra*; see also Crossroads GPS website, at <http://www.crossroadsgps.org/video/thanks-harry> (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 operated exclusively 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 primarily engaged 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)-1(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 direct or indirect participation or intervention in political campaigns 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 not primarily engaged in the promotion of the social welfare of the community and, therefore, is not 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) as long as it is primarily engaged in activities that promote social welfare[.]” 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 primarily 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. Your first and primary emphasis is on getting people elected to public office.

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

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 not 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

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

September 28, 2011

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: Request for IRS investigation into whether certain organizations
are ineligible for tax exempt status under section 501(c)(4).

Dear Commissioner Shulman and Director Lerner:

Democracy 21 and the Campaign Legal Center call on the Internal Revenue Service (IRS) to conduct an investigation into whether Crossroads GPS, Priorities USA, American Action Network and Americans Elect, all of which claim to be tax exempt groups organized under section 501(c)(4) of the Internal Revenue Code (IRC), 26 U.S.C. § 501(c)(4), are ineligible for the tax exempt status provided to section 501(c)(4) organizations.¹

Under the IRC, IRS regulations and court decisions interpreting the IRC, section 501(c)(4) organizations are required to primarily engage in the promotion of social welfare in order to obtain tax exempt status. Court decisions have established that in order to meet this requirement, section 501(c)(4) organizations cannot engage in more than an insubstantial amount of any non-social welfare activity, such as directly or indirectly participating or intervening in elections.

Thus, the claim made by some political operatives and their lawyers that section 501(c)(4) organizations can spend up to 49 percent of their total expenditures on campaign activity and maintain their tax exempt status has no legal basis in the IRC and is contrary to court decisions regarding eligibility for tax-exempt status under section 501(c)(4). An expenditure of 49 percent of a group's total spending on campaign activity is obviously far more than an insubstantial amount of non-social welfare activity.

¹ Last October, we asked for an investigation of Crossroads GPS on similar grounds. By this letter we re-state and supplement our earlier request for an investigation of Crossroads GPS.

The IRS applies the “primarily engaged” test on the basis of the “facts and circumstances” of an organization’s formation and operations. Here, we believe, the “facts and circumstances” show that each organization has engaged in far more than an insubstantial amount of participation or intervention in elections and that the overriding purpose of each organization is to influence elections.

Thus, under the IRC and court decisions interpreting the IRC, these organizations are not eligible to receive section 501(c)(4) tax exempt status.

In a 2008 Letter Ruling, the IRS stated that a group is not eligible for tax exempt status under section 501(c)(4) where the facts and circumstances show that the group’s “first and primary emphasis” is to get candidates elected to public office.

This standard is different than, and in conflict with, the standard applied by the courts. But even under this standard, we believe the “facts and circumstances” relating to the formation and activities of the four organizations discussed in this letter show that each group was organized and is operated for the overriding purpose of participating or intervening in elections.

Therefore, none of the four groups meets the standard for tax exempt status under section 501(c)(4) because they are not primarily engaged in “the promotion of social welfare.”

By claiming tax-exempt status under section 501(c)(4), these groups allow their donors to evade the public disclosure requirements that would apply if the organizations were registered under section 527 as “political organizations.” In fact, it appears that avoiding disclosure of their donors is the basic reason that these groups organized under section 501(c)(4).

Absent timely and appropriate action by the IRS, widespread abuses of the tax code by groups organized under section 501(c)(4) are likely to become commonplace in the 2012 presidential and congressional races. These abuses will come at the expense of the integrity and credibility of the tax laws and of the right of the American people to know the identity of the donors providing money to influence elections.

Accordingly, we request that the IRS promptly investigate the groups discussed in this letter and take appropriate enforcement action and impose appropriate penalties for any violations of section 501(c)(4) that the agency may find.

I. Crossroads GPS

On October 5, 2010, Democracy 21 and the Campaign Legal Center filed a letter with the IRS requesting an investigation into whether Crossroads GPS was operating in violation of the requirements for obtaining tax-exempt status under section 501(c)(4). Here, we supplement the information set forth in that earlier letter and continue our request for an investigation.

Crossroads GPS was organized in June, 2010 under section 501(c)(4) of the IRC “as an organization for the promotion of social welfare.” (“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 (FEC) 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. As a section 501(c)(4) organization, Crossroads GPS does not publicly disclose its donors.

An article in *Politico*, dated April 29, 2011, notes that Crossroads GPS was “founded under the guidance of GOP strategists [Karl] Rove and Ed Gillespie. . . .” and that it “accepts unlimited contributions from donors whose identities can be kept secret.”² The article notes:

In response to [the *Citizens United*] ruling, Rove and Gillespie helped form American Crossroads, which did disclose donors, and Crossroads GPS, which didn’t. During last year’s midterms, they raised a combined \$70 million, of which the donors of about \$43 million are still secret. The vast majority of that money was spent attacking Democratic candidates for the House and the Senate.

Id. According to another report:

Crossroads GPS took advantage of elements of the tax code to collect unlimited donations from individuals and corporations to spend tens of millions of dollars against Democratic candidates in the 2010 election.³

Another report noted that Crossroads GPS was formed for the very purpose of avoiding donor disclosure:

Meanwhile, section 501(c)(4) of the code, under which Crossroads GPS is incorporated, allows groups to shield their donors’ identities, but requires them to spend a majority of their cash on apolitical purposes – an obligation Democratic critics say Crossroads GPS and other right-leaning groups flaunted during the campaign, when they bombarded Democratic candidates with biting critical ads.

“Disclosure was very important to us, which is why the 527 was created,” Forti said. “But some donors didn’t want to be disclosed and, therefore, a (c)(4) was created,” Forti explained, referring to Crossroads GPS.

² J. Cummings, “New Dem money group takes on GOP,” *Politico* (April 29, 2011) (emphasis added).

³ M. O’Brien, “Obama alumni launch new outside group to boost reelection,” *The Hill* (April 29, 2011).

Forti's frank explanation differs from that previously offered by the Crossroads team, which had asserted that they always intended to create a 501(c)(4) because it was better suited to facilitate issue-based advocacy.⁴

A report in *The Wall Street Journal* discussed the plans of Crossroads GPS (and American Crossroads) to play a significant role in the 2012 elections:

Two conservative groups founded last year with the help of Republicans Karl Rove and Ed Gillespie have set a goal of raising \$120 million in the effort to defeat President Barack Obama, win a GOP majority in the Senate and protect the party's grip on the House in the 2012 election. . . .

If the conservative groups meet the target disclosed to *The Wall Street Journal*, they would establish their organizations – American Crossroads and Crossroads GPS – as possibly the largest force in the 2012 campaign, aside from the presidential candidates themselves and the political parties.⁵

According to another report, “‘2010 was only Crossroads’ opening act,’ Steven Law, the group’s president, told the Center for Public Integrity. These two groups hope to rake in \$120 million for 2012 compared to \$71 million last year.”⁶

In February, 2011, Crossroads GPS launched a radio ad campaign that was specifically designed to counter ads run by the Democratic Congressional Campaign Committee. According to one report:

Crossroads GPS, a 501(c)(4) group associated with GOP heavyweights Karl Rove and Ed Gillespie, is spending \$90,000 on radio ads in 19 districts where the Democratic Congressional Campaign Committee (DCCC) launched ads this week.

The group launched the ads to hit back against the DCCC ads, which accused the Republicans, many of whom are freshmen from swing districts, of wanting to slash spending for education and research and investment.⁷

⁴ K. Vogel, “SEIU, American Crossroads look back at 2010 spending,” *Politico* (Dec. 13, 2010) (emphasis added).

⁵ B. Mullins, “2012 Election Spending Race Heats Up,” *The Wall Street Journal* (March 1, 2011) (emphasis added).

⁶ P. Stone, “Democrats desperately seeking their own Rove,” *Center for Public Integrity –iWatch News* (March 14, 2011).

⁷ M. O’Brien, “Rove-backed group spends to bolster 19 targeted Republicans,” *The Hill* (Feb. 3, 2011).

Crossroads GPS also started to run ads attacking President Obama in key electoral battleground states:

In an early sign of its financial strength, Crossroads GPS announced Friday that it was launching a two-month, \$20 million television ad blitz attacking Obama's record on jobs, the deficit and the overall economy. The first ads will start June 27 and run in key battleground states such as Colorado, Florida, Missouri, Nevada and Virginia.⁸

A subsequent report stated that Crossroads GPS "is about midway through a two-month advertising binge attacking President Barack Obama and congressional Democrats that is expected to cost more than \$20 million, alone."⁹

President Obama announced his candidacy for re-election in the 2012 presidential race on April 4, 2011, well before the Crossroads GPS ads were run.

One report notes that Crossroads GPS is already spending money in Missouri as part of an effort to defeat Senator Claire McCaskill, who is up for reelection in 2012:

With nearly a year and a half to go before Election Day 2012, conservative-leaning national advocacy groups already have spent more than \$500,000 on advertising in Missouri in hopes of unseating incumbent Democratic Senator Claire McCaskill. . . .

The conservative groups, American Crossroads political action committee and its nonprofit affiliate, Crossroads GPS, already have hired southwest Missouri political operative Paul Mouton to help research and manage their efforts against McCaskill. Missouri is the only state with such an on-the-ground presence.

"As long as the race remains competitive, we will remain highly involved," said Jonathan Collegio, communications director for both groups. "Having someone on the ground in Missouri is a testament to how important we view this race."

When all is said and done, American Crossroads and Crossroads GPS expect to spend far and away more in Missouri than they did in 2010, when they spent around \$2.4 million opposing Democrat Robin Carnahan during her unsuccessful campaign for the U.S. Senate.¹⁰

⁸ P. Stone, "Obama groups raise \$4-5 million in first two months," *Center for Public Integrity-iWatch News* (June 24, 2011).

⁹ K. Vogel, "Both sides now in dash for anonymous cash," *Politico* (Aug. 9, 2011).

¹⁰ J. Hancock, "Both sides spending big to win Missouri Senate seat," *St. Louis Post-Dispatch* (Aug. 15, 2011).

Jonathan Collegio, the spokesman for Crossroads GPS and American Crossroads, said “Crossroads will continue to spend heavily in many competitive races through next November.”¹¹ According to this story, “‘The Crossroads groups have stated that we’ll be involved heavily in 2012, both in congressional races and the presidential side as well,’ Collegio said.” *Id.* (emphasis added).

Karl Rove, one of the founders of the Crossroads groups, was recently quoted at an appearance in Ohio as discussing their plans for campaign spending in Ohio in 2012:

Speaking with reporters before addressing an audience last night at Cedarville University, Rove said American Crossroads and its sister group, Crossroads GPS, view Ohio as the battleground where President Barack Obama must be stopped and where it is crucial to defeat incumbent Democratic Sen. Sherrod Brown to help Republicans take control of the Senate.

“Our objective is to be a strong presence in Ohio on the presidential contest, the Senate contest and wherever we might be needed in the House,” Rove said. “We raised \$72 million last time (in 2010); our goal is to raise \$250 million this time.”¹²

Another report indicates that the Crossroads groups may be shifting to emphasize spending through the section 501(c)(4) arm, Crossroads GPS. According to this report, “Crossroads Spokesman Jonathan Collegio said the group’s nonprofit arm, registered as a 501(c)(4) social-welfare organization by the IRS would be ‘more active’ than Crossroad’s main 527 group.”¹³

This may reflect the fact that Crossroads has been more successful in its fundraising of undisclosed contributions through the section 501(c)(4) arm. According to one report, the section 527 arm “has seen its fundraising lag behind its non-disclosing sister group. In the first six months of 2011, . . . it raised only \$3.9 million.”¹⁴

The same report described the evolution of the Crossroads groups as moving toward reliance on the section 501(c)(4) arm as a way to shield donors from disclosure:

[B]ack when Crossroads started out last year, it, too, shunned secret donations and extolled disclosure. Its chairman, Mike Duncan, described himself in May 2010

¹¹ D. Eggen, “Political groups, now free of limits, spending heavily ahead of 2012,” *The Washington Post* (May 21, 2011).

¹² J. Hallett, “Rove-affiliated PACs to spend big in Ohio,” *The Columbus Dispatch* (Sept. 21, 2011).

¹³ J. Gillum, “Priorities USA Raises \$5 Million to Counter Attack Ads From Karl Rove-Backed Crossroads GPS,” *Associated Press* (July 31, 2011).

¹⁴ K. Vogel, “Both sides now dash for anonymous cash,” *Politico* (Aug. 9, 2011).

as “a proponent of lots of money in politics and full disclosure in politics,” and said Crossroads intended to “be ahead of the curve on” transparency.

Less than one month later, with American Crossroads struggling to raise money from donors leery of having their names disclosed, operatives spun off Crossroads GPS, and its fundraising team, led by Rove, began emphasizing to prospective donors the ability to give anonymous contributions.

Fundraising took off, and together, the groups ended up raising more than \$70 in 2010, with the majority of it -- \$43 million -- going to Crossroads GPS.

Id.

On September 9, 2011, a published report stated that American Crossroads and Crossroads GPS have set a new fundraising goal that is at least twice the \$120 million announced earlier this year.¹⁵ According to the published report:

We see a pathway to at least doubling our earlier projected goal,” Steven Law, the president of Crossroads, told *iWatch News*. “Everyone is going to stretch as far as they can here because we all feel this is the most important election we have ever been involved with.”

To help achieve its new goal, the two groups have been talking to some prominent GOP figures, notably Mississippi Gov. Haley Barbour. The former Republican National Committee chairman has agreed to lend his Midas like rolodex to the Crossroads efforts.

“Gov. Barbour’s involvement with us gives us the capacity to focus on the presidential race, the Senate and the House at the same time,” Law said.

Id. (emphasis added).

II. Priorities USA.

Priorities USA announced its formation as a social welfare organization under section 501(c)(4) of the tax code by a memorandum distributed “to interested parties” on April 29, 2011. The memorandum makes clear that Priorities USA (and its companion section 527 political organization, Priorities USA Action), are intended to work for the reelection of President Obama by mimicking the structure and function of Crossroads GPS (and American Crossroads). According to the Priorities USA memorandum:

Our groups were formed to answer the hundreds of millions of dollars Karl Rove and the Koch brothers have dedicated to spending in the 2012 election. In 2010, Republicans spent millions distorting the debate on important issues and running

¹⁵ P. Stone, “Karl Rove-linked Crossroads has more than doubled its earlier fundraising goal of \$120 million,” *Center for Public Integrity- iWatch News* (Sept. 8, 2011).

vicious, dishonest attack ads. This is an effort to level the playing field and not allow right-wing activists to hijack the political system.¹⁶

One published report described Priorities USA as follows:

A group of Democrats aligned with the Obama administration today announced that they are starting an outside spending group similar to the conservative groups that President Obama has decried.

The new group has two arms: Priorities USA and Priorities USA Action. While one of the Priorities groups will disclose its donors, the other will not. The model is similar to that used by American Crossroads and Crossroads GPS, the conservative outside groups that raised more than \$70 million in the midterm election cycle to spend on behalf of candidates with a “conservative free-market legislative agenda.”¹⁷

Another report noted:

A group of leading Democrats, including some with close connections to the White House, have officially formed what are expected to be the major outside groups to combat Republicans – and support President Obama – in the 2012 elections with help from huge donations from big money donors and corporations who will have the legal ability to stay in the shadows that Mr. Obama has previously so vocally criticized.

The groups are to be called Priorities USA and Priorities USA Action, and, as such, are modeled after the Republican groups American Crossroads and Crossroads GPS that were started with help from the strategist Karl Rove and were credited with helping greatly in the party’s takeover of the House of Representatives this year – and, it happens, with facilitating a waterfall of anonymous donations from moneyed interests in the November elections.¹⁸

As another report noted:

Bill Burton and Sean Sweeney, two recently departed officials from the Obama White House, are forming Priorities USA, an organization that will seek to raise as much as \$100 million in the 2012 cycle. The group will consist of two branches: a 501(c)(4) nonprofit and a 527 political action committee. The

¹⁶ B. Smith, “In memo, Priorities USA defends secret-money shift,” *Politico* (April 29, 2011).

¹⁷ B. Montopoli, “Democrats launch outside spending group; conservatives charge hypocrisy,” *CBS News* (April 29, 2011).

¹⁸ J. Rutenberg, “Democrats Form Fund-Raising Groups,” *New York Times* (April 29, 2011).

structure will allow the organization to keep some of its donors secret, a practice that Democrats previously deplored when it was used by Republicans.¹⁹

The money raised by Priorities USA and its sister organization, Priorities USA Action, is described as intended to assist President Obama's reelection:

Two Democratic groups seeking big bucks to boost President Obama's re-election have tapped several high-powered fundraisers to help rope in \$4 million to \$5 million in the first two months. They've also snagged pledges for two to three times those sums towards their joint goal of raising at least \$100 million.

The two groups, Priorities USA Action and Priorities USA, are benefiting from the help of leading Democratic fundraisers and donors. . . .

Priorities USA Action is a 527 Super PAC which must disclose its donors and file quarterly reports, but Priorities USA, is a 501(c)(4) group that doesn't have to reveal its donors or file regular reports. Both groups can accept unlimited checks and under law must operate separately from the Obama campaign.²⁰

In discussing the spending plans of the Priorities USA organizations, Burton is quoted as emphasizing the impact on the election that the groups seek to have:

In response to "Rove's negative ads on the economy," Burton said, "we choose to invest in only swing states and, within those states, the most efficient television markets. Dollar for dollar, our spending is having a much greater impact on the voters who will decide the 2012 race."²¹

Another article about Priorities USA highlighted the fact that the group is expressly intended to counter the campaign activities of the Crossroads groups:

To fight his rivals, Burton has chosen to emulate them. His groups may take unlimited amounts, often from anonymous donors and will solicit money from political action committees, corporations and lobbyists that Obama's official election committee disavowed in 2008 and still shuns in the name of good government. . . .

¹⁹ A. Kornblut, "Democrats gear up to match GOP fundraising effort," *The Washington Post* (April 29, 2011).

²⁰ P. Stone, "Obama groups raise \$4-5 million in first two months," *Center for Public Integrity-iWatch News* (June 24, 2011) (emphasis added).

²¹ J. Gillum, "Priorities USA Raises \$5 Million to Counter Attack Ads From Karl Rove-Backed Crossroads GPS," *Associated Press* (July 31, 2011).

“The pool of money available to Karl Rove and the Koch brothers is bottomless and limitless,” said Paul Begala, a Democratic strategist who is advising Burton. [Pollster Geoff] Garin said Priorities USA “represents a way to level the playing field against Karl Rove and the Koch brothers”. . . .

Priorities USA and Priorities USA Action will focus on pointing to the weaknesses of Obama’s opponents, Burton said. The first advertisement criticized former Massachusetts Governor Mitt Romney, the Republican frontrunner in early polling, for supporting a Republican plan to convert Medicare into a system of vouchers to buy health insurance.²²

The same article makes clear that Priorities USA is part of a larger, coordinated campaign operation to support Democrats in the 2012 election:

The Priorities USA organizations, which will focus on the presidential race, will coordinate with three other newly formed Democratic groups: House Majority PAC will focus on House races, Majority PAC will concentrate on the Senate, and American Bridge 21st Century, will conduct opposition research on Republican candidates that other groups can use in advertising or direct mail literature.

Id. Press reports also indicate that the use of section 501(c)(4) organizations for spending is because of the anonymity offered to donors:

The three main anonymously funded Democratic outside groups – Priorities USA, American Bridge 21st Century Foundation and Patriot Majority – collected at least \$3.7 million in untraceable contributions, and probably much more, in the first half of the year, according to voluntary disclosures and anecdotal information on ad buys.

While that’s not as much as the \$5.8 million in fundraising reported in that same period by the sister organizations of those groups, which do disclose donors – Priorities USA Action, American Bridge 21st Century and Majority PAC – the feeling among some in Democratic fundraising circles is that the balance will likely tilt towards undisclosed donations as the groups seek to expand their donor bases. . . .

Many such donors “feel more comfortable donating to groups that don’t disclose,” [a strategist] said, because some are publicity adverse and also because “as soon as their name appears in the paper as having contributed, their phone number goes on the speed dial of every congressman, committee and party that wants to raise money.”²³

²² A Fitzgerald, “Rove Tops President Obama as Drawing Card in Democrat Burton’s Fundraising,” *Bloomberg News* (June 29, 2011).

²³ K. Vogel, “Both sides now in dash for anonymous cash,” *Politico* (Aug. 9, 2011).

III. American Action Network.

American Action Network (AAN) was founded in 2010 by Fred Malek, a leading national Republican fundraiser, and is chaired by former Republican Senator Norm Coleman. According to published reports, AAN shares offices with Crossroads GPS and other related groups.²⁴ AAN made numerous independent expenditures in the 2010 elections. For instance, according to one report:

[A] so-called Section 501(c)(4) group called American Action Network filed an independent expenditure report with the FEC Aug. 5 [2010] indicating that it is spending nearly \$435,000 for cable television and radio ads in the New Hampshire campaign for an open U.S. Senate seat. . . .

The new ad campaign attacks the Democratic Senate candidate, Rep. Paul Hodes (D-N.H.), and supports Republican Senate candidate Kelly Ayotte, New Hampshire's former attorney general.

The American Action Network has indicated on its website that it also sponsored ad campaigns focused on Senate races in Washington state and Florida; however, it filed no reports with the FEC on its spending in those states. The group indicated in press releases that it considered its efforts in these races to be "issue advocacy" not subject to any FEC reporting rules.

The ads that the American Action Network sponsored in Washington included an image of tennis shoes purportedly worn by Sen. Patty Murray (D-Wash.) stepping on the backs of business owners, taxpayers and children. The ad ends by telling Murray that "it's time you got off our backs."²⁵

Another report states:

While the group was intended to serve largely as a policy shop to rival the liberal Center for American Progress, it has mainly just been cutting ads attacking Democrats (including Feingold) who are currently engaged in tight races.

In addition to infusing hundreds of thousands of dollars in outside cash into Feingold's Wisconsin race, Coleman's group has also spent \$750,000 targeting Sen. Patty Murray (D-Wash.) in her tight contest against Republican Dino Rossi and \$450,000 attacking Senate candidate Rep. Paul Hodes (D) in New Hampshire. And because it is incorporated as a 501(c)(4) "social welfare" nonprofit, the D.C.-

²⁴ H. Bailey, "A guide to the shadow GOP": the groups that may define the 2010 and 2012 elections," *Yahoo News-The Upshot* (August 5, 2010).

²⁵ K. Doyle, "Campaign Spending Reports Filed with FEC," *BNA Money in Politics Report* (Aug. 12, 2010).

based AAN does not publicly disclose its donors and has not listed any contributors on the independent expenditure forms it is obliged to file with the FEC.²⁶

In addition to spending on Senate races, in 2010, American Action Network also spent on “really tight” House races:

The [Wall Street] Journal reported that American Action Network will air \$1.7 million in ads boosting the cash-strapped bids of Republicans Ryan Frazier, who is taking on Democratic Rep. Ed Perlmutter (D-Colo), and Jackie Walorski, who is challenging Democratic Rep. Joe Donnelly (D-Ind.). . . .

“The American Action Network has carefully calibrated really tight house races where there are candidates who strongly support our views of limited government and reduced deficits or on the other side candidates who really oppose our views,” said the group’s chairman, veteran GOP fundraiser Fred Malek.²⁷

American Action Network shares space with American Crossroads and Crossroads GPS, and according to press reports, the groups coordinate their political activities:

Sometimes that coordination is as easy as walking across the hall. Sharing office space with American Crossroads is the American Action Network (AAN), a group led by former Minnesota Senator Norm Coleman, a Republican, which may spend up to \$25 million this year. Originally billed as a conservative think tank, the AAN has increasingly turned to raw politics, having spent more than \$1 million on ad buys targeting Democrats such as Senators Patty Murray in Washington and Russ Feingold in Wisconsin. (“We definitely can’t afford him,” an AAN ad says of Feingold and his alleged free-spending record).²⁸

The coordinated focus that American Action Network had on influencing the 2010 elections is illustrated by this quote from Rob Collins, the president of the organization, shortly before the 2010 election:

Many of the conservative groups say they have been trading information through weekly strategy sessions and regular conference calls. They have divided up races to avoid duplication, the groups say, and to ensure that their money is spread around to put Democrats on the defensive in as many districts and states as possible – and more important, lock in whatever gains they have delivered for the Republicans so far.

²⁶ J. Zwick, “Coleman’s American Action Network Infuses Cash into Close Senate Races,” *Washington Independent* (Oct. 4, 2010).

²⁷ K. Vogel, “Rove: Obama’s attacks are helping,” *Politico* (Oct. 13, 2010).

²⁸ M. Crowley, “The New GOP Monday Stampede,” *Time* (Sept. 16, 2010).

“We carpet-bombed for two months in 82 races, now it’s sniper time,” said Rob Collins, president of American Action Network, which is one of the leading Republican groups this campaign season and whose chief executive is Norm Coleman, the former Senator from Minnesota. “You’re looking at the battle field and saying, ‘Where can we marginally push – where can we close a few places out?’”²⁹

According to one report published after the 2010 election, American Action Network “ended up with Republican victories in about 56 percent of the contests it invested in.”³⁰

As one report notes, “Republican political operatives bestow immense credit for their party’s competitiveness in 2010 on organizations such as Crossroads GPS and the American Action Network, both 501(c)(4) organizations. These groups can accept large donations that they do not have to disclose. . . .”³¹

American Action Network, like Crossroads GPS, also spent to influence a special congressional election in May, 2011. According to a published report, American Action Network spent \$94,694 on an election in the New York 26th congressional district.³²

In other spending in 2011, American Action Network has undertaken a \$1 million direct mail and newspaper campaign that “charges Democrats with attempting to ‘balance the budget on the backs of seniors’ . . .”³³ The mail campaign “will reach 22 congressional districts in 14 states, all of them represented in Congress by Republicans. . . . Most of the 22 are freshmen first elected in November 2010.” *Id.* According to another news report, the group subsequently “added 10 vulnerable freshmen House Republicans to its advocacy campaign defending Republicans on Medicare.”³⁴ According to this report, the mailing sent to one Florida congressional district reads, “Florida seniors can count on Congressman Allen West to stand up against the Obama Medicare plan.” *Id.*

²⁹ J. Rutenberg, “Pro-Republican Groups Prepare Big Push at End of Races,” *New York Times* (Oct. 25, 2010).

³⁰ M. Luo and G. Palmer, “Who Got the Most Bang for their Bucks?” *New York Times* (Nov. 4, 2010).

³¹ A. Becker and D. Drucker, “Members Weigh In on Draft Disclosure Order,” *Roll Call* (May 24, 2011).

³² P. Overby, “Outside Groups Spend Big in N.Y. Special Election,” *NPR* (May 25, 2011).

³³ A. Burns, “Ads to back GOPers on Medicare,” *Politico* (July 27, 2011).

³⁴ C. Joseph, “Conservative group defending 10 more House Republicans on Medicare,” *The Hill* (Aug. 3, 2011).

IV. Americans Elect

Americans Elect was initially organized as a “political organization” under section 527 of the tax code, but in October, 2010 changed its designation to a “social welfare” organization under section 501(c)(4) of the tax code.³⁵ It is seeking to gain a place on the 2012 ballot in all 50 states for a presidential candidate it intends to nominate.

According to one article, “Its mission is to upend the traditional party primary process by selecting an alternate presidential ticket through an online, open nominating convention.” *Id.* This report also notes that the manner in which the group is pursuing its aims:

. . . is highly unorthodox. Although it is attempting to qualify as a new party in California and other states, the group’s legal designation is that of a nonpolitical, tax exempt social welfare organization.

Under that designation, Americans Elect has been able to keep private its financiers, raising questions about what forces are driving the massive undertaking. The group has labored largely under the radar for the last 16 months, raising \$20 million while successfully gaining ballot access in Arizona, Alaska, Kansas and Nevada. It is seeking certification in Michigan, Hawaii, Missouri and Florida besides California, with an additional 18 states in the pipeline before the end of the year.

Id. According to the same article, Americans Elect has raised \$20 million, with no contribution exceeding \$5 million. The report noted, “Elliot Ackerman said Americans Elect does not take any money from special interests or political action committees, adding that it is up to donors to determine whether they want to be identified.” *Id.*

The same article notes that the organization plans to nominate a candidate for president:

Americans Elect now plans to hold an online convention in June 2012 that will be open to any registered voters who sign up. They will select a presidential ticket from a slate of candidates, all of whom will have been required to pick a running mate from a different political party.

Id. Another article described Americans Elect as follows:

Funded with at least \$20 million, the majority from large, mostly unnamed donors, Americans Elect is vying to become the most serious third-party insurgency since industrialist H. Ross Perot nearly upended the 1992 presidential campaign.³⁶

³⁵ M. Gold, “Americans Elect seeks to upend primary system,” *Los Angeles Times* (July 28, 2011).

³⁶ P. Jonsson, “Americans Elect launches centrist third-party bid amid Washington dysfunction,” *Christian Science Monitor* (July 29, 2011).

In an opinion piece published by *Politico*, Elliot Ackerman, the group's chief operating officer, described the group's purposes as follows:

We have set up a non-partisan nominating process for the presidency. We plan to hold a secure online convention in June 2012, where any registered voter can participate as a delegate. At this national convention, party functions will become delegate functions. The delegates will draft candidates; develop a platform of questions the candidates must answer, and discuss and debate the convention rules.

We are on our way, with our ballot access initiative, to ensure that our presidential ticket can be on the ballot in all 50 states... .

The Americans Elect nominating convention will be the first time that American voters have gained direct access to the ballot to nominate and elect a presidential candidate.³⁷

According to *The Arizona Daily Star* on July 30, 2011, "Americans Elect was recognized last week as a new political party by the state of Arizona and is eligible to have its presidential nominee on the ballot in the 2012 elections."³⁸

According to *The Detroit Free Press* on September 9, 2011, "Bureau of Elections spokesman Fred Woodhams said American Elect submitted nearly 68,000 petition signatures in May, more than double the 32,261 needed to qualify for the Michigan ballot as a minor party."³⁹

According to *The Oregonian* on September 19, 2011, Americans Elect "has already qualified for the ballot in six states and appears to have turned in enough signatures -- more than 1.6 million -- to make the 2012 ballot in California."⁴⁰

As these examples show, American Elect is not only devoted to intervening in the 2012 elections, it is actually qualifying itself as a political party for purposes of state ballot access laws. A political party is not eligible to qualify as a section 501(c)(4) tax exempt organization.

³⁷ E. Ackerman, "An online political convention," *Politico* (Aug. 10, 2011).

³⁸ M. Casey, "Americans Elect party to appear on '12 ballot," *Arizona Daily Star* (July 30, 2011).

³⁸ D. Bell, "State to vote on certifying new group with 2012 presidential hopes," *The Detroit Free Press* (Sept. 9, 2011) (emphasis added).

⁴⁰ J. Mapes, "New effort to establish centrist presidential campaign seeks to qualify for Oregon ballot," *The Oregonian* (September 19, 2011)

V. The IRS Should Investigate Whether Each Organization Is Ineligible for Section 501(c)(4) Tax Status Because Each Is Engaged In More Than An Insubstantial Amount of Campaign Activity.

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 operated exclusively 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 primarily engaged 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).

Political activity – spending to influence campaigns – does not constitute promoting social welfare. Section 1.501(c)(4)–1(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 direct or indirect participation or intervention in political campaigns 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).

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) as long as it is primarily engaged in activities that promote social welfare.” Rev. Rul. 81–95, 1981–1 C.B. 332 (emphasis added).

B. Section 501(c)(4), as construed by the courts, does not permit a “social welfare” organization to engage in more than an insubstantial amount of campaign activity.

Section 501(c)(4), as construed by the courts, does not permit a group organized under that section to engage in more than an insubstantial amount of campaign activity and still qualify for tax exempt status.

According to court decisions, the statutory requirement for a section 501(c)(4) organization to be “operated exclusively” for “the promotion of social welfare” means that the organization cannot engage in more than an insubstantial amount of activity that is not in furtherance of its social welfare function. This means that section 501(c)(4) organizations cannot engage in more than an insubstantial amount of campaign activities.

The “insubstantial” standard established by the courts certainly does not allow a section 501(c)(4) organization to spend up to 49 percent of its total expenditures in a tax year to participate or intervene in elections and still maintain its tax-exempt status, as some practitioners believe.

Under the statutory language of section 501(c)(4), a social welfare organization must be “operated exclusively” for social welfare purposes. The courts have interpreted this “operated exclusively” standard the same way they have interpreted a parallel provision of section 501(c)(3) that requires an organization that is tax exempt under that provision to be “organized and operated exclusively” for charitable, education or similar purposes.

In *Better Business Bureau v. U.S.*, 326 U.S. 279, 283 (1945), the Supreme Court construed a requirement that a non-profit organization be “organized and operated exclusively” for educational purposes to mean that “the presence of a single non-educational purpose, *if substantial in nature*, will destroy the exemption regardless of the number or importance of truly educational purposes.” (emphasis added).

Based on the *Better Business Bureau* decision, the courts have concluded that the word “exclusively” in the context of sections 501(c)(3) and 501(c)(4) is “a term of art” that does not mean “exclusive” as that term is normally understood and used.

The courts instead have said that, in the context of section 501(c)(4) of the IRC, this term means “that the presence of a single substantial non-exempt purpose precludes tax-exempt status regardless of the number or importance of the exempt purposes.” *Contracting Plumbers Coop. Restor. Corp. v. U.S.*, 488 F.2d 684, 686 (2d. Cir. 1973) (section 501(c)(4)); *American Ass’n of Christian Sch. Vol. Emp. v. U.S.*, 850 F.2d 1510, 1516 (11th Cir. 1988) (“the presence of a substantial non-exempt purpose precludes exemption under Section 501(c)(4)”); *Mutual Aid Association v. United States*, 759 F.2d 792, 796 (10th Cir. 1985) (same; section 501(c)(4)).

The courts have similarly held, in the context of section 501(c)(3) organizations, that the “operated exclusively” test means that “not more than an insubstantial part of an organization’s activities are in furtherance of a non-exempt purpose.” *Easter House v. United States*, 12 Ct. Cl. 476, 483 (1987) (group not organized exclusively for a tax exempt purpose under section 501(c)(3)); *New Dynamics Foundation v. United States*; 70 Fed. Cl. 782, 799 (Fed. Cl. Ct. 2006) (same); *Nonprofits Ins. Alliance of California v. U.S.*, 32 Fed. Cl. 277, 282 (Fed. Cl. Ct. 1994) (same).

Under these court rulings, a section 501(c)(4) organization cannot engage in more than an insubstantial amount of campaign activity and remain in compliance with the statutory requirements for tax-exempt status under section 501(c)(4). Any “substantial, non-exempt purpose” (such as campaign activity) will defeat an organization’s tax-exempt status under section 501(c)(4). *Christian Sch. Vol. Emp.*, *supra* at 1516.

There is nothing, furthermore, in these rulings, in IRS regulations or in other IRS actions to support the proposition that spending 49 percent of total expenditures on campaign activities constitutes an insubstantial amount of non-exempt activity.⁴¹

⁴⁰ On July 27, 2011, Democracy 21 and the Campaign Legal Center filed a petition for rulemaking with the IRS which seeks revisions in the regulations implementing section 501(c)(4). In particular, the petition contends that the “primarily engaged” standard in section 1.501(c)(4)-1(a)(2)(i) does not correctly

C. Political campaign activity not limited to “express advocacy” communications under the Internal Revenue Code.

IRS regulations 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. Thus, so-called “issue ads” that promote, attack, support or oppose a candidate fall with the meaning of direct or indirect participation or intervention in political campaigns.

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 political activities and activities to promote social welfare. The IRS Revenue Ruling 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 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

implement the statutory “operated exclusively” standard in section 501(c)(4) of the IRC, as interpreted by the courts.

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, even if an ad discussing an issue does not express advocacy, it may nonetheless be treated as “exempt function” electioneering activity under IRS regulations, depending on the “facts and circumstances.” Therefore, even where an ad discusses an “issue,” and where 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 the promotion of social welfare.

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. These factors are not in themselves dispositive. In the end, the regulations require a determination to be made based on “the facts and circumstances” of each advertisement.

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 “facts and circumstances” test, each of the organizations discussed in the letter is engaged more than an insubstantial amount of campaign activity and, in fact, is primarily engaged in activities for the purpose of participating and intervening in political campaigns.

In the case of Crossroads GPS and American Action Network, both organizations were created just months before the 2010 congressional elections, and were conceived, organized and staffed by leading political party strategists and operatives. Both organizations defined their activities as spending money to influence the 2010 House and Senate races, and both were closely affiliated with other organizations similarly spending large sums to influence the 2010 elections.

The activities of both groups were targeted to battleground states involving key congressional races, and to supporting Republican candidates or opposing Democratic candidates in those elections.

The ads run by both organizations identified candidates by name, discussed their position on issues in the midst of a campaign, and did so in ways that supported those candidates or criticized their opponents.

Finally, the timing of the groups’ activities did not correspond with external events outside the control of the groups, such as a legislative vote on an issue, but rather corresponded with congressional election campaigns.

With regard to Priorities USA, statements by the founders of the organization make clear that it is modeled on Crossroads GPS, and is to play a similar function with the overriding purpose of conducting campaign activities to support the re-election of President Obama.

Finally, with regard to Americans Elect, the sole thrust of the organization is to obtain

ballot access to use to nominate candidates for president and vice president. The organization is qualifying on ballots as a political party. These activities are *per se* campaign activities in connection with an election.

Accordingly, each of the section 501(c)(4) organizations discussed above has engaged in more than an insubstantial amount of campaign activity, has a “substantial, non-exempt purpose” of participating or intervening in elections and is not entitled to tax-exempt status under section 501(c)(4).

VI. The IRS Also Should Investigate Whether Each Organization Is Ineligible for Section 501(c)(4) Tax Status Because the Organization Is “Primarily Engaged” in Campaign Activity

In a 2008 Letter Ruling, the IRS applied the “primarily engaged” standard to mean that a section 501(c)(4) organization’s primary activities cannot constitute direct or indirect political intervention.

This interpretation of the statutory standard is in conflict with the court rulings interpreting section 501(c)(4), discussed above, that require an exempt organization to engage in no more than an insubstantial amount of campaign activity.

Nevertheless, the organizations discussed in this letter also fail to comply with the standard set forth in this Revenue Ruling. In the 2008 Ruling, the IRS found an organization did not qualify for tax exempt status under section 501(c)(4) because it was not primarily engaged in promoting “social welfare.” 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. Your first and primary emphasis is on getting people elected to public office.

Id. 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.

Id.

Here, we believe that an IRS investigation will show that the "first and primary emphasis" of each of the four organizations discussed above is "on getting people elected to public office." In particular, the IRS should investigate whether the "facts and circumstances" show that each of the organizations discussed in the letter is primarily engaged in activities which constitute direct or indirect participation or intervention in political campaigns under IRS regulations. For reasons discussed above, we believe each organization has overriding purpose to engage in campaign activities, and thus is operating contrary to the requirements of section 501(c)(4).

VII. Conclusion.

In the 2010 congressional races, section 501(c) organizations spent more than \$135 million on campaign activities that were financed by secret contributions. The bulk of these expenditures were made by section 501(c)(4) organizations. The amount of secret contributions funding campaign expenditures by section 501(c)(4) organizations is expected to grow dramatically in the 2012 presidential and congressional races.

Crossroads GPS, Priorities USA, American Action Network and Americans Elect are each organized under section 501(c)(4) of the Internal Revenue Code. Based on the information about each organization set forth above, the IRS should conduct an investigation of whether each such organization has engaged in more than an insubstantial amount of non-exempt activity by participating or intervening in political campaigns and accordingly is not primarily engaged in the promotion of social welfare. The IRS should also conduct an investigation of whether each organization's primary activity is campaign activity and is accordingly not primarily engaged in the promotion of social welfare.

If the IRS investigation determines that the facts and circumstances show that the organizations discussed above are not primarily engaged in "the promotion of social welfare," because they have engaged in more than an insubstantial amount of campaign activity or because the organization's primary activity is campaign activity, the organizations should be denied or should lose tax-exempt status. In addition, appropriate penalties should be imposed by the IRS for violations the agency finds. The penalties should take into account the need for strong deterrence to stop similar violations from occurring in the future.

Sincerely,

/s/ Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

December 14, 2011

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: Request for IRS investigation into whether certain section 501(c)(4) organizations are operating in violation of tax exempt status

Dear Commissioner Shulman and Director Lerner:

We are writing to supplement our letter to the Internal Revenue Service of September 28, 2011.

In the September 28th letter, Democracy 21 and the Campaign Legal Center called on the IRS to investigate whether four organizations – Crossroads GPS, the American Action Network, Americans Elect and Priorities USA – are operating in violation of their claimed tax-exempt status under section 501(c)(4) of the Internal Revenue Code because each organization is engaging in far more political activity than the Code allows for “social welfare” organizations.

These groups are claiming section 501(c)(4) tax status in order to keep secret from the American people the donors financing their expenditures to influence federal elections

We previously wrote to the IRS on October 5, 2010 asking for an investigation of Crossroads GPS and its eligibility to receive section 501(c)(4) tax status. We also wrote to the IRS on July 27, 2011 challenging the IRS regulations on eligibility for section 501(c)(4) tax status as not properly implementing the law.

We are writing today to provide additional information on the political activities of three of the four groups addressed in our September 28th letter, the American Action Network, Americans Elect and Crossroads GPS that further demonstrates that these groups are not entitled to section 501(c)(4) tax-exempt status.

As you are aware, section 501(c)(4) “social welfare” organizations are not required to disclose their donors to the public. If the four organizations discussed in our September 28th letter are not eligible for the tax status they claim under section 501(c)(4), then they are improperly shielding their donors from public disclosure and improperly using secret contributions to influence the 2012 national elections.

We are deeply concerned about the failure of the IRS to take any public steps to show that the agency is prepared to enforce the tax laws applicable to section 501(c)(4) tax-exempt groups.

Since bringing these abuses of the tax laws to your attention, beginning more than a year ago, we have seen no evidence that the IRS is prepared to address what appear to be blatant abuses in order to keep secret from the American people the sources of money being spent to influence federal elections.

The failure of the IRS to carry out its statutory enforcement responsibilities to prevent the abuse of the tax laws could have a major impact on the 2012 elections, as we have stated in our previous letters to the IRS.

We urge the IRS in the strongest possible terms to expeditiously examine the matters we have brought to its attention and to address any possible abuses and violations of the tax laws before it is too late.

As our prior letters state, section 501(c)(4) “social welfare” organizations are required to primarily engage in the promotion of social welfare in order to obtain tax exempt status. Federal court decisions have established that in order to meet this requirement, section 501(c)(4) organizations cannot engage in more than an *insubstantial* amount of any non-social welfare activity, such as directly or indirectly participating or intervening in elections.

In our letter of September 28, 2011, we provided voluminous information demonstrating that each of the four organizations discussed in the letter are engaging in *substantial* campaign-related activity. Indeed, the facts relating to the formation and activities of the four organizations show that each group was organized and is operated for the overriding purpose of participating or intervening in elections.

By claiming tax-exempt status under section 501(c)(4), these groups allow their donors to evade public disclosure requirements that would apply if the organizations were registered under section 527 as “political organizations.” In fact, it appears that avoiding disclosure of their donors is the reason that these groups have claimed section 501(c)(4) tax status.

American Action Network

An article from the Center for Public Integrity’s *iWatch News* (October 31, 2011) reported that American Action Network spent \$30 million in 2010. According to the article and federal campaign finance reports, \$26 million of the \$30 million spent by American Action

Network in 2010 was spent for “independent expenditures” and “electioneering communications,” as defined by federal campaign finance laws. The article states:

The conservative American Action Network, a leading independent player in last year’s election, poured \$26 million – out of some \$30 million in spending – from secret donors into political ads and activities to help Republican candidates. . . .

As required by law, the network reported the \$26 million it spent on political activities to the Federal Election Commission before Election Day.¹

This means that 87 percent of American Action Network’s expenditures in 2010 were made for campaign-related activities reported to the FEC under the nation’s campaign finance laws. The article states:

“If over 80 percent of a group’s expenditures are for political purposes that require reporting to the FEC, then that organization will not qualify for tax-exempt status under section 501(c)(4),” Marc Owens, who was director of the IRS exempt organizations division for a decade, told *iWatch News*.

Under no one’s understanding of the tax laws is an organization eligible for section 501(c)(4) tax-exempt status if 87 percent of its expenditures are made for campaign-related activities reported under the nation’s campaign finance laws.

Based on these facts, the IRS must move promptly in order to stop American Action Network from again abusing the tax laws in the 2012 elections.

According to the *iWatch News* article, former Senator Norm Coleman, the chairman of American Action Network, is quoted as stating that the group will be heavily involved in spending to influence the 2012 congressional campaign. If the IRS does not take action, it could be responsible for allowing campaign-related expenditures by American Action Network that are improperly financed with secret contributions to influence and possibly decide the outcome of targeted House and Senate races.

Americans Elect

Americans Elect, which we also addressed in our September 28th letter, continues to qualify for ballot access as a political party in states throughout the nation in order to run a presidential/vice-presidential candidate ticket in 2012. The organization is claiming section 501(c)(4) status in order to keep its donors secret from the American people.

A recent news story stated that Americans Elect “has raised \$22 million and is likely to place a third presidential candidate on the ballot in every state next year.”² According to this

¹ P. Stone, “Fine line between politics and issues spending by secretive 501(c)(4) groups,” *iWatch News* (Oct. 31, 2011).

article, Americans Elect “has ballot slots in Florida, Michigan, Nevada, Ohio and five other states, with certifications pending in several others.”

According to a recent *POLITICO* article, “Americans Elect this week announced that it qualified for the ballot in Colorado and Mississippi, bringing the total number of states in which it has access to 11 – including Alaska, Arkansas, Arizona, Kansas, Nevada, Michigan, Florida, Ohio and Utah. Certification is pending in California and Hawaii.”³

The notion that this group qualifies as a section 501(c)(4) “social welfare” organization is absurd.

A group legally qualified in states as a political party in order to obtain ballot access to run a candidate for president cannot simultaneously be a tax-exempt “social welfare” organization under section 501(c)(4).

In this particular case, the failure of the IRS to act could have enormous consequences.

Just as third party candidates decided the 2000 presidential race, a third party candidate representing Americans Elect could decide the outcome of the 2012 presidential election. If that were to happen and the IRS has failed to take action here, the agency would be responsible for allowing secret money and a secretly financed organization to decide who is elected to be our next president.

The IRS must not allow this to happen. The agency must move immediately to address the apparent abuses of the tax laws.

Crossroads GPS

As we demonstrated in our September 28th letter, the overriding purpose of Crossroads GPS is to influence elections. In engaging in its campaign-related activities, Crossroads GPS works in tandem with American Crossroads, a so-called Super PAC, to elect Republicans and defeat Democrats running for federal office. That is the organization’s purpose and that is what the organization is spending its money to do.

According to published reports, American Crossroads and its affiliated organization Crossroads GPS plan to spend a combined \$240 million to influence the 2012 presidential and congressional elections.

² K. Thompson, “Moderate Americans Elect group hoping to add third candidate to 2012 election ballot,” *The Washington Post* (November 24, 2011).

³ T. Mak, “Christine Todd Whitman to Jon Huntsman: Run third party,” *POLITICO* (December 2, 2011)

Based on the Internal Revenue Code, court decisions and even the flawed IRS regulations, Crossroads GPS is not entitled to the section 501(c)(4) tax-exempt status it has claimed in order to hide its donors. This is another clear case that demands prompt action.

A recent article in *The New York Times* shows that Crossroads GPS is continuing to spend substantial amounts of money to influence federal elections. According to the article:

Crossroads GPS, a conservative advocacy group founded by Mr. Rove and other Republican strategists, has placed the biggest bet so far on negative messages. By its own count, it has spent about \$20 million this year on political advertising. Much of its was broadcast during the debt-ceiling debate this summer, when it singled out members of Congress with advertisements that portrayed Democrats and Mr. Obama as fiscally irresponsible and unable to fix the economy.

In recent weeks, the group has taken on Mr. Obama and his economic agenda, spending \$2.6 million on a commercial that criticizes his support for an upper-income tax increase and suggests a split on the issue between Mr. Obama and former President Bill Clinton. . . .

Many of the Crossroads advertisements have been running in swing states like Colorado, Florida, Ohio and Pennsylvania and have been timed to coincide with presidential trips.

“It creates a scenario where the president’s visit is greeted with a strong counterpoint to the argument he’s making,” said Jonathan Collegio, communications director for Crossroads GPS.

“And in battleground states where the issue framing is going to impact 2012, it’s critical to be making your point there early and often,” Mr. Collegio said. “There may be some value in advertising now that will be impossible to achieve toward the end of the campaign, when virtually all of the advertising on television and radio is political.”⁴

Similarly, a recent article in *National Journal* reported that Crossroad GPS has recently “reserved more than \$500,000 on air time in Nebraska’s two largest media markets,” to run ads that are for the purpose of dissuading Senator Ben Nelson (D-NE) from running for reelection.⁵ According to the article:

“We want Ben Nelson to recognize that 2012 will be an extraordinarily grueling proposition in the case he decides to run,” said Jonathan Collegio, a Crossroads spokesman, in confirming the buy.

⁴ J. Peters, “TV Attack Ads Aim at Obama Early and Often,” *The New York Times* (November 26, 2011) (emphasis added).

⁵ R. Wilson, “Crossroads Will Drop Half Million Against Nelson,” *National Journal* (Dec. 12, 2011).

Crossroads began the two-week blitz last week with a spot blasting Nelson's vote in favor of health care reform legislation. *Id.*

The statement by the spokesman for Crossroads GPS makes clear that it is intending to make Senator Nelson's year "grueling," should he decide to run for re-election. The campaign focus of Crossroads GPS's activities could not be more overt.

In failing to properly enforce the tax laws that apply to section 501(c)(4) groups, the IRS is failing the American people.

The IRS is also creating the potential for this illegal activity to play a major role in influencing and possibly determining the outcome of the 2012 presidential election and individual congressional races.

We reiterate our request that the IRS move promptly to address whether the organizations detailed in our September 28th letter are improperly claiming tax-exempt status under section 501(c)(4) and are improperly using that status to keep secret the donors to these groups whose contributions are being spent to influence federal elections.

The IRS has an obligation to the American people to properly enforce the tax laws and thereby to protect the integrity of our elections. Democracy 21 and the Campaign Legal Center strongly urge the IRS to meet its obligation.

Sincerely,

/s/ Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

March 9, 2012

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: Request for IRS investigation into whether certain section 501(c)(4)
organizations are operating in violation of tax-exempt status

Dear Commissioner Shulman and Director Lerner:

On September 28, 2011, Democracy 21 and the Campaign Legal Center called on the IRS to conduct an investigation into whether four groups claiming tax-exempt status under section 501(c)(4) of the Internal Revenue Code are ineligible for exemption under that provision because they are substantially engaged in campaign activities, not social welfare activities. The groups discussed in our letter are Crossroads GPS, Priorities USA, American Action Network and Americans Elect.

On December 14, 2011, we supplemented our request by providing additional information about the campaign activities conducted by three of these groups.

According to an article in *The New York Times* on March 6, 2012:

In recent weeks, the I.R.S has sent dozens of detailed questionnaires to Tea Party organizations applying for nonprofit tax status, demanding to know their political leanings and activities. The agency plans this year to press existing nonprofits like American Crossroads, on the Republican side, and Priorities USA, on the Democratic side, to justify their tax-protected status as “social welfare” organizations, a status that many tax professionals believe is being badly abused.¹

¹ J. Weisman, “Scrutiny of Political Nonprofits Sets Off Claim of Harassment,” *The New York Times* (March 6, 2012). We believe the reference in the article to American Crossroads, which is a

The *Times* article also stated that there is “pushback” against any investigation by the IRS of whether groups that may be engaged in campaign-related activities are entitled to 501(c)(4) tax-exempt status, and that such resistance is likely to be “fierce.” According to one attorney quoted in the article, the IRS is engaged in “‘McCarthyism’ tactics” and its investigation is “a coordinated effort by the I.R.S. . . . to stifle free speech activities.”

We strongly urge the IRS not to succumb to such arguments, or to any public or political pressure to back away from carrying out the agency’s statutory responsibilities to enforce the tax laws.

The IRS must enforce the law fairly and without partisan bias. The agency also must not shrink from enforcing the law against violations of the tax code by political groups. The stakes here – namely the integrity of our elections and of our tax laws – are much too high for the IRS to walk away from its responsibility to ensure that the tax laws are not being abused for political purposes.

The investigations we have urged the IRS to conduct involve organizations conducting substantial campaign activities that we believe are misusing the tax laws to keep secret from the American people the donors financing their campaign activities. We presented compelling evidence in our letters to show that these groups are primarily involved in campaign-related activities and, as such, do not qualify for exempt status under section 501(c)(4).

As we explained in our earlier letters, the law provides that section 501(c)(4) organizations are required to primarily engage in the promotion of social welfare in order to obtain tax-exempt status under section 501(c)(4). Court decisions have established that in order to meet this requirement, section 501(c)(4) organizations cannot engage in more than an insubstantial amount of any non-social welfare activity, including direct or indirect participation or intervention in elections.

The facts outlined in our earlier letters clearly demonstrate, we believe, that the four organizations we requested the IRS to investigate are engaged in far more than an “insubstantial” amount of campaign-related activities that do not qualify as “social welfare” activities. One of these organizations supports Democratic candidates, two of them support Republican candidates, and one of them is seeking to nominate and run its own candidate for President.

By claiming tax-exempt status under section 501(c)(4), these groups allow their donors to evade the public disclosure requirements that would apply if the organizations were registered under section 527 as “political organizations.” In fact, as our previous letters demonstrated, it appears that avoiding disclosure of their donors is the basic reason that these groups chose to claim section 501(c)(4) tax status.

Absent enforcement of the law, the IRS will be countenancing an improper scheme that allows organizations engaged substantially in campaign activities to hide the sources of money being used to influence elections by claiming exempt status under section 501(c)(4). This is

section 527 group, is instead intended to be a reference to Crossroads GPS, an affiliated section 501(c)(4) organization.

contrary to the long established principle that citizens are entitled to know who is giving and spending money to influence their votes in order to protect the integrity of our elections and to safeguard against corruption. This principle is embodied in the Internal Revenue Code through the requirement that “political organizations” – those groups primarily organized and operated to influence elections – are subject to full disclosure of the sources of their funding. 26 U.S.C. § 527.

To the extent these organizations are operating improperly as section 501(c)(4) groups, the interests of the American people are being seriously harmed. The IRS has an obligation to enforce the tax laws as written and interpreted by the courts, and to ensure that tax-exempt groups substantially engaged in campaign activities are not allowed to misuse section 501(c)(4) to hide their donors from the public.

Such enforcement is not partisan, nor is it contrary to First Amendment values. Groups are free to obtain tax-exempt status and to engage in as much campaign activity as they wish – so long as they operate under section 527 and comply with its disclosure requirements.

We urge the IRS to move forward expeditiously to investigate the groups we have identified in our earlier letters and to conduct all other appropriate investigations to ensure proper compliance with the eligibility requirements of section 501(c)(4).

Sincerely,

/s/ Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

April 17, 2012

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: Secret donations to “social welfare “ organizations making campaign expenditures

Dear Commissioner Shulman and Director Lerner:

Democracy 21 and the Campaign Legal Center again call on the IRS to investigate and take appropriate enforcement action against Crossroads GPS regarding its claimed status as a section 501(c)(4) tax-exempt “social welfare” organization.

We also again call on the IRS to similarly investigate and take appropriate enforcement action against Priorities USA, American Action Network and Americans Elect, other organizations which we believe are improperly claiming status under section 501(c)(4).

It appears clear that Crossroads GPS is engaging in substantial spending to influence elections and is accordingly not eligible for section 501(c)(4) tax status under existing tax law and court interpretations of the law. It is also appears clear that Crossroads GPS is raising numerous secret million dollar and multi-million dollar donations to fund these expenditures.

In an article dated April 13, 2012 (copy enclosed), *The Washington Post* reported that Crossroads GPS received a secret donation of \$10 million dollars to be used to make expenditures to attack President Obama’s campaign for reelection.

According to the report:

An anonymous donor has given \$10 million to run ads attacking President Obama and his policies, escalating the money race that is defining the 2012 presidential campaign. And in the new, freewheeling environment of independent political giving, the identity of this donor, like many others, is likely to remain a permanent mystery.

The donation went to Crossroads GPS, the conservative nonprofit group founded with support of political operative Karl Rove, which also reported another donor giving at least \$10 million over the past two years, according to draft tax returns released by the organization.

The group would not identify the donors, who could be individuals, groups or corporations, and under tax and campaign laws, is not required to disclose them.¹

The new \$10 million secret contribution to Crossroads GPS to run attack ads against President Obama as he runs for re-election is a stark illustration of the problem caused by groups engaged in campaign spending claiming eligibility as “social welfare” organizations under section 501(c)(4).

The report in *The Washington Post* stated that Crossroads GPS and its affiliated Super PAC, American Crossroads, together plan to spend an estimated \$300 million in the 2012 elections. The expenditures by these two affiliated groups clearly appear to be for one overriding purpose: to elect and defeat candidates.

The *Washington Post* article also shows the huge size of the contributions from secret donors that are being used to finance campaign-related expenditures:

The tax returns show that Crossroads GPS has collected the vast majority of its donations from the super-rich. The forms show that nearly 90 percent of its contributions through the end of 2011 had come from as few as two dozen donors, each giving \$1 million or more.

In prior letters sent to you on October 5, 2010, September 28, 2011, December 14, 2011 and March 9, 2012, our organizations have called on the IRS to investigate and take appropriate enforcement action against Crossroads GPS and other similarly situated organizations improperly claiming tax-exempt status as section 501(c)(4) “social welfare” organizations.

In our earlier letters, we noted that the overriding purpose of these groups is to influence elections and that the groups are spending substantial amounts to do so. These groups appear to be spending far more to intervene and participate in campaigns than the law and court interpretations allow “social welfare” organizations to spend for such purposes.

¹ T.W. Farnum, “Mystery donor gives \$10 million to Crossroads GPS group to run anti-Obama ads,” *The Washington Post* (April 13, 2012).

It is apparent that these groups are claiming section 501(c)(4) tax status in order to keep secret from the American people the donors financing their campaign-related expenditures. If these organizations are not eligible for tax status under section 501(c)(4), then they are improperly using the tax laws to shield their donors from public disclosure and improperly using secret contributions to influence the 2012 national elections.

As we have previously noted, it appears that the overriding purpose of Crossroads GPS is to influence elections. The ads run by Crossroads GPS are campaign-related under IRS standards. The standards provide that ads do not have to contain express advocacy in order to be treated as intervention and participation in campaigns for purposes of determining eligibility for tax-exempt status as a section 501(c)(4) organization.

As we have stated in our previous letters, we are deeply concerned about the failure of the IRS to take any public steps to show that the agency is prepared to enforce the tax laws applicable to section 501(c)(4) “social welfare” groups.

The ongoing harm to the public from the agency’s failure to act is that section 501(c)(4) groups are being used as vehicles to raise and spend secret contributions on a massive scale to influence the 2012 elections.

Unless the IRS acts, the public interest in transparent campaign finance activities – an interest that was strongly affirmed by the Supreme Court in the *Citizens United* case – will be greatly damaged by the agency allowing groups to misuse the tax laws to hide the identities of wealthy donors giving huge amounts to influence this year’s presidential and congressional elections.

Sincerely,

/s/ Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

September 27, 2012

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: Crossroads GPS

Dear Commissioner Shulman and Director Lerner:

Democracy 21 and the Campaign Legal Center have written to you on multiple occasions seeking an investigation by the IRS into whether four organizations—Crossroads GPS, Priorities USA, American Action Network and Americans Elect—are improperly claiming status as a “social welfare” organizations under section 501(c)(4) of the tax code.

Our first letter challenging the claim by Crossroads GPS to tax-exempt status as a “social welfare” organization was sent to the IRS nearly two years ago, on October 5, 2010. We have subsequently sent eight letters to you regarding Crossroads GPS and the other organizations. (These letters are dated July 27, 2011, September 28, 2011, December 14, 2011, March 9, 2012, March 22, 2012, April 17, 2012, May 24, 2012 and July 23, 2012.)

We believe the facts we have presented to you in our letters make clear that each of these organizations is, to put it simply, a campaign operation—an organization whose overwhelming focus and purpose has been to elect and/or defeat candidates in the 2012 elections. Because the primary purpose of each of these organizations is to participate or intervene in candidate elections, these organizations are not, and should not be permitted to claim status as, “social welfare” organizations under section 501(c)(4).

There is a serious and continuing harm in the failure of the IRS to enforce the law. If these groups were registered as “political organizations” under section 527 of the tax code, they would be required to disclose their donors of \$200 or more and the public would be able to scrutinize the sources of money they are using to fund their campaign activities. 26 U.S.C. § 527(j). But as purported “social welfare” organizations, these groups are not required to publicly disclose their donors, and can therefore spend millions of dollars on efforts to influence the 2012 elections while hiding their donors from the American people.

In recent letters to the IRS, Senator Carl Levin (D-MI) has raised appropriate concerns about the agency’s lack of enforcement of the rules governing section 501(c)(4) status. As Senator Levin pertinently noted, “I find it unacceptable that the IRS appears to be passively standing by while organizations that hold themselves out to be ‘social welfare’ organizations clearly ignore the tax code with no apparent consequences.”¹

We strongly agree.

The purpose of this letter is to provide additional information to document that Crossroads GPS is an organization with an overriding purpose to influence candidate elections, and is accordingly not entitled to tax-exempt status as a section 501(c)(4) “social welfare” organization. In addition, this letter raises as a second ground for denying tax-exempt status the fact that Crossroads GPS also fails to meet the applicable legal test under the “private benefit” doctrine because it serves private political interests, not public “social welfare” interests.

Crossroads GPS reported in its Form 990s filed with the IRS for 2010 and 2011 that it received 24 separate donations of \$1 million or more in 2010 and 2011—the largest being two single donations of \$10 million. But the organization did not disclose the identity of any of these donors. As one published report stated, “In its first 18 months, Crossroads GPS raised \$67 million of its total \$77 million from as few as 16 rich donors.”² Undoubtedly, Crossroads GPS has received more such contributions this year.

There is little question that these million dollar donors are funding the campaign ads being sponsored by Crossroads GPS, yet the identity of these donors is hidden from the public by the fact that they have funneled their money through a group improperly claiming status under section 501(c)(4). This is an abuse of the tax laws, in service of evading the bedrock principle that money spent to influence federal elections should be subject to public disclosure.

The evidence we have presented to the IRS shows that Crossroads GPS is being operated “for the substantial nonexempt purpose of benefiting the private interests of Republican Party entities and candidates.” *See American Campaign Academy v. Commissioner*, 92 T.C. 1053 (1989). Under these circumstances, Crossroads GPS is not entitled to section 501(c)(4) tax-

¹ Letter of August 31, 2012 from Senator Carl Levin to The Honorable Daniel H. Shulman, Commissioner, Internal Revenue Service.

² S.V. Date, “Rove’s Crossroads GPS Gets Explicit In Anti-Obama Air War,” *NPR* (Sept. 12, 2012).

exempt status under the “private benefit” doctrine because it is an organization created and operated to serve private political interests, not public “social welfare” purposes.

Crossroads GPS and its sister Super PAC organization, American Crossroads, were established in the summer of 2010, and were conceived and founded by Karl Rove and Ed Gillespie. Crossroads GPS was created shortly after American Crossroads in order for donors to be able to provide funds anonymously to influence federal elections.

Karl Rove is the leading Republican Party political operative in the country. Rove was the chief political adviser to President George W. Bush for his eight years in office.

Ed Gillespie was named a counselor to the Romney campaign in April 2012 and serves as a senior adviser for the Romney presidential campaign. Gillespie is a former Chairman of the Republican National Committee and served as a counselor to President George W. Bush in 2007 and 2008. In 2010, Gillespie was named chairman of the Republican State Leadership Committee, which helps elect state attorneys general, lieutenant governors, secretaries of state and house and senate candidates across the country.

The evidence clearly indicates that Crossroads GPS (along with American Crossroads) was founded by Rove and Gillespie to carry out their private political interests in electing Republicans and defeating Democrats, and not to engage in public “social welfare” activities. The organization’s operations have furthered these private political interests.

Karl Rove recently confirmed publicly that Crossroads GPS is a political operation and that its activities are intended to elect Republicans and defeat Democrats. In an op-ed article published in *The Wall Street Journal* (August 1, 2012) (emphasis added), Rove said:

Roughly \$111 million of Mr. Obama’s ad blitz was paid for by his campaign; outside groups chipped in just over \$20 million. The Romney campaign spent only \$42 million over the same period in response, with \$107.4 million more in ads attacking Mr. Obama’s policies or boosting Mr. Romney coming from outside groups (with Crossroads GPS, a group I helped found, providing over half).

Rove thus stated that in response to an “ad blitz” by President Obama’s reelection campaign and supportive Democratic outside groups, Crossroads GPS spent more than \$53 million on ads “attacking Mr. Obama’s policies or boosting Mr. Romney.” This blunt statement by Rove un masks the fact that Crossroads GPS is a campaign operation and makes clear that the ads run by Crossroads GPS about Obama and Romney are campaign ads.

This unambiguously partisan political activity clearly falls within the standard set forth by the IRS in a ruling denying section 501(c)(4) tax-exempt status to an organization that was “not operated primarily to promote social welfare because your activities are conducted primarily for the benefit of a political party and a private group of individuals, rather than the community as a whole.” Final Determination Letter, Number 201128032 (April 4, 2011).

In that matter, the IRS concluded that “an organization which conducts its educational activities to benefit a political party and its candidates serves private interests. And . . . an organization that primarily serves private interests fails to qualify for exemption under section 501(c)(4).” *Id.* at 6 (citing *American Campaign Academy*). The IRS concluded in that matter:

In summary, you are not operated primarily to promote social welfare because your activities are conducted primarily for the benefit of a political party and a private group of individuals, rather than the community as a whole. Accordingly, you do not qualify for exemption as an organization described in section 501(c)(4) of the Code and you must file federal income tax returns.

Id.; see also Determination Letter 201221028 (March 2, 2012) (“Educational activities undertaken to provide a partisan benefit are considered to serve private interests, rather than the common good.”); Determination Letter, Number 201224034 (March 21, 2012) (same).

The information we are submitting here, as well as the information we have submitted in our past letters to the IRS, also shows that the overriding, if not exclusive, purpose of Crossroads GPS is to influence candidate elections and that it is engaged primarily in campaign activities. Under these circumstances, Crossroads GPS does not have a primary purpose of conducting “social welfare” activities and is therefore not entitled to tax-exempt status as a section 501(c)(4) organization.

There can be no doubt that Crossroads GPS is engaging in massive spending on television ads that have the purpose and effect of influencing the 2012 elections, and thereby constitute participation or intervention in the campaign.

The apparent basis for the claim by Crossroads GPS that it is entitled to tax status as a “social welfare” organization is its assertion that its ads are “issue” ads, not campaign ads, because the ads do not contain “express advocacy.”³ As one recent press report stated, “For

³ Ironically, Crossroads GPS did switch to “express advocacy” ads for a short period in order to avoid disclosure of its donors under the campaign finance laws. In a March 2012 ruling, a federal district court invalidated an FEC regulation which limited disclosure of donors to groups that make “electioneering communications” (*i.e.*, ads that are proximate in time to an election but do not contain express advocacy). This ruling required donor disclosure by groups sponsoring electioneering communications, but not for independent expenditures (*i.e.*, ads that do contain express advocacy and are subject to a different FEC disclosure regulation). In order to avoid disclosure once its ads were within the electioneering communications time frame, Crossroads GPS and other section 501(c)(4) groups began adding express advocacy to their ads in early September, so those ads became independent expenditures rather than electioneering communications. K. Doyle, “D.C. Circuit Revives FEC Rule Allowing Political Ad Sponsors to Avoid Disclosure,” *BNA Money and Politics Report* (Sept. 19, 2012) (“One paradoxical result was that groups previously sponsoring ‘issue ads’ began sponsoring messages that explicitly call for votes for or against candidates. The reporting rules for such ‘independent expenditure’ messages were not affected by the Van Hollen litigation and continued to allow ad sponsors to keep donors secret. The groups switching from electioneering communications to independent expenditures include such high-profile, GOP-leaning organizations as U.S. Chamber of Commerce, Americans for Prosperity, and Crossroads GPS. . . .”). The Court of Appeals for the D. C. Circuit reversed the district

months, the tax-exempt Crossroads GPS has argued that its anti-Obama ads were merely issue ads and not political ads.”⁴ The same story stated, “Crossroads GPS spent more than \$50 million on ads attacking President Obama this spring and summer. But its officers do not believe those count as political activity because they did not tell viewers to vote against Obama.” *Id.* (emphasis added).

As noted above, however, Karl Rove has publicly confirmed that more than \$53 million in ads run by Crossroads GPS are campaign ads run in response to President Obama’s “ad blitz.”

Furthermore, it is a flat misstatement of the law to claim that ads are “issue” ads, and not campaign ads, simply because the ads do not contain “express advocacy.” The IRS has made clear in rulings that “express advocacy” is not required for a group’s spending to count as intervention or participation in a campaign for purposes of assessing a group’s eligibility for exempt status under section 501(c)(4). A recent report by the Congressional Research Service summarized the law as it applies to 501(c)(4) organizations:

Clearly, any advertisement that expressly endorses or opposes a candidate is campaign activity. It is also clear that there is no rule that campaign intervention occurs only when an organization expressly advocates for or against a candidate.⁵

Instead, the IRS has set forth in two Revenue Rulings the “facts and circumstances” that the agency takes into consideration in determining whether an ad constitutes intervention or participation in a campaign, even if the ad does not contain “express advocacy.”

Revenue Ruling 2004-6, 2004-1 C.B. 328, 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 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

court ruling earlier this month. *Center for Individual Freedom v. Van Hollen*, ___ F.3d ___, 2012 WL 4075293 (D.C. Cir. Sept. 18, 2012) reversing *Van Hollen v. FEC*, 851 F.Supp. 2d 69 (D.D.C. 2012).

⁴ S.V. Date, “Rove’s Crossroads GPS Gets Explicit In Anti-Obama Air War,” *NPR* (Sept. 12, 2012).

⁵ E. Lunder, “R42684: Political Ads: Issue Advocacy or Campaign Activity Under the Tax Code,” *Congressional Research Service* (Aug. 29, 2012).

to be considered to determine whether the expenditure is for an exempt function under § 527(e)(2).

Id. (emphasis added)

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. These factors are not in themselves dispositive. In the end, the regulations require a determination to be made based on “the facts and circumstances” of each advertisement.

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.

Similarly, in Rev. Rul. 2007-41, 2007-1 C.B. 1421, the IRS stated that “[w]hether an organization is participating or intervening, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office depends upon all of the facts and circumstances of each case.” Rev. Rul. 2007-41 at 2. With regard to campaign ads, the Revenue Ruling states:

Even if a statement does not expressly tell an audience to vote for or against a specific candidate, an organization delivering the statement is at risk of violating the political campaign intervention prohibition if there is any message favoring or opposing a candidate. . . . All the facts and circumstances need to be considered to determine if the advocacy is political campaign intervention.

Id. at 6 (emphasis added). According to the Revenue Ruling, the factors relevant to this determination include:

- Whether the statement identifies one or more candidates for a given public office;
- Whether the statement expresses approval or disapproval for one or more candidates’ positions and/or actions;
- Whether the statement is delivered close in time to the election;
- Whether the statement makes reference to voting or an election;
- Whether the issue addressed in the communication has been raised as an issue distinguishing candidates for a given office;
- Whether the communication is part of an ongoing series of communications by the organization on the same issue that are made independent of the timing of any election; and
- Whether the timing of the communication and identification of the candidate are related to a non-electoral event such as a scheduled vote on specific legislation by an officeholder who also happens to be a candidate for public office.

Id. The Revenue Ruling notes, “A communication is particularly at risk of political campaign intervention when it makes reference to candidates or voting in a specific upcoming election.” *Id.* at 7.

Under established IRS rulings, and with regard to the requirement that the group be primarily engaged in “social welfare activities,” the agency needs to examine the body of ads run by Crossroads GPS this year, to apply the standards laid out in the pertinent IRS Revenue Rulings, and to determine whether the ads run by Crossroads GPS constitute intervention or participation in candidate elections. Once the IRS has determined the extent to which Crossroads GPS has engaged in spending for ads to intervene or participate in candidate elections, the agency can then determine whether such campaign activities constitute its “primary purpose,” in violation of the permissible standard for “social welfare” organizations.

In order to assist the IRS in its task of determining the extent of non-social welfare activities being engaged in by Crossroads GPS, we have enclosed a transcript of each ad that has been aired by Crossroads GPS from January 1, 2012 through September 24, 2012. We believe that a review of these ads, and the circumstances related to where and when they have been run, will demonstrate that under the applicable IRS standards, these ads constitute intervention and participation in candidate elections.

For example, an ad entitled “Suffered,” that was run by Crossroads GPS on July 23, 2012, states:

Narrator: America has suffered three years of crushing unemployment. Remember this: Obama: “We’ll create nearly half a million jobs by investing in clean energy.”
Narrator: What really happened? Billions wasted on failed investments.
Thousands of Americans lost jobs. While stimulus money went to companies that created jobs overseas. Paid for by the \$4 billion Obama has added to our debt every day. Tell President Obama, for real job growth, cut the debt. Support the New Majority Agenda at newmajorityagenda.org.

This ad identifies President Obama and expresses strong disapproval for his positions on jobs and stimulus, two issues that distinguish the candidates in the election. This ad was run in this campaign season and was not related to any identified non-electoral event. Given these facts and circumstances, there is little doubt that this ad would constitute candidate campaign intervention and participation under the standards set forth in the Revenue Rulings discussed above.

The same is true for all of the other ads run by Crossroads GPS this year. For instance, an ad entitled “Basketball,” which began running on May 22, 2012, states:

Woman: “I always loved watching the kids play basketball. I still do, even though things have changed. It’s funny, they can’t find jobs to get their careers started and I can’t afford to retire and now we are all living together again. I supported President Obama because he spoke so beautifully. He promised

change, but things changed for the worse. Obama started spending like our credit cards have no limits. His health care law made health insurance even more expensive. We've had stimulus and bailouts. Obama added over \$16,000 in debts for every American. How will my kids pay that off when they can't even find jobs? Now, Obama wants more spending and taxes. That won't fix things. I had so many hopes. Cutting taxes and debt and creating jobs. That's the change we need. Tell President Obama to cut the job killing debt and support the new majority agenda at newmajorityagenda.org.

This ad, as well, identifies and criticizes President Obama on issues that are central to the presidential election—the health care law, the stimulus and the national debt. There is little doubt that this ad would constitute candidate campaign intervention under applicable IRS standards.

Almost all of the ads run by Crossroads GPS, furthermore, have been run in presidential battleground states and/or states involving contested Senate races. In a number of cases, the Crossroads GPS ads mention both President Obama and a Senate candidate in states that are both a presidential battleground state and a state with a contested Senate race.

Thus, for example, 47 of the 60 ads mention Obama and a Senate candidate, or just the Senate candidate. They include: eight ads that mention Virginia Democratic Senate candidate Tim Kaine, seven ads that mention Montana Democratic Senator Jon Tester, seven ads that mention Nevada Democratic Senate candidate, Representative Shelley Berkley, six ads that mention North Dakota Senate candidate Heidi Heitkamp, six ads that mention Ohio Democratic Senator Sherrod Brown, five ads that mention Missouri Democratic Senator Claire McCaskill, three ads that mention Wisconsin Senate Democratic candidate, Representative Tammy Baldwin, two ads that mentions Indiana Democratic Senate candidate, Joe Donnelly, two ads that mention New Mexico Democratic Senate candidate, Representative Martin Heinrich and one ad that mentions Florida Democratic Senator Bill Nelson.

The Senate races in Montana, Virginia, North Dakota, Nevada, Missouri, Ohio, Wisconsin, New Mexico, Florida and Indiana—the states where the Crossroads GPS ads mentioning Senate candidates have run—are all races that have been considered “in play” during the 2012 elections and have been viewed as key races in determining whether the Republicans can take control of the Senate in 2013.

The transcripts of the ads have been obtained by us from YouTube where Crossroads GPS posts its ads. We do not know how often each of these ads has run, but the IRS can and should obtain that information as part of reviewing the activities of Crossroads GPS to determine whether the group is eligible for section 501(c)(4) tax status.

We urge the IRS to review each of the attached ads, and to apply the agency's standards to determine whether the ads constitute candidate campaign intervention. If you find, as we believe you must, that all, or the overwhelming majority, of these ads are campaign ads, then the inescapable conclusion is that the primary purpose of Crossroads GPS is to participate or intervene in the 2012 elections. As such, its claim to status as a “social welfare” organization

under section 501(c)(4) is not in compliance with the tax laws. Similarly, the IRS should find that the “private benefit” doctrine disqualifies Crossroads GPS for tax-exempt status under section 501(c)(4).

The IRS should act expeditiously in examining these ads, in denying Crossroads GPS tax-exempt status and in imposing appropriate penalties on the organization. The IRS should also act expeditiously in addressing the information we have presented in our prior letters with regard to Priorities USA, American Action Network and Americans Elect, and similarly should deny tax exempt status to those groups and impose appropriate penalties.

Crossroads GPS is engaged in a massive scheme to serve as a black box conduit to mask the sources of tens of millions of dollars flowing into the 2012 elections. We believe that Crossroads GPS is blatantly abusing the non-profit tax laws to do so.

It is the responsibility of the IRS to stop this abuse. We urge you to do so promptly.

Sincerely,

/s/ Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

December 3, 2012

Steven T. Miller
Acting 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: Political Activities by section 501(c)(4) organizations

Dear Acting Commissioner Miller and Director Lerner:

The IRS last week released its 2012-2013 Priority Guidance Plan (Nov. 19, 2012), which “contains 317 projects that are priorities for allocation of the resources of our offices during the twelve-month period from July 2012 through June 2013 (the plan year).”

Inexplicably, however, nowhere on this list of 317 agency “priorities,” which includes a list of 13 priorities specifically relating to exempt organizations, is there any mention of a project to revise and clarify the rules dealing with political activities by section 501(c)(4) groups.

There simply is no basis for the IRS to ignore, as it apparently has done, the widespread abuses that occurred in the 2012 election by groups claiming section 501(c)(4) tax-exempt status and the role that the IRS’s flawed regulations played in contributing to these abuses.

An estimated \$400 million in secret contributions were laundered into the 2012 elections through section 501(c) organizations. A large portion of these funds was spent by groups improperly claiming tax-exempt status as section 501(c)(4) “social welfare” organizations in order to hide the identities of their donors from the American people.

In the absence of any action by the IRS to address this problem, even greater abuses of the tax laws are expected to occur in future elections by groups improperly claiming to be “social welfare” organizations. The failure of the IRS to act on this matter is doing great harm to the American people and to their fundamental right to know who is providing the money to influence their votes.

Democracy 21 and the Campaign Legal Center wrote to the IRS on ten occasions during 2011 and 2012 to request the agency to investigate and take action on serious abuses of the tax laws by groups that were improperly claiming tax-exempt status under section 501(c)(4).

These groups had an overriding purpose to influence federal elections and engaged in campaign activities that failed to meet the eligibility requirements of section 501(c)(4) and court interpretations of the law.

On July 27, 2011, we submitted a petition for rulemaking in which we requested the IRS to initiate a proceeding to clarify and bring into compliance with the law the IRS regulations that govern campaign activity by groups claiming status as “social welfare” organizations.

On July 17, 2012, almost one year later, we received a letter from Ms. Lerner which acknowledged that “the IRS is aware of the current public interest in this issue,” recognized that the existing regulations were more than a half-century old and stated that the IRS would “consider proposed changes in this area.”

It is an indefensible abdication of responsibility for the IRS, after stating in the July 17, 2012 letter to us that the agency would “consider proposed changes in this area,” to fail to include the section 501(c)(4) regulations dealing with political activity on the agency’s Priority Guidance Plan.¹

Since “social welfare” organizations are not required to disclose their donors to the public, such groups can serve as vehicles for secretly injecting huge contributions into federal elections. Just one such group claiming status as a “social welfare” organization – Karl Rove’s Crossroads GPS – spent \$70 million on electioneering communications and independent expenditures in the 2012 campaign.

Not one of the sources of the \$70 million spent by Crossroads GPS was disclosed to the public.

As we have previously demonstrated in our letters to the IRS, Crossroads GPS does not meet the eligibility requirements for a 501(c)(4) “social welfare” organization. Rather, it is a campaign organization whose primary purpose in 2012 was to elect Republican candidates.

¹ We note that at page 37 of the Guidance, the IRS states that in January 2013 it will publish a “Revenue Procedure updating procedures for issuing determination letters and rulings on the exempt status of organizations under §§501 and 521.” Since this proposed publication will address only “procedures for issuing determination letters,” it does not appear to have relevance to the standards an organization must satisfy in order to qualify for exempt status under section 501(c)(4). The fact that this proposed publication is not listed in the portion of the Guidance document that relates to substantive rules for exempt organizations (pp. 10-11) also supports the view that this will be a non-substantive issuance.

Crossroads GPS is similar to a number of other groups masquerading as “social welfare” organizations that operated in the 2012 elections to support candidates of both parties. The contributions spent by these groups for campaign activities were shielded from public disclosure because of their claim for exemption under section 501(c)(4).

Our previous letters to the IRS also challenged the eligibility of Priorities USA, a group formed to support the re-election of President Obama, American Action Network and Americans Elect to receive tax-exempt status under section 501(c)(4).

It is a matter of urgent public importance for the IRS to move promptly to fix its rules.

The existing flawed regulations are playing a key role in the massive amounts of secret money being spent in federal elections by groups that are improperly claiming status as “social welfare” organizations. This large-scale abuse of the tax laws to hide political donors is contrary to the Internal Revenue Code, to court interpretations of the Code and to the longstanding national policy of transparency for campaign finance contributions and expenditures.

Prompt and effective action by the IRS to address this matter is essential to prevent a repeat in 2014 of campaign operatives using phony “social welfare” organizations as conduits to inject secret money into federal campaigns and thereby to frustrate the public’s right to know the sources of money spent to influence our elections.

In that light, the refusal of the IRS even to list the regulations governing eligibility for section 501(c)(4) tax-exempt status in its Priority Guidance Plan for 2012-2013 is indefensible, unacceptable and in direct conflict with the interests of the American people.

The November 19 Guidance states that the IRS will periodically update its work plan “to reflect additional items that have become priorities. . . .”

We strongly urge you to add the section 501(c)(4) regulations to the agency’s regulatory priorities and to take timely and effective steps to address the fundamental flaws in these regulations prior to the 2014 campaign. The IRS must ensure that the widespread abuses of laundering secret money into federal elections through section 501(c)(4) organizations does not repeat itself in the future, to the great detriment of the American people and our democracy.

We request a meeting with you as soon as possible to discuss our concerns and the urgent need for a rulemaking proceeding to address the problems that exist.

Sincerely,

/s/ Gerald Hebert

/s/ Fred Wertheimer

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

January 2, 2013

Steven T. Miller
Acting 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: Application for section 501(c)(4) status by Crossroads GPS

Dear Acting Commissioner Miller and Director Lerner:

ProPublica, a news organization, recently received and publicly disseminated the Form 1024, "Application for Recognition of Exemption under Section 501(a), filed by Crossroads GPS on September 3, 2010, seeking recognition as a "social welfare" organization under section 501(c)(4) of the Internal Revenue Code. So far as we are aware, the IRS has yet to grant the application.

In its application, Crossroads GPS states that 50 percent of its activities will be devoted to "public education," 30 percent will be devoted to "influenc[ing] legislation and policymaking," and 20 percent will be devoted to "research." Application at 2. Thus, when asked to provide a "detailed narrative description of all the activities of the organization – past, present and planned," Crossroads GPS fails to mention any activities devoted to influencing federal elections, and instead describes 100 percent of its activities as involving efforts other than electioneering.

Inconsistently, in response to a different question on the application, Crossroads GPS states that it plans to spend funds "to distribute independent political communications," but such activity "will be limited in amount, and will not constitute the organization's primary purpose." *Id.* at 4.

We have written to you on a number of occasions in the past two years regarding the enormous sums of money spent by Crossroads GPS to influence the 2010 and 2012 federal

elections. In those letters, we have challenged the organization's eligibility for section 501(c)(4) tax-exempt status.

According to the Center for Responsive Politics (CRP), Crossroads GPS spent \$70 million on independent expenditures to elect Republican candidates or defeat Democratic candidates in the 2012 elections. This is an extraordinary amount of money to be spent on influencing elections by a group which claims it is a "social welfare" organization.

Indeed, Crossroads GPS and its affiliated Super PAC, American Crossroads, together spent a total of \$175 million on independent expenditures and electioneering communications to influence the 2012 elections—far more than any other outside spender, according to CRP.

The \$70 million in campaign expenditures attributed to Crossroads GPS consists overwhelmingly of ads reported to the Federal Election Commission as "independent expenditures," *i.e.*, ads that contain "express advocacy."

As we have discussed at length in our prior correspondence with you, the IRS uses a different test to define activity that constitutes intervention or participation in elections, and additional ads by Crossroads GPS that may not be subject to reporting to the FEC may nonetheless fall well within the test used by the IRS to determine what constitutes campaign spending by a tax-exempt group.

In continuing any ongoing review of the application submitted by Crossroads GPS for status as a section 501(c)(4) organization, we believe it is essential that you not accept at face value either the obviously self-serving statement on its application that Crossroad GPS's campaign spending will not constitute its "primary purpose" or any self-serving claims by the organization that communications were "issue ads."

The IRS should closely scrutinize the spending that Crossroads GPS engaged in during the 2012 campaign. This includes both the spending that was reported to the FEC as "independent expenditures" because it included "express advocacy," and any other spending on communications that may well have constituted intervention or participation in campaigns under IRS rules, even if the ads did not contain "express advocacy."

In particular, we strongly urge you not to accept at face value any claim by Crossroads GPS that any or all of its ads that mention federal candidates and did not contain express advocacy were "public education ads" or "issue ads." These ads, and the context in which they were run, must be reviewed by the IRS to determine whether in fact any or all of the ads constituted ads to intervene or participate in elections, within the IRS definition of that standard. *E.g.*, Revenue Ruling 2004-6, 2004-1 C.B. 328.

In our letter to you of September 27, 2012, we submitted transcripts of the ads run by Crossroads GPS from January 1, 2012 through September 24, 2012. We urged the IRS to review each of these ads, and to apply the agency's standards to determine whether the ads constituted intervention or participation in campaigns. We again urge you to conduct such a review.

In any event, we submit that the \$70 million spent by Crossroads GPS just on campaign ads reported to the FEC in 2012 is *prima facie* evidence that the organization does have a “primary purpose” to engage in campaign activities. The statement made by Crossroads GPS two years ago on its application for tax-exempt status that its campaign activities will be “limited in amount, and will not constitute the organization’s primary purpose” are simply not credible, in light of the actual practices of the organization and the tens of millions of dollars Crossroads GPS spent on campaign ads since then.

As we have stated in previous letters, the misuse of “social welfare” organizations as vehicles for campaign spending results in direct and serious harm to the American people because it hides from public scrutiny the identity of the donors funding the campaign spending.

Crossroads GPS itself reported on its Form 990s filed with the IRS for 2010 and 2011 that it received 23 separate donations of \$1 million or more in 2010 and 2011 – including two contributions of \$10 million each. But Crossroads GPS used its claim to section 501(c)(4) tax-exempt status as the basis for not publicly disclosing the identity of any of these million-dollar and multi-million dollar donors. It is very likely the case that the organization received additional seven- or eight-figure donations in 2012.

It is also very likely that some, if not most, of the undisclosed contributions raised by Crossroads GPS were spent for campaign ads to influence the 2012 elections. Thus, the tactic of directing campaign money through the form of an entity claiming to be a “social welfare” organization has enabled tens of millions of dollars of “dark” money to be spent to influence federal elections.

It is the responsibility and obligation of the IRS to stop this kind of abuse of the tax laws. It is imperative that the IRS closely and critically review the assertions made by Crossroads GPS in its application for tax-exempt status, and in its tax returns, in light of its massive, campaign spending in the 2012 federal elections.

Crossroads GPS served as little more than a campaign operation in 2012. Crossroads GPS has no business being treated as a “social welfare” organization and the IRS should deny its application for tax-exempt status as a section 501(c)(4) organization.

Sincerely,

/s/ *Gerald Hebert*

/s/ *Fred Wertheimer*

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21

January 16, 2013

Steven T. Miller
Acting 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: Application for section 501(c)(4) status by American Tradition Partnership

Dear Acting Commissioner Miller and Director Lerner:

Democracy 21 and the Campaign Legal Center are writing to request the IRS to conduct an investigation into whether American Tradition Partnership (ATP), formerly known as Western Tradition Partnership (WTP), obtained its section 501(c)(4) tax-exempt status based on false information submitted to the IRS.

According to published reports, the apparently false information included misrepresentations made to the IRS by WTP in urging expedited approval of its application and misrepresentations in its application to the IRS, asserting that it would not participate or intervene in elections.

WTP submitted its Form 1024, Application for Recognition of Exemption under Section 501(a), to the IRS on July 21, 2008. A copy of the application is publicly available.

According to a news report by *ProPublica* and *Frontline*, WTP submitted a letter to the IRS on September 29, 2008, while their IRS application was still pending, requesting that the IRS expedite processing of its application.¹ According to the *ProPublica/Frontline* report, the

¹ Kim Barker, *ProPublica*, and Rick Young and Emma Schwartz, *Frontline*, “Did the Dark Money Group that Spurred a Landmark Ruling Mislead the IRS?” *ProPublica and Frontline*, Oct. 22, 2012, <<http://www.propublica.org/article/did-the-dark-money-group-that-spurred-a-landmark-ruling-mislead-the-irs>>.

request for expedition stated that Jacob Jabs, who was described as the organization's "primary donor," had promised to make a \$300,000 donation to the group, but only if WTP received recognition from the IRS for tax-exempt status by September 29, 2008. *Id.*

The letter further said, however, that Jabs had extended his deadline, and said he "will give us the grant if we receive our tax exempt status by October 15, 2008. If we have not received our tax exempt status by this date, Mr. Jabs has assured us that he will no longer contribute said amount and instead will direct his donation to other organizations." *Id.*

According to the *ProPublica/Frontline* report, the IRS responded to WTP the next day, September 30, 2008, and said that the request for expedited consideration would be granted. Tax-exempt status as a section 501(c)(4) "social welfare" organization was granted to WTP two days later on October 2, 2008. *Id.*

According to a report published by *ProPublica* and *Frontline* on October 30 2012, Jabs has subsequently said "he had never pledged money to the group, and never even been in contract with them until press stories appeared naming him."² The *ProPublica/Frontline* report states:

"I think they just grabbed my name out of a hat to forward their agenda," Jabs told us. "I know nothing about the group, never heard of them, never have heard of them until the last few days, and I did not, absolutely did not, commit \$300,000 to start this company." (Jabs also spoke with the Bozeman Daily Chronicle, again denying any connection to the group.)

According to *ProPublica* and *Frontline*, a subsequent release of WTP's bank records as a result of state court litigation in Montana "show[ed] no money came in from the man WTP claimed as its primary donor when it asked the IRS to expedite the approval of its application."³

Assuming the *ProPublica/Frontline* reports are correct, the IRS apparently agreed to expedited processing of WTP's application for tax-exempt status that resulted in its approval, based on apparent material fraudulent information that WTP provided to the IRS and that WTP had to know was false.

² Kim Barker, *ProPublica*, and Rick Young and Emma Schwartz, *Frontline*, "More Evidence Key Dark Money Group May Have Misled IRS," *ProPublica and Frontline*, Oct. 30, 2012, <<http://www.propublica.org/article/more-evidence-key-dark-money-group-may-have-misled-irs>>.

³ Kim Barker, *ProPublica*, and Rick Young and Emma Schwartz, *Frontline*, "Dark Money Group's Donors Revealed," *ProPublica and Frontline*, Nov. 5, 2012, <<http://www.propublica.org/article/dark-money-groups-donors-revealed>>.

On these grounds alone, the section 501(c)(4) tax-exempt status of WTP should be revoked and the IRS should consider what, if any, other actions it should take against WTP. The IRS should also forward any relevant information in this case to the Department of Justice so the Department can determine what, if any, action it should take against WTP for apparently submitting material false information to a federal agency in order to obtain action by the agency.

Furthermore, according to its initial application for tax-exempt status, WTP stated that “[t]he organization will not directly or indirectly participate or intervene on behalf of or in opposition to a candidate for public office.” Application at 2. It reiterated its intention to engage in no campaign related activities in response to a separate question on page 4 of the application.

However, according to a report by *ProPublica* and *Frontline* published on October 22, 2012, shortly before WTP submitted its IRS application in 2008, the organization “and a related political committee sent out fliers weighing in on candidates for Montana state office” in the days before the Republican primary in the state.⁴

ProPublica and *Frontline* reported that “the group sponsored mailers that criticized politicians in the 2008 Republican primary.”⁵ According to the *ProPublica/Frontline* report, WTP has continued to participate or intervene in campaigns, in contravention of the representation it made to the IRS that it would engage in no campaign activity:

Western Tradition Partnership is now known as American Tradition Partnership. So far this election season [in 2012], the group has advocated for candidates in Montana’s Republican primary, putting out a press release announcing that 12 of those candidates won.⁶

Furthermore, according to *ProPublica* and *Frontline*, WTP “raised money specifically by telling people and corporations that they could give unlimited amounts in secret” to be spent to influence elections:

“The only thing we plan on reporting is our success to contributors like you who can see the benefits of a program like this,” said one document, a 2010 election briefing to read to potential donors. “You can just sit back on election night and see what a difference you’ve made.”⁷

⁴ Kim Barker, *ProPublica*, and Rick Young and Emma Schwartz, *Frontline*, “Did the Dark Money Group that Spurred a Landmark Ruling Mislead the IRS?” *ProPublica and Frontline*, Oct. 22, 2012, <<http://www.propublica.org/article/did-the-dark-money-group-that-spurred-a-landmark-ruling-mislead-the-irs>>.

⁵ Kim Barker, *ProPublica*, and Rick Young and Emma Schwartz, *Frontline*, “More Evidence Key Dark Money Group May Have Misled IRS,” *Pro Publica and Frontline*, Oct. 30, 2012, <<http://www.propublica.org/article/more-evidence-key-dark-money-group-may-have-misled-irs>>.

⁶ *Id.*

⁷ Kim Barker, *ProPublica*, and Rick Young and Emma Schwartz, *Frontline*, “Documents Found in Meth House Bare Inner Workings of Dark Money Group,” *ProPublica and Frontline*, Oct. 29, 2012,

The reported campaign activities by WTP and its successor, ATP, raise serious questions about whether WTP knowingly misrepresented its planned activities to the IRS in its initial application for tax-exempt status and whether it continued this misrepresentation over the years. This matter also warrants an investigation by the IRS to determine whether the organization's tax-exempt status should be revoked on these grounds and what, if any, other action should be taken against the organization.

The *ProPublica/Frontline* reports also raise serious questions about whether WTP has as its primary purpose intervening and participating in campaigns and is improperly claiming tax-exempt status in order to serve as a vehicle for secret contributions to be injected into state and federal elections. The IRS should also investigate this matter to determine what, if any, action should be taken against WTP based on these circumstances.

The IRS is responsible for enforcing the tax laws and preventing the tax laws from being misused to keep secret from the American people the sources of money spent to influence elections.

We strongly urge the IRS to investigate WTP/ATP and to take appropriate action against the organization for any violations of the tax laws and other federal laws that may have occurred.

Sincerely,

/s/ *Gerald Hebert*

/s/ *Fred Wertheimer*

J. Gerald Hebert
Executive Director
Campaign Legal Center

Fred Wertheimer
President
Democracy 21