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CORPORATE DONATIONS

'527' Organizations

By George J. Terwilliger III and John C. Wells

FOR THE SECOND time in as many presidential election contests, attention has again been focused on so-called "527" organizations, including Swift Boat Veterans for Truth, Americans Coming Together and MoveOn.org, to name a few. What are the origins of these organizations, what is their place in the current legal and regulatory scheme that governs campaign expenditures and what should corporate counsel know about them?

Background on 527 organizations

These organizations draw their name from the Internal Revenue Code, which grants them tax-exempt status under its § 527. Pursuant to that provision, an organization that is "organized and operated primarily for the purpose of directly or indirectly accepting contributions or making expenditures" need not declare contributions, dues or fund-raising proceeds as income if the money is used for "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." 26 U.S.C. 527(e).

When Congress first enacted this section in 1975, it created no specific provisions regarding registration or disclosure of 527 organizations with the IRS or the Federal Election Commission (FEC). At the time, Congress likely believed such organizations would be required to report contributions and expenditures to the FEC under the Federal Election Campaign Act (FECA), 2 U.S.C. 431 et seq., which required disclosure of any such expenditures by "political committees." The FECA used almost exactly the same language to define "contribution" and "expenditure"—key terms for determining whether an organization was a "political committee" under the statute—as § 527 used in defining a covered organization. In each case, the definition turned on whether the purpose of the contribution, expenditure or committee was to influence a federal election.

A recent advisory opinion by the FEC may in some cases curtail the effectiveness of corporate giving to a '527' organization.

Only shortly after Congress enacted § 527, however, the Supreme Court announced its landmark decision in *Buckley v. Valeo*, 424 U.S. 1 (1976). In *Buckley*, the court narrowed the FECA's references to "political committees" to make clear that they did not "reach groups engaged purely in issue discussion," but rather only those that have as their "major purpose" the election or nomination of a candidate. Id. at 79. The court had already held that the FECA's limit on expenditures, although broadly worded, would have to be limited to expenditures for "express advocacy"—that is, expenditures expressly advocating the election or defeat of a specified candidate for public office in a specific election—to render it constitutional. The court similarly limited the term "expenditure" for purposes of determining what groups constitute political committees.

The *Buckley* decision thus effectively eliminated any disclosure requirement applicable to 527 organizations not engaged in "express advocacy."

During the 2000 presidential primaries, advertising purchased by 527 organizations that referred to candidates but did not use the "magic words" identified in *Buckley* ("vote for," "elect," "support," "cast your ballot for," "Smith for Congress," "vote against," "defeat" or "reject") and thought to consti-

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tute express advocacy created a terrific stir. Many observers decried the ads and the anonymous nature of their funding. In light of the generally unenlightening names that 527 organizations are given, and the lack, at that point, of any requirement that their contributors or expenditures be publicly reported or disclosed, 527 organizations were referred to as "stealth PACs."

That year, Congress passed, and President Clinton signed into law, amendments to § 527 designed to address these concerns by creating—in new subsections (i) and (j)—registration and disclosure requirements for 527 organizations with more than $25,000 in annual receipts. Such organizations now had to formally notify the secretary of the treasury of their intent to invoke tax-exempt status, and had to disclose the name, address and occupation of each contributor giving more than $200, and the name and address of each recipient of $500 or more of expenditures, as well as the purpose of such expenditures.

Two years after the 2000 amendments to the FECA, Congress took another, more dramatic step into campaign finance regulation with the Bipartisan Campaign Reform Act of 2002 (BCRA), the act commonly known as "McCain-Feingold." Among other provisions, the BCRA requires the disclosure of any "electioneering communication," which is defined as any broadcast communication that occurs within 60 days of a general election (or 30 days of a primary election) and refers to a clearly identified candidate for federal office.

The BCRA also extends the general prohibition on the expenditure of corporate or union general treasury funds for express advocacy to cover any electioneering communication. These provisions thus broaden the scope of the category of communications triggering federal campaign finance law restrictions. The BCRA imposes a restriction on the ability of political party committees to solicit funds for 527 organizations, and a prohibition on parties' donating funds, or directing donations, to these organizations. These provisions, as interpreted by *McConnell v. FEC*, 540 U.S. 93 (2003), only restrict the ability of political parties to solicit or donate funds not raised in accordance with the FECA. The BCRA essentially left alone 527 organizations, except for the new electioneering communications regulations.

Corporations have long been subject to strict limits on their financial participation in the political process. As the Supreme Court noted in *McConnell*, the first such restriction was imposed in a 1907 law that banned outright any corporate contribution of money in connection with a federal election. 124 S. Ct. at 644. Subsequently, the prohibition on contributions was extended to reach "anything of value," and either giving or accepting a banned contribution was rendered a crime. Id. Union political contributions were soon seen to raise similar concerns, and were also regulated.

In 1972, with the enactment of the FECA, Congress reaffirmed that funds from the general treasuries of corporations and unions could not be used for political contributions or expenditures. However, it also permitted corporations and unions to establish separate, segregated funds—political action committees, or PACs—for the purpose of making such contributions and expenditures. The FECA generally permits corporations to solicit contributions to their PACs from shareholders or employees, but not from those unaffiliated with the corporation. In 1974, Congress amended the campaign finance laws again, restricting the use of unlimited numbers of political committees for fund-raising purposes, limiting individual and aggregate contributions, imposing spending limits on candidates and parties, requiring reporting and public disclosure of contributions and expenditures above set limits and establishing the FEC.

In spite of these restrictions, corporations, as well as individuals, have remained free to donate unlimited funds to 527 organizations operating outside the strictures of the FECA. Such funds need not come from a corporate PAC.

Generally speaking, 527 organizations also remained free to spend such contributions without regard to their source (assuming, of course, that they eschewed express advocacy). Early this year, however, the FEC issued an advisory opinion indicating that at least those 527 organizations that are registered with the FEC as federal PACs may use only "federal" or "hard" money—money raised subject to the requirements of the FECA—for communications that "promote," "support," "attack" or "oppose" a candidate for a federal election. See www.fec.gov/ aos/linkfiles/2003-37.pdf. Thus, under the opinion, 527 organizations seeking to fund what had generally been conceived of as issue-advocacy advertisements, which permissibly could be paid for using unregulated funds, might find instead that the advertisements they sought to fund could be paid for only with regulated funds. Plainly, this rule may in some cases curtail the effectiveness of corporate giving to a 527 organization. At least when the organization has an FEC-regulated component, the range of permissible uses of corporate funds may now be substantially narrowed.

New rules will take effect in 2005

On Aug. 19, the FEC adopted new rules (to take effect in 2005, after the upcoming election) dealing primarily with this same question of allocation between federal and nonfederal funds by 527 organizations. As significant as the rules the FEC did adopt, however, were rules that it declined to adopt. These rules would have significantly altered the analysis of whether a 527 organization counts as a "political committee" under the FECA. If a 527 organization does count as a political committee, contributions to it are capped at $5,000. Whether it is a "political committee" for purposes of the FECA is thus an enormously significant question for such an organization.

In sum, despite the FEC's recent decision declining to adopt these rules, it is fair to say that the status of 527 organizations is in flux. Since these organizations constitute one of the last remaining avenues for corporate participation in the political process using corporate funds, further developments and the policy decisions behind them are worth counsel's attention. NLJ

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