

September 30, 2005

By Electronic Mail

Ms. Mai T. Dinh
Assistant General Counsel
Federal Election Commission
999 E Street NW
Washington, DC 20463

**Re: Comments on Notice 2005-20: Definition of “Electioneering
Communication”**

Dear Ms. Dinh:

These comments are submitted jointly by the Campaign Legal Center, Democracy 21, and the Center for Responsive Politics in response to the Commission’s Notice of Proposed Rulemaking (“NPRM”) 2005-20, published at 70 Fed. Reg. 49508 (August 24, 2005), seeking comment on proposed changes to its rule defining “electioneering communication” under 11 C.F.R. § 100.29. Specifically, the Commission seeks comment on proposed changes to the definition of “publicly distributed” found at section 100.29(b)(3)(i), and to the exemption for section 501(c)(3) organizations found at section 100.29(c)(6).

For the reasons set forth below, we urge the Commission to:

- Adopt the proposal to remove the “for a fee” language from the definition of “publicly distributed” at 11 C.F.R. § 100.29(b)(3)(i);
- Reject the proposal to create a new exemption for unpaid, non-PASO communications;
- Eliminate, in its entirety, the existing exemption for section 501(c)(3) organizations from the definition of “electioneering communication” at 11 C.F.R. § 100.29(c)(6);
- Reject the proposal to incorporate a PASO standard into the section 501(c)(3) exemption at 11 C.F.R. § 100.29(c)(6);
- Reject the proposal to exempt from the “electioneering communication” regulations all communications that do not PASO a federal candidate; and

- Modify the proposed exemption from the definition of “electioneering communication” for advertisements promoting films, books, and plays run within the ordinary course of business.

The three commenters request the opportunity to testify at the hearing on this rulemaking, scheduled for October 19-20, 2005.

I. BCRA’s Legislative History, Purpose and Structure Make Clear That the Definition of “Electioneering Communication” is Critical to Preventing Circumvention of Disclosure Requirements and the Corporation/Labor Organization Expenditure Ban.

The Bipartisan Campaign Reform Act of 2002 (BCRA) amended the Federal Election Campaign Act (FECA) to define and regulate “electioneering communication,” defined as any broadcast, cable or satellite communication which: (1) refers to a clearly identified federal candidate; (2) is made within 30 days of a primary or 60 days of a general election; and (3) is “targeted” to the electorate of the identified candidate. 2 U.S.C. § 434(f)(3)(A)(i).

Corporations and labor organizations are prohibited from using treasury funds to make any payment for an “electioneering communication.” 2 U.S.C. §§ 441b(a) and (b)(2). Furthermore, any person who disburses more than \$10,000 during any calendar year for producing and airing an “electioneering communication” is required to file a statement with the Commission identifying, *inter alia*, the person making the disbursement, all persons who contributed \$1,000 or more to the person making the disbursement, the amount of the disbursement, and the elections and candidates to which the electioneering communication pertains. 2 U.S.C. § 434(f)(2).

Senator Snowe, a chief sponsor of BCRA’s “electioneering communication” provisions, explained the intent of these provisions:

I have spoken of the exploding phenomenon of the so-called issue advertising in elections. ... I am talking about broadcast advertisements that are ... in the overwhelming number of instances designed to influence our Federal elections, and yet no disclosure is required and there are none of the funding source prohibitions that for decades have been placed on other forms of campaigning. These are broadcast ads on television and on radio that masquerade as informational or educational but are really stealth advocacy ads for or against candidates.

147 Cong. Rec. S2455-56 (daily ed. Mar. 19, 2001).

Congress created three specific and narrow exceptions to the statutory definition of “electioneering communication”:

- (i) a “news media” exemption for any communication appearing in a news story, editorial, or commentary;¹
- (ii) an exemption for any communication that is otherwise an “expenditure” or “independent expenditure” under the FECA;² and
- (iii) an exemption for any communication that constitutes a “candidate debate or forum” under Commission rules.

2 U.S.C. §§ 434(f)(3)(B)(i)-(iii).

In addition, in clause (iv) of the same statutory section, Congress provided the Commission with carefully circumscribed discretion to exempt “any other communication ... under such regulations as the Commission may promulgate (consistent with the requirements of this paragraph) to ensure the appropriate implementation of this paragraph, except that under any such regulation a communication may not be exempted if it meets the requirements of this paragraph and is described in [2 U.S.C. § 431(20)(A)(iii)].” *Id.* at § 434(f)(3)(B)(iv). Section 431(20)(A)(iii), in turn, describes a public communication that promotes, attacks, supports, or opposes (the so-called “PASO” test) a federal candidate, regardless of whether the communication expressly advocates a vote for or against the candidate.³

Thus, the Commission’s clause (iv) authority to craft exemptions to the definition of “electioneering communication” has two important constraints: *First*, any such exemption must be “appropriate,” and “consistent” with the requirements of the underlying definition of “electioneering communication” — in other words, the regulatory exemption must not undermine the purpose of the statute to close the sham “issue ad” loophole. *Second*, any clause (iv) exemption must not exempt public communications that promote, support, attack or oppose a federal candidate. Such communications fall within the scope of 2 U.S.C. § 431(20)(A)(iii) and therefore are, by definition, outside the scope of the Commission’s clause (iv) authority.

Representative Shays, in discussing clause (iv) on the House floor, explained its purpose and exceedingly narrow scope:

¹ This provision mirrors the identical, and longstanding, “news media” exemption from the definition of “expenditure” in FECA. 2 U.S.C. § 431(9)(B)(i).

² Any such “expenditure” would independently be subject to full disclosure under 2 U.S.C. § 434 and to the ban on corporate and union spending under 2 U.S.C. § 441b. Thus, to include such expenditures within the definition of “electioneering communications” would have been redundant.

³ “The terms ‘Federal election activity’ means ... a public communication that refers to a clearly identified candidate for Federal office ... and that promotes or supports a candidate for that office, or attacks or opposes a candidate for that office (regardless of whether the communication expressly advocates a vote for or against a candidate).” 2 U.S.C. § 431(20)(A)(iii).

[I]t is possible that the[r]e could be some communications that will fall within this definition [of electioneering communication] even though they are *plainly and unquestionably not related to the election*.

Section 201(3)(B)(iv) [codified at 2 U.S.C. § 434(f)(3)(B)(iv)] was added to the bill to provide [the] Commission *with some limited discretion in administering the statute* so that it can issue regulations to exempt such communications from the definition of “electioneering communications” because they are *wholly unrelated to an election*.

148 Cong. Rec. H410-11 (daily ed. Feb. 13, 2002) (emphasis added). Representative Shays gave an example of the type of communication that would merit an exclusion — a broadcast of a religious service that mentions in passing the name of an elected official who is also a candidate. *Id.* at H411.

Representative Shays specifically and pointedly emphasized that clause (iv) would *not* authorize the Commission to promulgate any broad-brush exemption for section 501(c)(3) organizations: “[W]e do not intend that Section 201(3)(B)(iv) be used by the FEC to create any *per se* exemption from the definition of ‘electioneering communications’ for speech by Section 501(c)(3) charities.” *Id.*⁴ Representative Meehan⁵ and Senators Feingold⁶ and McCain⁷ explicitly concurred in this statement. Thus, the statutory language of clause (iv) was identically construed by not one, but by *all four* principal sponsors of BCRA – to specifically prohibit the very *per se* exemption for section 501(c)(3) groups that the Commission then nonetheless created. These contemporaneous views by the key sponsors of BCRA are entitled to substantial weight in the Commission’s statutory interpretation.⁸

⁴ Representative Shays did urge the Commission to consider whether standards developed by the IRS in administering Section 501(c)(3) could be applied “to exempt specific categories of speech where it is clear that such communications are made in a manner that is neutral in nature, wholly unrelated to an election, and cannot be used to promote or attack any federal candidates.” *Id.*

⁵ 148 Cong. Rec. E178-79 (Feb. 15, 2002).

⁶ 148 Cong. Rec. S2143 (daily ed. Mar. 20, 2002) (“Mr. Shays discussed how the provisions of the bill dealing with electioneering communications permit the FEC to promulgate regulations to exempt certain communications I also endorse that discussion, which appears in the Record of February 13, 2002, at pages H410-411.”).

⁷ *Id.* (“I agree with my friend from Wisconsin that these statements express our intent in this bill quite well.”).

⁸ Although “the statements of one legislator” during floor debate may not be “controlling,” the remarks made by a “sponsor of the language ultimately enacted are an authoritative guide to the statute’s construction.” *N. Haven Bd. of Educ. v. Bell*, 456 U.S. 512, 526-27 (1982). Courts give particular weight to “precise analyses of statutory phrases by the sponsors of the proposed laws.” *S&E Contractors, Inc. v. United States*, 406 U.S. 1, 13 n.9 (1972). Here, the statutory language in issue was identically construed by not one, but by *all four* principal sponsors.

II. The Supreme Court in *McConnell* upheld BCRA’s “electioneering communication” provisions in their entirety.

Plaintiffs in *McConnell v. FEC*, 540 U.S. 93 (2003), challenged on constitutional grounds the BCRA definition of “electioneering communication,” as well as the related disclosure provisions and the prohibition on corporation/labor organization payment for “electioneering communication.” The Supreme Court in *McConnell* upheld these provisions in every respect. *See id.* at 189-211.

A. The *McConnell* Court found the definition of “electioneering communication” to be an “easily understood,” constitutionally permissible alternative to the “functionally meaningless” express advocacy standard.

The Court began its analysis of BCRA’s various “electioneering communication” provisions by examining the statutory definition of “electioneering communication,” which underlies the disclosure requirements and the corporation/labor organization prohibition. The Court began:

The major premise of plaintiffs’ challenge to BCRA’s use of the term “electioneering communication” is that *Buckley* drew a constitutionally mandated line between express advocacy and so-called issue advocacy, and that speakers possess an inviolable First Amendment right to engage in the latter category of speech. ... That position misapprehends our prior decisions, for the express advocacy restriction was an endpoint of statutory interpretation, not a first principle of constitutional law.

Id. at 190. The Court continued: “In narrowly reading the FECA provisions in *Buckley* to avoid problems of vagueness and overbreadth, we nowhere suggested that a statute that was neither vague nor overbroad would be required to toe the same express advocacy line.” *Id.* at 192.

The Court recognized and explained the importance of BCRA’s “electioneering communication” provisions:

Indeed, the unmistakable lesson from the record in this litigation, as all three judges on the District Court agreed, is that *Buckley*’s magic-words requirement is functionally meaningless. Not only can advertisers easily evade the line by eschewing the use of magic words, but they would seldom choose to use such words even if permitted. And although the resulting advertisements do not urge the viewer to vote for or against a candidate in so many words, they are no less clearly intended to influence the election. *Buckley*’s express advocacy line, in short, has not aided the legislative effort to combat real or apparent corruption, and Congress enacted BCRA to correct the flaws it found in the existing system.

Id. at 193-94 (footnotes omitted)(internal citations omitted)(quoting *McConnell v. FEC*, 251 F. Supp. 2d 176, 303-304 (D.D.C. 2003)(Henderson, J.); *id.* at 534 (Kollar-Kotelly, J.); *id.*, at 875-879 (Leon, J.).

To illustrate the need for BCRA’s “electioneering communication” provisions, the Court noted a “striking example” of a sham issue ad by the 501(c)(4) organization “Citizens for Reform.”⁹ The ad stated:

Who is Bill Yellowtail? He preaches family values but took a swing at his wife. And Yellowtail’s response? He only slapped her. But ‘her nose was not broken.’ He talks law and order ... but is himself a convicted felon. And though he talks about protecting children, Yellowtail failed to make his own child support payments-then voted against child support enforcement. Call Bill Yellowtail. Tell him to support family values.

McConnell, 540 U.S. at 194 n.78 (quoting 5 1998 Senate Report 6305 (minority views)). The Court concluded: “The notion that this advertisement was designed purely to discuss the issue of family values strains credulity.” *Id.*

The Court found that BCRA’s definition of “electioneering communication” “raises none of the vagueness concerns that drove our analysis in *Buckley*.” *Id.* 194. According to the Court, the definition of “electioneering communication” is “both easily understood and objectively determinable.” The Court upheld the definition as constitutional, concluding: “the constitutional objection that persuaded the Court in *Buckley* to limit FECA’s reach to express advocacy is simply inapposite here.” *Id.*

B. The *McConnell* Court found BCRA’s “electioneering communications” disclosure requirements advance the government’s important interests in informing the electorate, preventing real and apparent corruption, and facilitating enforcement of other campaign finance restrictions.

Plaintiffs in the *McConnell* litigation likewise challenged BCRA’s “electioneering communications” disclosure requirements. The Court upheld the disclosure provisions, stating:

We agree with the District Court that the important state interests that prompted the *Buckley* Court to uphold FECA’s disclosure requirements — providing the electorate with information, deterring actual corruption and avoiding any appearance thereof, and gathering the data necessary to enforce more substantive electioneering restrictions — apply in full to BCRA. Accordingly, *Buckley* amply supports application of FECA § 304’s disclosure requirements to the entire range of “electioneering communications.”

⁹ Two 501(c)(4) organizations, “Citizens for Reform” and “Citizens for the Republic Education Fund,” both run by the for-profit corporation Triad Management Services, spent between \$3 and \$4 million in 1996 on television ads in support of Republican candidates in 29 House and Senate races. See Michael Trister, *The Rise and Fall of Stealth PACs*, AM. PROSPECT, Sept. 24, 2000, available at <http://www.prospect.org/print/V11/21/trister-m.html>.

McConnell, 540 U.S. at 196 (footnote omitted).

C. The *McConnell* Court found the BCRA prohibition of corporate “electioneering communication” narrowly tailored to advance the government’s compelling interest in eliminating the “corrosive and distorting effects” of wealth on the political process.

Plaintiffs in *McConnell* challenged BCRA’s prohibition of corporation/labor organization payment for an “electioneering communication” on the grounds that the ban was both overbroad and underinclusive. *Id.* at 204. Resolving the challenge required the Court to examine the degree to which BCRA’s “electioneering communication” provisions burden First Amendment expression, and to evaluate whether a compelling governmental interest justifies the burden. The Court reasoned: “The latter question — whether the state interest is compelling — is easily answered by our prior decisions regarding campaign finance regulation, which ‘represent respect for the legislative judgment that the special characteristics of the corporate structure require particularly careful regulation.’” *Id.* at 205 (quoting *FEC v. Beaumont*, 539 U.S. 146, 155 (2003); *FEC v. National Right to Work Comm.*, 459 U.S. 197, 209-210 (1982)). The Court continued: “We have repeatedly sustained legislation aimed at ‘the corrosive and distorting effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public’s support for the corporation’s political ideas.’” *Id.* (quoting *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652, 660 (1990)).

The plaintiffs did not challenge this long-recognized government interest in regulating corporate political activity. “Rather, plaintiffs argue[d] that the justifications that adequately support the regulation of express advocacy do not apply to significant quantities of speech encompassed by the definition of electioneering communications.” *McConnell*, 540 U.S. at 205-06. The Court rejected this overbreadth argument, reasoning:

This argument fails to the extent that the issue ads broadcast during the 30- and 60-day periods preceding federal primary and general elections are the *functional equivalent of express advocacy*. The justifications for the regulation of express advocacy apply equally to ads aired during those periods if the ads are intended to influence the voters’ decisions and have that effect. The precise percentage of issue ads that clearly identified a candidate and were aired during those relatively brief preelection time spans but had no electioneering purpose is a matter of dispute between the parties and among the judges on the District Court. *Nevertheless, the vast majority of ads clearly had such a purpose.*

Id. at 206 (emphasis added)(internal citations omitted)(citing *McConnell v. FEC*, 251 F.Supp.2d 176, 307-312 (D.D.C. 2003)(Henderson, J.); *id.* at 583-587 (Kollar-Kotelly, J.); *id.* at 796-798 (Leon, J.).

The Court “was not persuaded that plaintiffs ha[d] carried their heavy burden of proving” that BCRA’s corporation/labor organization “electioneering communication” prohibition is overbroad. *McConnell*, 540 U.S. at 207. The Court was likewise unpersuaded that the prohibition is impermissibly underinclusive because it does not apply to the print media or the Internet, finding that “reform may take one step at a time, addressing itself to the phase of the

problem which seems most acute to the legislative mind,” and holding that the evidentiary record in the case “amply justifies Congress’ line drawing.”

Finally — and importantly to this rulemaking— plaintiffs in *McConnell* challenged the application of BCRA’s corporate “electioneering communication” ban to nonprofit corporations. The Court made short work of the challenge, reasoning:

Prior to the enactment of BCRA, FECA required such [nonprofit] corporations, like business corporations, to pay for their express advocacy from segregated funds rather than from their general treasuries. Our recent decision in *Federal Election Comm’n v. Beaumont*, 539 U.S. 146 (2003), confirmed that the requirement was valid except insofar as it applied to a subcategory of corporations described as “*MCFL* organizations,” as defined by our decision in *MCFL*, 479 U.S. 238 (1986). The constitutional objection to applying FECA’s segregated-fund requirement to so-called *MCFL* organizations necessarily applies with equal force to [BCRA’s corporate “electioneering communication” prohibition].

McConnell, 540 U.S. at 209-10 (footnote omitted). The Court concluded: “Indeed, the Government itself concedes that [BCRA’s corporate “electioneering communication” prohibition] does not apply to *MCFL* organizations. As so construed, the provision is plainly valid.” *Id.* at 211.

In short, the Supreme Court in *McConnell* recognized that BCRA’s “electioneering communication” provisions are a constitutionally permissible means of closing the sham issue ad loophole and eliminating the corrosive and distorting effects of corporate wealth on the political process.

III. The Commission’s First “Electioneering Communication” Rulemaking

In August 2002, the Commission published NPRM 2002-13, seeking comment on proposed rules regarding the definition of “electioneering communication.” 67 Fed. Reg. 51131 (August 7, 2002). The Campaign Legal Center, Democracy 21 and the Center for Responsive Politics each submitted written comments on the notice.¹⁰

The “electioneering communication” rule proposed in NPRM 2002-13 contain neither the *per se* exemption for 501(c)(3) organizations, nor the “for a fee” requirement – the two provisions that were successfully challenged in the *Shays* litigation, necessitating the present rulemaking.

¹⁰ See Comments of Campaign Legal Center on Notice 2002-13 (August 21, 2002); Comments of Democracy 21 on Notice 2002-13 (August 22, 2002); Comments of the Center for Responsive Politics on Notice 2002-13 (August 21, 2002).

A. Genesis of the existing 501(c)(3) *per se* exception.

NPRM 2002-13 proposed the creation of multiple exceptions to the regulatory definition of “electioneering communication” — several of which reflected exceptions appearing in the statute, but many of which did not. The current commenters each generally supported proposed rules implementing exceptions found in the statute, and generally opposed the creation of new exceptions not found in the statute.¹¹

The proposed rule made no mention of the possibility that the Commission might create a *per se* exception for corporations with section 501(c)(3) tax status. The term 501(c)(3) appeared only once in the NPRM — in reference to the fact that unincorporated 501(c)(3) organizations are permitted under BCRA to make payments for “electioneering communication.” 67 Fed. Reg. at 51137.

A number of organizations in written comments or testimony urged the Commission to adopt a *per se* exemption for section 501(c)(3) organizations.¹² The General Counsel’s proposed final regulations explicitly *rejected* this idea as inconsistent with the law. His proposed E&J accompanying a proposed final rule explained:

The Commission has decided not to include a *per se* exemption for a communication by an organization described in 26 U.S.C. 501(c)(3). *Such a blanket exemption is too broad for the limited exemption authority BCRA provides to the Commission.* The Commission also has rejected a limited exemption based on the provisions of the Internal Revenue Code. While the Commission defers to the Internal Revenue Service’s enforcement of the Internal Revenue Code, the civil enforcement of BCRA lies within the jurisdiction and responsibility of this Commission and cannot be left to another agency’s policing of those subject to another statute.¹³

The Commission, however, ignored both clear expressions of legislative intent and the advice of its General Counsel, and amended the proposed final regulations to include an exemption from the definition of “electioneering communication” for *any* communication that “is paid for by any organization operating under Section 501(c)(3) of the Internal Revenue Code of 1986.” 11 C.F.R. § 100.29(c)(6).

¹¹ See Comments of Campaign Legal Center on Notice 2002-13 at 6-13; Comments of Democracy 21 on Notice 2002-13 at 7-13; Comments of the Center for Responsive Politics on Notice 2002-13 at 4-7.

¹² See, e.g., Comments of Alliance for Justice on Notice 2002-13, 2-5 (August 21, 2002); Comments of OMB Watch on Notice 2002-13, 5-7 (August 21, 2002); Comments of Independent Sector on Notice 2002-13, 7-8 (August 21, 2002); FEC, Transcript from Aug. 28, 2002 Public Hearing on Electioneering Communications, Testimony of Tim Mooney, Alliance for Justice, pp. 208-70; Testimony of Lloyd Mayer, Independent Sector, pp. 204-70. See also FEC, Transcript from Aug. 29, 2002 Public Hearing on Electioneering Communications, Testimony of Kay Guinane, OMB Watch, pp. 111-83.

¹³ Agenda Doc. No. 02-68, “Final Rule, Interim Final Rule, and Explanation and Justification for Electioneering Communications,” Sept. 24, 2002, at 48-9 (emphasis added).

In the E&J for the final rule, the Commission explicitly acknowledged the limitations on its power to create Title II exemptions, explaining:

In addition to the exemptions expressly created by BCRA, the statute also provides that “to ensure the appropriate implementation” of the electioneering communication provisions, the Commission may promulgate regulations exempting other communications from the “electioneering communications” definition. 2 U.S.C. 434(f)(3)(B)(iv). However, the statutory authorization to exempt communications is expressly limited in two ways. The exemption must be promulgated consistent with the requirements of the new electioneering communication provision, and *the exempted communication must not be a “public communication” that refers to a clearly identified candidate for Federal office and that promotes or supports a candidate for that office, or attacks or opposes a candidate for that office.* 2 U.S.C. 434(f)(3)(B)(iv) (referencing 2 U.S.C. 431(20)(A)(iii)).

67 Fed. Reg. at 65198 (emphasis added).

Yet the *per se* exemption for section 501(c)(3) groups on its face exempted *all* public communications by section 501(c)(3) organizations that would otherwise be “electioneering communications” — even one that “refers to a clearly identified candidate for Federal office and that promotes or supports a candidate for that office, or attacks or opposes a candidate for that office.”

B. Genesis of the existing “for a fee” restriction.

NPRM 2002-13 proposed clarification of the statutory definition of “electioneering communication” by replacing the statutory term “made,” 2 U.S.C. § 434(f)(3)(A)(II), with the term “publicly distributed.” 67 Fed. Reg. at 51132. The NPRM proposed rule, in turn, defined the term “publicly distributed” to mean “aired, broadcast, cablecast or otherwise disseminated through the facilities of a television station, radio station, cable television system, or satellite system.” 67 Fed. Reg. at 51145 (proposed 11 C.F.R. § 100.29(b)(6)).

The current commenters each supported the proposed definition of “publicly distributed.”¹⁴ In the final rule, however, the Commission modified the definition of “publicly distributed” to mean “aired, broadcast, cablecast or otherwise disseminated *for a fee* through the facilities of a television station, radio station, cable television system, or satellite system.” Electioneering Communications Final Rules and Explanation and Justification (E&J), 67 Fed. Reg. 65190, 65211 (Oct. 23, 2002)(11 C.F.R. § 100.29(b)(3)(i))(emphasis added). The Commission concluded: “Based on the legislative history of BCRA, the Commission has determined that electioneering communications should be limited to paid programming.” 67 Fed. Reg. at 65193.

¹⁴ See Comments of Campaign Legal Center on Notice 2002-13 at 4; Comments of Democracy 21 on Notice 2002-13 at 4; Comments of the Center for Responsive Politics on Notice 2002-13 at 1.

These two provisions of the Commission’s “electioneering communication” regulations, along with many other regulations implementing BCRA, were challenged by BCRA’s principal congressional sponsors in federal court.

IV. *Shays v. FEC*

The present rulemaking is necessitated by federal district and appellate court decisions in *Shays v. FEC*, 337 F. Supp. 2d 28 (D.D.C. 2004) *aff’d* 414 F.3d 76 (D.C. Cir. 2005), which invalidated the *per se* exemption for section 501(c)(3) groups, and the “for a fee” rule.

The district court in *Shays* began its examination of the “electioneering communication” rule by attempting to discern whether the section 501(c)(3) exemption was a permissible construction of the statute under so-called *Chevron* analysis. The court found:

It is clear that the validity of the Commission’s regulation depends on whether or not the tax laws and regulations, as well as their enforcement, effectively prevent Section 501(c)(3) groups from issuing “public communications” that promote or oppose a candidate for federal office. It is the FEC, not the IRS, that is charged with enforcing FECA. ... [A] prerequisite to the FEC enforcing its exemption is the completion of enforcement action by the IRS pursuant to “its own standards for enforcing the tax code.” This is troubling, given the fact, as acknowledged by the Commission, ... that the IRS in the past has not viewed Section 501(c)(3)’s ban on political activities to encompass activities that are so considered under FECA.

Shays, 337 F. Supp. 2d at 126–27. The court continued:

It is therefore not clear to the Court whether or not the IRS will conform its views on political activity under the tax laws to those regulated in the realm of campaign finance law. Accordingly, the Court finds the record unclear as to whether the Commission’s regulation, by relying on the IRS’s views on “participat[ion] in, or interven[tion] in ... any political campaign on behalf of (or in opposition to) any candidate for public office,” 26 U.S.C. § 501(c)(3), meets the requirements set forth by Congress in 2 U.S.C. § 434(f)(3)(B). The Court finds that this lack of clarity precludes it from determining whether or not the regulation fails *Chevron* review.

Id.

Although the district court refrained from declaring the section 501(c)(3) exemption invalid on *Chevron* grounds, the court held that “the Commission failed to conduct a ‘reasoned analysis’ and therefore the regulation violates the APA.” *Id.* at 127. The court noted several deficiencies with the Commission’s E&J for the 501(c)(3) exemption:

Absent from its explanation ... is any discussion of the compatibility of the IRS’s enforcement of the ban on political activity of Section 501(c)(3) groups and

FECA's requirements; specifically, the FEC did not discuss whether or not the IRS viewed as political activity "public communications" that support or oppose a candidate as those concepts are understood under this nation's campaign finance laws. Moreover, the FEC did not note that tax laws permit Section 501(c)(3) organizations to engage in limited lobbying activities, or discuss the risk, if any, that such activities could run afoul of 2 U.S.C. § 434(f)(3)(B)(iv). *See* 26 U.S.C. § 501(c)(3), (h). Nor did the Commission address the implications of allowing the IRS to take the lead in campaign finance law enforcement. It is clear from its E & J that if a Section 501(c)(3) organization does make a "public communication" that supports or opposes a candidate, the FEC would do nothing until the IRS investigated and decided whether or not the organization violated the tax laws. The effectiveness of this sort of enforcement should have been at least mentioned.

Id. The district court concluded:

In short, the Commission did not fully address whether the tax code does preclude Section 501(c)(3) organizations from making the "public communications" FECA requires be regulated, and how its delegation of the first response to potential violations to the IRS would impact enforcement of the campaign finance laws. In this way, the Court finds that the agency has "entirely failed to consider ... important aspect[s] of the problem," which renders its rule arbitrary and capricious.

Id. at 128 (quoting *Motor Vehicle Mfrs. Ass'n of the United States, Inc. v. State Farm Mutual Auto. Ins. Co.*, 463 U.S. 29, 43 (1983)).

Having found the Commission's 501(c)(3) exemption arbitrary and capricious, the district court then turned to the "for a fee" requirement. The court applied *Chevron* step one analysis and flatly rejected the Commission's argument that the statutory language is susceptible to the Commission's "for a fee" interpretation.

Congress in enacting BCRA provided that certain communications were not to be considered "electioneering communications." 2 U.S.C. § 434(f)(3)(B)(i)-(iii). It also included a provision delegating authority to the FEC to create exemptions for communications, but limited the Commission's authority by expressly prohibiting from exemption "public communications" "that promote[] or support [] a candidate for [federal] office, or attacks or opposes a candidate for [federal] office." *Id.* § 434(f)(3)(B)(iv), 431(20)(A)(iii). ... Here the FEC has exempted from regulation *all* communications, regardless of their content, provided that a fee is not paid for their broadcast. This cannot be squared with the plain meaning of BCRA's text. Accordingly, the Court finds that the Commission's "for a fee" requirement violates *Chevron* step one.

Id. at 128-29 (footnotes omitted).

The Commission appealed the district court's decision with regard to the "for a fee" requirement, but did not appeal the district court's invalidation of the 501(c)(3) exemption. *See Shays*, 414 F.3d 76, 107-09 (D.C. Cir. 2005). The D.C. Circuit Court of Appeals explained the "for a fee" legal issue as follows:

According to *Shays* and *Meehan*, nothing in the statute supports limiting "electioneering communications" to *purchased* transmissions. As the Congressmen see it, the statute applies equally to unpaid broadcasts, such as public service announcements. Indeed, they worry that sham PSAs could become the new sham issue ads — communications evading regulation though functionally indistinguishable from campaign ads. To give an example used by the FEC in the very rulemaking here, supporters could "us[e] a PSA to associate a Federal candidate with a public-spirited endeavor" — say, a blood drive or veterans' support effort — "in an effort to promote or support that candidate." Electioneering Communications, 67 Fed. Reg. 65,190, 65,202 (Oct. 23, 2002). Indeed, given a friendly broadcaster willing to forgo its fee, supporters could even air unambiguous election aids, i.e., ads clearly identifying a federal candidate, targeting the relevant electorate, and appearing close to the election.

Id. at 108.

The court of appeals agreed with the district court finding that "the FEC's definition violated Congress's clearly expressed intent under *Chevron* step one. The court explained:

In effect, the Commission has taken the three parts of BCRA's standard — (1) candidate identification, (2) within 30 or 60 days, and (3) targeted at the electorate — and added a fourth: "for a fee." Nothing in the statute suggests that Congress contemplated such an element. Certainly, the word "made" carries no such connotation. When one says, "dinner is made," the implication is that dinner exists, not that someone paid for it. Likewise here, to say a "broadcast, cable, or satellite communication ... is made" implies quite simply that the communication exists — i.e., that it was transmitted — not that someone paid a fee to make the transmission happen.

Id.

The court of appeals rejected the Commission's argued justifications for the "for a fee requirement," in particular the Commission's claim that its requirement was necessary to prevent the chilling of "entertainment, educational, and documentary programs that mention or portray a federal candidate only incidentally," as well as PSAs featuring federal candidates and "encouraging citizens to donate blood, for example." *Id.* at 109. The court noted that this rationale was never given during the rulemaking process, and that it need not be considered given that the court ruled on *Chevron* grounds. Nonetheless, the court found it:

...worth pointing out that avoiding chilling particular types of communication could hardly justify the FEC's broad exclusion of *all* unpaid broadcasts,

regardless of content. Furthermore, because BCRA already includes an express exemption for “communication[s] appearing in a news story, commentary, or editorial,” 2 U.S.C. § 434(f)(3)(B)(i), no further exemption was necessary to avoid chilling those. As for PSAs, excluding federal candidates from broadcasts promoting blood drives and other worthy causes for 90 days out of every two years (30 days before the primary plus 60 days before the general election) would hardly seem unreasonable given that such broadcasts could “associate a Federal candidate with a public-spirited endeavor in an effort to promote or support that candidate” — a risk the FEC itself acknowledged, in the very same rulemaking, in justifying its refusal to promulgate a general exemption for PSAs (whether paid or unpaid), *see* 67 Fed. Reg. at 65,202.

Id. The court thus held that the regulation “contradicts BCRA’s plain text and thus fails *Chevron* step one,” and that insofar as the “for a fee” requirement constitutes an exemption, “it runs roughshod over express limitations on the Commission’s power, thus again flunking *Chevron* one.” *Id.* The court of appeals affirmed the district court’s invalidation of the “for a fee” requirement and concluded:

As the Supreme Court (rather fatalistically) observed in *McConnell*, “Money, like water, will always find an outlet.” 540 U.S. at 224, 124 S. Ct. 619. Offered there as a reason for “no illusion that BCRA will be the last congressional statement on [campaign finance],” *id.*, this comment serves equally well here to illustrate the importance of faithfully implementing the statute Congress has passed. For if regulatory safe harbors permit what BCRA bans, we have no doubt that savvy campaign operators will exploit them to the hilt, reopening the very soft money floodgates BCRA aimed to close. Because the rules at issue in this appeal either fall short of Congress’s mandate or lack record support showing otherwise, we affirm their invalidation by the district court.

Id. at 115.

V. Exemption for Section 501(c)(3) Organizations—11 C.F.R. § 100.29(c)(6).

As noted above, the *per se* exemption for section 501(c)(3) organizations from the definition of “electioneering communication” was challenged and invalidated in *Shays*. As noted in NPRM 2005-20, the district court identified three specific deficiencies of the E&J:

- i. The E&J did not discuss whether or not public communications that PASO a Federal candidate would be viewed by the IRS as political activity in which section 501(c)(3) organizations may not engage;
- ii. The E&J did not discuss the risk, if any, that lobbying activity permitted for section 501(c)(3) organizations could give rise to advertisements that PASO a Federal candidate; and

iii. The E&J did not address the implications of allowing the IRS “to take the lead in campaign finance law enforcement.”

70 Fed. Reg. at 49510. NPRM 2005-20 discusses the court’s three concerns in order.

A. PASO Communications as Political Activity

Section 501(c)(3) tax status is available to charitable organizations that do not “participate in, or intervene in ... any political campaign on behalf of (or in opposition to) any candidate for public office.” 26 U.S.C. § 501(c)(3). The IRS has interpreted this tax code section to allow far more political activity by section 501(c)(3) organizations than Congress intended to permit when it enacted BCRA’s prohibition on a corporation’s use of treasury funds to pay for “electioneering communication.” Despite claims to the contrary made by various organizations during the 2002 rulemaking, IRS enforcement of section 501(c)(3) of the tax code does not effectively prevent section 501(c)(3) organizations from engaging in “electioneering communications” that could impact federal elections. Section 501(c)(3) organizations can and do distribute communications that “promote, support, attack or oppose” candidates for public office while acting lawfully within their tax-exempt status. For this reason, a *per se* section 501(c)(3) exemption from the definition of “electioneering communication” constitutes an impermissible construction of BCRA’s Title II provisions. We urge the Commission to eliminate the section 501(c)(3) exemption found at 11 C.F.R. § 100.29(c)(6).

1. The administrative record. In the NPRM, the Commission admits the inadequacy of record support for a *per se* exemption from Title II for section 501(c)(3) groups. 70 Fed. Reg. at 49510. (there is “a limited record for the Commission to exempt all section 501(c)(3) organizations’ communications.”) This is correct. Indeed, the record makes clear that 501(c)(3) organizations can and do engage in “electioneering communications” of the type that Congress intended Title II to cover.

The NPRM notes that one section 501(c)(3) organization that submitted written comments in the 2002 rulemaking, the Southeastern Legal Foundation, “stated that it does engage in issue advocacy that includes broadcast advertisements that refer to candidates and officeholders, and implied that these advertisements may well PASO a candidate.” 70 Fed. Reg. at 49510.

The Commission further notes that “the record in *Shays v. FEC* includes press reports describing a radio ad run by a section 501(c)(3) organization, the Federation for American Immigration Reform (“FAIR”), that appears to attack or oppose a Federal candidate.” *Id.* The text of the ad stated:

This is an urgent message about our jobs. Senator Spence Abraham is again pushing a bill to import hundreds of thousands more foreign workers to take American jobs—our jobs. * * * Recently Abraham killed the requirement that employers hire Americans first. He clearly thinks it’s OK to favor foreign workers. Why treat Americans so badly? Money. Abraham has raised big political money from huge corporations that want cheap, foreign labor. And his

newest bill gives them everything they want. Is your job next? Let's try to convince Abraham not to sell our jobs. His bill could be voted on any day. So call now: 1-800-xxx-xxxx. That's 1-800-xxx-xxxx. Tell him you've had enough of his big foreign labor bills, like S. 2045. This message sponsored by the Federation for American Immigration Reform. Visit our website at fairUS.org.

Id. This advertisement is precisely the sort of sham issue ad that the sponsors of BCRA sought to regulate through adoption of BCRA's "electioneering communication" provisions.¹⁵

The Commission asks: "To the extent that section 501(c)(3) organizations pay for advertisements similar to the one by FAIR described above, do the section 501(c)(3) organizations broadcast their advertisements during the 30- and 60-day electioneering communication windows?" 70 Fed. Reg. at 49510. This question misses the point, which is whether a section 501(c)(3) organization *could*, consistent with its tax status, sponsor broadcast ads that implicate the congressional concerns behind Title II. If the IRS interpretation of section 501(c)(3) allows (or effectively fails to prevent) such organizations to air ads of the sort Congress intended Title II to cover in the BCRA window, then it would be contrary to BCRA for the Commission to create a BCRA exemption for such organizations.

Perhaps the most compelling evidence that IRS enforcement of section 501(c)(3) does not prevent covered corporations from engaging in PASO communications is IRS Technical Advice Memorandum 89-36-002 (Sept. 8, 1989), cited by the Commission in the NPRM. In that TAM, the IRS "'reluctantly conclude[d]' that television advertisements by a section 501(c)(3) organization that would be generally understood to 'support or oppose a candidate in an election campaign' did not constitute intervention in a political campaign because the communication was core to the organization's mission." *Id.* (quoting IRS Technical Advice Memorandum 89-36-002, *supra*).¹⁶

¹⁵ We offer another example of alleged political activity by a section 501(c)(3) group. In July 2002, during an Arkansas gubernatorial election, a section 501(c)(3) corporation named the Next Step Foundation launched a radio and television ad campaign featuring incumbent candidate Gov. Mike Huckabee. The Next Step Foundation, led by a political consultant who worked for past Huckabee campaigns, claimed the purpose of the ads was to promote the governor's education policy. The state Democratic Party director, however, complained that "Next Step is a political smoke screen Huckabee is hiding behind to get on TV. ... This is a disgusting abuse of ethics and power. Not surprisingly, some of Huckabee's top campaign supporters are also top contributors to Next Step." James Jefferson, "Fischer Says Huckabee Education Ads Skirt Campaign Law," ASSOCIATED PRESS STATE AND LOCAL WIRE, July 17, 2002. *See also* Seth Blomeley, "Next Step Ads Bend Campaign Law," ARKANSAS DEMOCRAT-GAZETTE, July 17, 2002, at B1; Laura Kellams, "Two Next Step Groups To Push For Huckabee's Education Plan," ARKANSAS DEMOCRAT-GAZETTE, June 25, 2002, at B1. In September 2002, less than two month before the general election, Next Step shifted its advertising campaign from ads featuring the incumbent governor, to ads criticizing the education plan of the governor's opponent. James Jefferson, "Huckabee Defends Foundation's Criticism of Fisher," ASSOCIATED PRESS STATE AND LOCAL WIRE, Sept. 18, 2002.

¹⁶ The Commission asks how it should "interpret the Technical Advice Memorandum, which does not have precedential authority?" 70 Fed. Reg. 49510. Much like FEC advisory opinions, IRS technical advice memoranda guide the regulated community in their understanding of, and compliance with, federal

The NPRM asks for evidence of the “extent to which have section 501(c)(3) organizations availed themselves” of the current exemption from the Title II rules. 70 Fed. Reg. at 49511. We think this is a useful inquiry. If the record fails to demonstrate that a large number of section 501(c)(3) groups utilized the exemption during the relevant windows in the 2004 cycle, it would undermine any argument that the exemption is necessary.

In the 2002 rulemaking, some charitable groups argued that the application of BCRA’s “electioneering communication” provisions to charities would impair legitimate lobbying activities by such groups. Of course, the same claim against Title II was made to Congress by section 501(c)(4) groups and, indeed, by all corporations and labor unions covered by the statute. Public comments submitted in the 2002 rulemaking did not produce a record of *actual lobbying ads* run by section 501(c)(3) groups that would be swept up by the BCRA’s “electioneering communication” provisions, in order to justify the broad exemption adopted by the Commission. Absent such a record in 2004, or in the years prior to BCRA, there is no record basis to justify a re-promulgation of the exemption.

On the other hand, if any ads were run by section 501(c)(3) groups in 2004 that would have been “electioneering communications” but for the exemption, the Commission should closely scrutinize such ads to determine if they in fact promoted or attacked a candidate. The burden of proof here should be on those who support a continuation of the exemption, to show that it is necessary and appropriate, and would not undermine the Title II provisions.

2. The NPRM’s proposed limitations on the exemption. In addition to seeking comment on the adequacy of the administrative record supporting the current exemption, the NPRM proposes to amend the current rule by limiting the exemption in two respects. “First, the exemption would not apply to communications that PASO a Federal candidate. Second, the exemption would not apply to section 501(c)(3) organizations that are directly or indirectly established, financed, maintained or controlled by a Federal candidate or officeholder.” 70 Fed. Reg. at 49511.

We oppose re-promulgating a section 501(c)(3) exemption, even in this modified form. Instead, the exemption should be repealed in its entirety.

Although it is obviously correct to say that a charity “established, financed, maintained or controlled” by a Federal candidate or officeholder should not be permitted to run “electioneering communications,” that modest limitation on the scope of the exemption is far too under-inclusive to satisfy the statutory provision or congressional intent.

tax law. Although not vested with “precedential authority,” these memoranda provide valuable insight into the IRS’ understanding of the laws it enforces. The Commission should interpret Technical Advice Memorandum 89–36–002 as a clear statement that the IRS considers television advertisements by 501(c)(3) organizations, which might fit within the definition of “electioneering communication” and which might promote or attack a candidate, to be permissible so long as the communication is “core to the organization’s mission.”

The proposed PASO limitation also fails, because it undermines the whole point of the statute, which is to provide a “bright line” test for what constitutes an “electioneering communication.” And the proposal raises constitutional questions because it would impose a PASO standard that is not appropriate for application to individuals and entities other than candidates, political committees or other groups with a principal purpose to influence elections.

Congress in BCRA recognized that application of the PASO standard to entities other than “major purpose” groups might raise concerns of constitutional vagueness. It was those concerns that led the Supreme Court in *Buckley v. Valeo*, 424 U.S. 1 (1976), to narrowly construe the statutory phrase “for the purpose of influencing” to be limited to “express advocacy,” when applied to entities other than “major purpose” groups such as political committees. *Id.* at 77-79.

The *Buckley* Court did not, however, narrowly construe the definition of “expenditure” as applied to political committees – “organizations that are under the control of a candidate or the major purpose of which is the nomination or election of a candidate” – because “[e]xpenditures of candidates and of ‘political committees’ so construed can be assumed to fall within the core area sought to be addressed by Congress. They are, by definition, campaign related.” *Id.* at 79.

When enacting BCRA, Congress understood that the Supreme Court had held in *Buckley* that all expenditures by *political committees* “for the purpose of influencing a federal election” could be regulated without a concern for vagueness of that standard. This same is true for the closely related PASO test. Thus, in BCRA, Congress applied the PASO standard to the activities of state political party committees — entities with a self-proclaimed major purpose of influencing elections — as a means of defining and regulating political party “federal election activity.” 2 U.S.C. § 431(20)(A)(iii); see *McConnell v. FEC*, 540 U.S. 93, 170, n.64 (2003) (upholding constitutionality of PASO test against vagueness challenge as applied to state political party committees).

By contrast, in order to avoid any constitutional infirmities, Congress enacted BCRA’s bright-line “electioneering communication” standard in Title II for entities *other than* political committees. The Supreme Court in *McConnell* found that BCRA’s definition of “electioneering communication” “raises none of the vagueness concerns that drove our analysis in *Buckley*.” *McConnell*, 540 U.S. at 194. According to the Court, the definition of “electioneering communication” is “both easily understood and objectively determinable.” The Court upheld the definition as constitutional, concluding: “the constitutional objection that persuaded the Court in *Buckley* to limit FECA’s reach to express advocacy is simply inapposite here.” *Id.*

The Commission now proposes, in effect, to write a regulation to replace the clearly constitutional bright-line standard of Title II with the PASO test, by making the determination of whether a broadcast ad is an “electioneering communication” turn on whether it contains a PASO message. But for reasons stated above, this is potentially unconstitutional as applied to entities, such as section 501(c)(3) corporations, which are not “major purpose” entities. This proposed regulation would clearly undermine congressional intent to enact a bright-line, constitutional test for distinguishing between regulated electioneering speech by non-“major

purpose” entities, and other speech by such entities which is not subject to regulation under federal campaign finance laws.

The Commission correctly notes in the NPRM that the Supreme Court in *McConnell* rejected a vagueness challenge to the PASO standard, holding that PASO provisions — *with respect to political parties* — “provide explicit standards for those who apply them and give the person of ordinary intelligence a reasonable opportunity to know what is prohibited.” 70 Fed. Reg. at 49511 (quoting *McConnell*, 540 U.S. at 170 n.64). The NPRM, however, quotes only part of the Supreme Court passage. The Court went on to explain that the PASO standard is not unconstitutionally vague *as applied to political party committees* because “actions taken by political committees are presumed to be in connection with election campaigns.” *McConnell*, 540 U.S. at 170 n.64 (citing *Buckley*, 424 U.S. at 79). The constitutionality of the PASO standard as applied to entities other than “major purpose” groups such as political committees is far from certain.

3. Endorsement Ads. The Commission seeks comment on whether its conclusion in Ad.Op. 2003–25 that a federal candidate’s endorsement does not PASO that federal candidate was correct, and whether the conclusion can be applied in the context of communications by section 501(c)(3) organizations. 70 Fed. Reg. at 49511. In AO 2003-25, the Commission properly applied the PASO test to a political committee, and determined that the advertisement in question did not PASO a federal candidate. Ad. Op. 2003-25 at 4. The Commission further found that the advertisement were not “electioneering communication” because they ran outside of the “electioneering communication” time frame.

The Commission also cites an example of a public service announcement that was the subject of Ad.Op. 2004-14, and asks if the communication should be exempt under a non-PASO standard. *Id.* In Ad.Op. 2004-14, the advertisement ran outside of the “electioneering communication” window and the Commission correctly advised the requestors that the communications were not “electioneering communication.” Because the entity paying for the advertisement in Ad.Op. 2004-14 was not a political committee, application of the PASO test would have been inappropriate.

In the context of discussing these advisory opinions, the Commission provides the following example of a hypothetical candidate endorsement, asking whether the advertisement should be exempt from the definition of “electioneering communication” as a non-PASO communication: “a section 501(c)(3) organization pays for a television advertisement that features a Federal candidate endorsing the section 501(c)(3) organization and the advertisement satisfies the timing and targeting elements of the definition of ‘electioneering communication.’” 70 Fed. Reg. at 49511.

We strongly oppose the creation of a *per se* rule that candidate “endorsements” of 501(c)(3) corporations are exempt from the definition of “electioneering communication.” As noted by the court of appeals in *Shays*, the mere association of a candidate with a “public spirited endeavor” could benefit and be desirable to the candidate. *Shays*, 414 F.3d at 109. Indeed, the Commission itself, in the 2002 rulemaking, *rejected* an exemption for PSA ads because it recognized that PSA ads “could be easily abused by using a PSA to associate a Federal candidate

with a public-spirited endeavor in an effort to promote or support that candidate,” that “historically PSAs have been used for ‘electorally related purposes’ and that such communications are ‘at the very heart of what the statute is trying to get to.’” 67 Fed. Reg. 65202.

The analogy suggested by the NPRM – that because a federal candidate’s endorsement of a state candidate does not PASO the federal candidate (*see* Ad.Op. 2003-25), therefore a federal candidate’s endorsement of a charity will also not PASO the federal candidate – is not logically correct. The good will and public support that could redound to a federal candidate by closely associating himself through an endorsement with a popular or sympathetic charity is likely to be much greater than the benefit a federal candidate would receive by endorsing a state candidate.

Furthermore, such an exemption would be indisputably contrary to the legislative history of BCRA’s “electioneering communication” provisions. Most obviously, it would directly conflict with Representative Shays’s explicit statement that the sponsors “do not intend” that clause (iv) be used “to create any per se exemption ... for speech by Section 501(c)(3) charities.” 148 Cong. Rec. at H411. If Congress had wanted to exempt all candidate endorsements of section 501(c)(3) corporations, it knew how to do so, as illustrated by the BCRA provisions that specifically address nonprofit advocacy groups organized under Section 501(c)(4).¹⁷

B. Lobbying Activity That May Include PASO Communications

The district court in *Shays* took issue with the Commission’s failure to discuss the risk that lobbying activities permissible under section 501(c)(3) could promote or attack federal candidates, and thus run afoul of the clause (iv) restriction on the Commission’s authority to enact a blanket section 501(c)(3) exemption. *See Shays*, 337 F. Supp. 2d at 128.

During the 2002 rulemaking on this subject, the Commission uncritically accepted the argument that the tax code’s prohibition on section 501(c)(3) groups “interven[ing]” in political campaigns would prevent them from running the type of sham “issue ads” that BCRA is aimed at. Yet, as Representative Shays pointed out, “[n]otwithstanding this prohibition, some such charities have run ads in the guise of so-called ‘issue advocacy’ that clearly have had the effect of promoting or opposing federal candidates.” 148 Cong. Rec. at H411.

More importantly, the Commission failed to take into account the possibility that section 501(c)(3) groups might become the *new* vehicles for evasion of the law, *precisely because* BCRA now bars those for-profit and nonprofit corporations which had run sham “issue ads” in the past from doing so in the future. Prior to BCRA, there was little incentive for section 501(c)(3) organizations to run such ads simply because section 501(c)(4) groups could do so, with less risk. Now that section (c)(4) groups are prohibited from using treasury funds to run such ads, the new law creates the incentives – and the threat – that this activity will shift to (c)(3) groups.

¹⁷ 2 U.S.C. § 441b(c)(2) allows corporations organized under Section 501(c)(4) of the tax code to fund “electioneering communications” if paid for “exclusively by funds provided directly by individuals” This provision was essentially superseded by the “Wellstone Amendment,” 2 U.S.C. § 441b(c)(6).

The threat is evidenced by the types of ads that charities *can* run, consistent with their tax status. Section 501(c)(3) organizations can engage in public communications, including broadcast ads, that support or oppose legislation. The tax code provides that section 501(c)(3) corporations may make expenditures “to influence any legislation through an attempt to affect the opinions of the general public,” 26 U.S.C. § 4911(d)(1)(A), so long as such expenditures do not constitute a “substantial part” of the organization’s activities, 26 U.S.C. § 501(c)(3), or do not exceed the lobbying expenditure ceiling, calculated as a percentage of the organization’s non-lobbying expenditures (approximately 20% but subject to an overall limit). *See* 26 U.S.C. §§ 501(h) and 4911. It is this *limit* on lobbying expenditures — not the act of lobbying itself — that distinguishes lobbying by section 501(c)(3) groups from lobbying by section 501(c)(4) groups. *Thus, section 501(c)(3) corporations may engage in lobbying activities identical to those of 501(c)(4) corporations, but must do so to a relatively lesser extent (as compared to their overall activities).*

In their efforts to affect public opinion or legislation, section 501(c)(3) corporations can refer to clearly identified candidates in broadcast communications aired in the period immediately before an election that are targeted to the electorate of the candidate mentioned. (Indeed, if this were not the case, then an exemption from the Title II rules for section 501(c)(3) groups would be a moot point).

This proposition is illustrated by the recent IRS discussion in Revenue Ruling (“Rev. Rul.”) 2004-6. *See* IRS Rev. Rul. 2004-6, *published in* Int. Rev. Bulletin 2004-4 (Jan. 26, 2004).¹⁸ There, the IRS uses six hypothetical advertisements to trace the line between lobbying activity and “exempt function” activity, which is defined under section 527(e)(2) of the IRC to include efforts to influence the nomination or election of individuals to public office.¹⁹ All six hypothetical advertisements identify a candidate, appear shortly before an election, and target the voters in that election — falling squarely within BCRA’s definition of “electioneering communication.” The IRS, however, has no bright-line test to distinguish between lobbying and “exempt function” activity (or electioneering). Instead, the IRS applies a nuanced “facts and circumstances” test, listing six factors that “tend to show” that an advertisement is candidate

¹⁸ By its terms, Rev. Rul. 2004-6 applies to section 501(c)(4), (5) and (6) organizations, not to section 501(c)(3) organizations. Yet there is no reason to believe that the discussion in the revenue ruling about what constitutes “lobbying” would be different for a section 501(c)(3) group than it is in the context of a section 501(c)(4) group. The relationship between the two is supported by the IRS regulations under section 501(c)(4), which cross-reference the regulations under section 501(c)(3) defining an “action organization,” thus illustrating the commonality of the definition of “lobbying” between the two provisions. *See* 26 C.F.R. § 1.501(c)(4)-1(a)(2)(ii) *citing id.* at § 1.501(c)(3)-(1)(c)(3)(ii), (iv).

¹⁹ The distinction is important for the section 501(c) groups covered by the Revenue Ruling. Such groups “may, consistent with their exempt purpose, publicly advocate positions on public policy issues.” Rev. Rul. 2004-6. So too, such groups “may engage in an exempt function within the meaning of § 527(e)(2) [and] may do so with [their] own funds or by setting up a separate segregated fund under § 527(f)(3).” But “if the organization chooses to use its own funds, ... [it] is subject to tax under section 527(f)(1) on the lesser of its investment income or the amount of the exempt function expenditure.” *Id.* Thus, the question of whether spending by a section 501(c) group constitutes “exempt function” activity or lobbying determines whether the requirements of section 527, including the tax imposed under section 527(f)(1), apply to the spending.

electioneering, and five competing factors that “tend to show” that an advertisement qualifies as lobbying. Rev. Rul. 2004-6 at 3-4.

Applying this “facts and circumstances” test in Rev. Rul. 2004-6, the IRS concluded that three of the advertisements qualify as lobbying activity. *See* Rev. Rul. 2004-6, Situations 1, 2 and 5. The ruling, for instance, treats as lobbying, not electioneering, an advertisement that “identifies Senator C, appears shortly before an election in which Senator C is a candidate, ... targets voters in that election ... [and] identifies Senator C’s position on the issue as contrary to” the sponsor of the ad. *Id.* (Situation 2). Although this sounds like the classic sham issue ad — even down to the “Call or write Senator C to tell him to vote for S. 24” tag line that was a hallmark of the abusive pre-BCRA regime — the IRS concluded that it would treat this ad as lobbying because, under the facts of the hypothetical, it is timed to appear before a Senate vote on the issue discussed. As such, this ruling indicates that the IRS would allow a section 501(c)(3) group to sponsor such an ad as part of a *lobbying* campaign, and *not* treat such an ad as subject to the absolute prohibition on campaign intervention that tax law applies to section 501(c)(3) organizations.

BCRA’s “electioneering communication” provisions were intended to encompass precisely these kinds of ads. As a matter of *election* law, the Supreme Court concluded that “the issue ads broadcast during the 30- and 60-day periods preceding federal primary and general elections are the functional equivalent of express advocacy.” *McConnell*, 540 U.S. at 206. Whether the IRS chooses to apply a different, and more fact-dependent, test for purposes of *tax* law is of no moment to how the Commission is required to implement the campaign finance regulatory regime that it bears sole responsibility for enforcing.

Rev. Rul. 2004-6 was issued shortly after the Commission promulgated the *per se* exemption for 501(c)(3) groups in its 2002 Title II rulemaking. At the time, tax law experts noted the potential for abuse that was created by the combination of the IRS’s interpretation of tax law, and the FEC’s *per se* exemption. Indeed, in a news article about this revenue ruling, several tax law experts expressed concerns that the IRS interpretations, in light of the Commission’s “electioneering communication” regulation exempting charities, “may have inadvertently handed campaign strategists an enormous loophole.” Damon Chappie, *New IRS Guidance May Open Loophole*, ROLL CALL, Jan. 26, 2004, at 2. One expert said the new IRS interpretation, combined with the Commission’s “electioneering communication” regulation, opened up “a very real and likely loophole.” *Id.*

Attorneys Gregory L. Colvin and Rosemary E. Fei, noted tax law experts, wrote to the IRS shortly after the ruling was issued, to warn that section 501(c)(3) charities could become “the ideal vehicle for interventionist advertising.” Their letter begins:

Any time we get guidance from the IRS on political activities of exempt organizations, it is welcome and useful. This certainly includes Revenue Ruling 2004-6, announced on December 23, 2003. We have to worry, though, in situations where the IRS appears to give a green light to a type of activity that could be exploited to intervene in candidate election campaigns. After the passage and recent validation of the McCain-Feingold campaign finance reform

legislation (the Bipartisan Campaign Reform Act of 2002 or BCRA), tens of millions of dollars can be expected to pour into any promising loophole in the scheme of regulation.

Specifically, we are concerned that the IRS may have inadvertently handed campaign strategists an enormous loophole in the form of Situation 2 of the new Revenue Ruling. We believe there is a very real possibility that, unless the IRS clarifies this example promptly, *massive amounts of soft money will be used to pay for TV and radio ads in battleground states that meet the criteria of Situation 2. The contributions for these ads would not only be unlimited, but they would be anonymous and could even be tax deductible.*²⁰

Colvin and Fei describe the potential abuse as arising from the IRS interpretation in light of the Commission's *per se* exemption from Title II for section 501(c)(3) groups:²¹

[T]he potential for abuse of the new Revenue Ruling has been greatly heightened by recent events outside of tax law. Here's why:

The McCain-Feingold legislation contains a ban on corporate and labor payments for TV and radio ads that mention the name of a candidate within 60 days before a general election and within 30 days before a primary or caucus....The ban applies to Section 501(c)(6), (c)(5) and most (c)(4) nonprofit corporations, but a Federal Election Commission regulation allows 501(c)(3) charities to run such ads, relying upon the IRS to ensure that charitable broadcast advertising will be nonpolitical.

A 501(c)(3) charity might become the ideal vehicle for interventionist advertising, based upon Situation 2 in the new Revenue Ruling. All a charity need to do is find a bill (related to its exempt purposes) that is coming up for a vote in Congress

²⁰ Letter of December 30, 2003 from Gregory L. Colvin and Rosemary E. Fei to Judith E. Kindell, Esq, *republished in* 2004 Tax Analysts, TAX NOTES TODAY (Jan. 2, 2004), 2004 TNT 1-25 (emphasis added). For the Commission's convenience, a copy of the letter is attached as Exhibit A.

²¹ Colvin and Fei explain their view that the reasoning of Rev. Rul. 2004-6 will apply to section 501(c)(3) groups even though the ruling by its terms it discusses only section 501(c)(4), (c)(5) and (c)(6) groups:

While the Revenue Ruling does not explicitly address Section 501(c)(3) charitable organizations, the Service has said on many occasions that the line between political and nonpolitical activities for (c)(3) charities is the same as for (c)(4) social welfare groups and for Section 527 political organizations...*Therefore, especially in light of the lack of current 501(c)(3) precedential guidance on prohibited candidate electioneering, an IRS revenue ruling on political activities for non-(c)(3)'s will be read by practitioners as equally applicable to 501(c)(3) organizations.* To depart from the identity of the (c)(3) and (c)(4) standards would be to create much confusion and disarray.

Letter at 1, n.1 (emphasis added).

before the election, where the candidates have not been publicly known to be divided on the issue, and where the incumbent is believed to be vulnerable. The charity can drop in to a specific state or district, run TV, radio, or newspaper ads attacking the incumbent's positions and calling on the audience to contact him or her to "vote right" on the bill. The charity can use tax-deductible funds for the ads, without disclosure of donors whose funds paid for the ads, treating the ads as grass roots communications within its lobbying limits.

Id. at 2 (emphasis added).

Colvin and Fei close by noting the danger that this loophole could be exploited in the future:

Our law firm has a substantial practice in this area. We have always advised our Section 501(c)(3), (c)(4), and 527 clients that targeting ads that criticize or praise public officials solely to areas where they face close elections is political and not charitable. We would not have advised (c)(3) or (c)(4) clients that they could target ads as in Situation 2 as a nonpolitical activity, prior to the announcement of Revenue Ruling 2004-6. Perhaps we have been too cautious in our advice. *If the IRS does not clarify this ruling soon, and especially if our clients' adversaries engage in targeted advertising described in Situation 2, we will feel obliged to advise them that the IRS appears to condone such advertising.*

Id. at 3 (emphasis added).

To our knowledge, the IRS has not clarified or modified the advice given in Rev.Rul. 2004-6, and the dangers outlined in the Colvin-Fei letter – including the potential for abuse created by the Commission's *per se* exemption from Title II – remain in place.

Thus, the premise of the Commission's *per se* exemption – that section 501(c)(3) groups cannot by law engage in the types of ads within the concern of Title II – is flawed. As one tax law expert explained: “[c]haritable organizations that are exempt from tax under section 501(c)(3) are prohibited from intervention in a political campaign. Yet the record is equally clear that the muddled definition of educational advocacy on social issues versus campaign advocacy for or against specific candidates has permitted extensive political campaign activity by exempt charities.” Daniel L. Simmons, *An Essay on Federal Income Taxation and Campaign Finance Reform*, 54 Fla. L. Rev. 1, 107-08 (Jan. 2002). Indeed, rather than the FEC deferring to the IRS in determining what is campaign intervention, this author specifically argues that the contrary approach is more appropriate – and that the *inclusion* of charities within the Commission's Title II regulations will help resolve the problem: “Broadening and clarifying the definition of political intervention to include all campaign advocacy, *particularly advocacy that meets the definition of an electioneering communication under the McCain-Feingold standard*, will help identify charitable organizations that attempt to influence the outcome of elections.” *Id.* at 108 (emphasis added).

As another academic noted prior to the passage of BCRA, “[d]ue to loopholes in the IRC and FECA, charities and social welfare groups are able to engage in partisan activities, yet argue

that their actions are nonpolitical.” Robert Paul Meier, *The Darker Side of Nonprofits: When Charities and Social Welfare Groups Become Political Slush Funds*, 147 U. Pa. L. Rev. 971, 985-86 (Apr. 1999) (discussing one section 501(c)(3) group, “Vote Now ’96,” which “virtually operated as a Democratic Party subsidiary”). The Commission’s *per se* exemption for section 501(c)(3) organizations allows such activity to continue unabated, thereby frustrating the goals of Title II.

Finally, In NPRM 2005-20, the Commission cites the “SNAP: Strengthening Nonprofit Advocacy Project” research survey, as well as data from the National Center for Charitable Statistics, and asks how the Commission should interpret the reports. 70 Fed. Reg. at 49512. If the Commission believes that the application of BCRA’s “electioneering communication” provisions will inhibit the work of Section 501(c)(3) groups, the response is the same as the *McConnell* Court made to all other entities subject to the Title II provisions: such groups “may finance genuine issue ads during those time frames by simply avoiding any specific reference to federal candidates,” 540 U.S. at 206, or by choosing non-broadcast media.

C. Reliance on IRS Enforcement

As noted in NPRM 2005-20, the district court in *Shays* held that the effect of the blanket 501(c)(3) exemption in current 11 CFR § 100.29(c)(6) is that “the FEC would do nothing until the IRS investigated and decided whether or not the organization violated the tax laws.” *Shays*, 337 F. Supp. 2d at 128. The district court invalidated the *per se* section 501(c)(3) exemption in part on the ground that the “Commission failed to consider the effectiveness of, and the problems presented by, adopting an enforcement policy that relies on the IRS’s enforcement of the tax code.” 70 Fed. Reg. at 49512.

In the NPRM, the Commission now incorrectly frames the operative legal issue, stating:

In addressing the extent to which the Commission could or should rely on IRS enforcement of the tax code as a safeguard for ensuring that section 501(c)(3) organizations *do not make communications that would support or oppose a Federal candidate*, the Commission is considering statements and testimony from several sources, including section 501(c)(3) organizations and the Government Accountability Office (“GAO”).

70 Fed. Reg. at 49512 (emphasis added). This framing of the issue implies that the Title II provisions should apply only to organizations which make PASO communications, and only to the extent that they do make PASO communications. But if this is true for section 501(c)(3) groups, the same logic would apply to section 501(c)(4) groups as well. The net effect would be to collapse the bright-line statutory standard of Title II into a PASO test. For the reasons stated above, this is plainly contrary to the language of the statute, to congressional intent, and to constitutional principles.

The NPRM notes that several section 501(c)(3) organizations commented in the 2002 rulemaking that “the possibility of an IRS revocation of their 501(c)(3) status because of their

political activities was a strong deterrent to their engaging in activity that may be viewed as supporting or opposing candidates.” 70 Fed. Reg. at 49512.

The relevance of this statement depends on the incorrect premise that section 501(c)(3) groups cannot as a matter of tax law engage in communications that promote or oppose a candidate, in the sense contemplated by Congress in BCRA.²² While it is true that section 501(c)(3) of the tax code contains a broadly stated prohibition on “intervention” in a political campaign, this tax law prohibition is not co-extensive with BCRA’s prohibition on “electioneering communications.” Even if the tax law prohibits “intervention” in a campaign, an ad that favorably portrays a candidate (such as a public service announcement) or that criticizes a candidate (such as an ad with a lobbying message), might not be treated by the IRS as “intervention” in a political campaign, yet could promote or oppose the candidate in ways that undermine the purposes of BCRA. In other words, a section 501(c)(3) corporation could engage in “electioneering communication,” even one that is clearly within the scope of what Congress intended Title II to regulate, and in no way jeopardize its tax status.

Furthermore, the IRS enforces the non-intervention standard of Section 501(c)(3) through either revocation of tax exempt status or the imposition of penalties. Yet “in reality, neither of these sanctions is meaningful[.]”²³ As one commentator explains:

Revocation of the exempt status of a charitable organization that is intervening in political campaigns will not prevent abuse. The revocation process is long and difficult, revocation generally would be initiated after tax-free money has already been expended in the electoral process and after the charitable organization has attempted to accomplish its political purpose, and the promoters of the charitable organization are not restrained from the creation of a new organization to carry on the political activities.²⁴

Another tax law expert explains further:

²² As noted above, the Commission in another context has acknowledged that this premise is incorrect. Last year, the Commission published a Notice of Proposed Rulemaking regarding “Political Committee Status,” 69 Fed. Reg. 11736, which in part discussed the definition of the term “expenditure.” The NPRM raised the question whether all payments by Section 501(c)(3) groups should be exempt from the term “expenditure.” The Commission, however, noted: “In this regard, how should the Commission interpret the Internal Revenue Service’s Technical Advice Memorandum 89-36-002 (Sept. 8, 1989), which permitted a 501(c)(3) organization to make advertisements that ‘support or oppose a candidate in an election campaign,’ without losing its 501(c)(3) status for intervening in a political campaign?” 69 Fed. Reg. at 11742. Thus, the Commission itself has acknowledged that the IRS interprets tax law to allow a Section 501(c)(3) group to run ads that “support or oppose” candidates, an admission completely inconsistent with the premise of its *per se* exemption for section 501(c)(3) groups.

²³ Francis R. Hill, “Newt Gingrich and Oliver Twist: Charitable Contributions and Campaign Finance,” 66 TAX NOTES 237, 246 (Jan. 1995).

²⁴ Daniel L. Simmons, *An Essay on Federal Income Taxation and Campaign Finance Reform*, 54 Fla. L. Rev. 1, 108 (Jan. 2002).

A section 501(c)(3) organization that loses its exempt status is required to dissolve and to transfer its assets to another section 501(c)(3) organization. If a political charity loses its exempt status, which is a protracted administrative process, those involved in the imperiled organization can simply establish a new organization, generally with a slightly altered board of directors, and, when the former organization's exemption is revoked, transfer any remaining assets to its successor. In this process, the organization itself can determine which section 501(c)(3) organization will receive its assets.²⁵

Indeed, the IRS itself has explicitly recognized that revocation is an ineffective sanction. In a preamble to proposed regulations implementing new excise taxes for non-complying organizations, the IRS stated:

Congress enacted sections 4955, 6852 and 7409 because it determined that revocation of exemption was not a sufficient sanction to enforce effectively the prohibition on political intervention by section 501(c)(3) organizations. For example, if an organization engaged in significant, uncorrected political intervention, revocation could be ineffective as a penalty or deterrent, particularly if the organization used all its assets for political intervention and then ceased operations.

59 Fed. Reg. at 64359-60.

So too, the organizational penalty Congress created to supplement revocation may itself be “a mere formalism” that “is as meaningless as revocation of exemption.” Hill, *supra*, at 248. And this of course further assumes that even if meaningful sanctions were available to impose, the IRS has the resources to police its standard, and that it sets its priorities to do so. But “[p]olicing exempt organizations is something of a sideline for the IRS; ‘[t]he Service doesn’t like it because it doesn’t raise revenue.’”²⁶

Government statistics bear this out. Although there were more than 850,000 Section 501(c)(3) groups operating in 2001, a total of only 96 organizations had their charitable status revoked in the six-year period from 1996-2001, and of these, only 16 were penalized for conducting non-exempt activities. See GAO, *Political Organizations: Data Disclosure and IRS’s Oversight of Organizations Should Be Improved*, GAO-02-444 (July 2002) at 44 (Table 5) (Number of Section 501(c) Tax-Exempt Organizations, Fiscal Years 1995-2001), and 48 (Table 9) (Revocations of Section 501(c)(3)-(6) Tax-Exempt Status, Fiscal Years 1995-2001); see also GAO, *Tax-Exempt Organizations: Improvements Possible in Public, IRS and State Oversight of Charities*, GAO-02-526 (Apr. 2002) at 68 (Table 21) (Primary Reasons for Revocations by Fiscal Year, 1996-2001).

²⁵ Hill, 66 TAX NOTES 237, 246, *supra*.

²⁶ Laura Brown Chisolm, *Sinking the Think Tanks Upstream: The Use and Misuse of Tax Exemption Law to Address the Use and Misuse of Tax-exempt Organizations by Politicians*, 51 U. Pitt. L. Rev. 577, 593 (Spring 1990) (quoting former IRS Commissioner Sheldon Cohen).

The GAO notes that the “IRS has not kept up with growth in the charitable sector. IRS staffing for overseeing tax-exempt organizations fell between 1996 and 2001 while at the same time the number of new applications for tax exemption and the number of Forms 990 filed increased.” GAO-02-526 at 20. Thus, “the resources devoted to oversight dropped for fiscal years 1996 through 2001.” *Id.* at 22.

Under the current, invalidated “electioneering communication” regulation, the Commission erred in functionally delegating the enforcement of BCRA’s “electioneering communication” provisions to the IRS, without regard for IRS interpretations, enforcement resources, or priorities. By simply assuming that IRS application of section 501(c)(3) standards would be sufficient to ensure that such corporations did not engage in sham “issue” advocacy, the Commission abdicated its own independent responsibility to enforce BCRA.

The Commission’s General Counsel specifically advised against creating the *per se* section 501(c)(3) exemption precisely because “the civil enforcement of BCRA lies within the jurisdiction and responsibility of this Commission and *cannot be left to another agency’s policing of those subject to another statute.*” Agenda Doc. No. 02-68, “Final Rule, Interim Final Rule, and Explanation and Justification for Electioneering Communications,” Sept. 24, 2002, at 49 (emphasis added).

This franchising out of the Commission’s enforcement authority for the campaign finance laws is no more appropriate in the BCRA context than it would be for the Commission to adopt a regulation exempting charities from the longstanding FECA prohibition on “express advocacy” by all corporations (including charities), 2 U.S.C. § 441b(a), on the theory that charities are separately prohibited by tax law from engaging in express advocacy. Notwithstanding the arguable overlap between the tax law and election law, the Commission has never, by regulation, repealed the election law applicable to charities under FECA. Nor should it do so under BCRA.

VI. Communications Publicly Distributed Without a Fee—11 C.F.R. § 100.29(b)(3)(i).

As the Commission noted in NPRM 2005-20, both the district court and the court of appeals in *Shays* “determined that the ‘for a fee’ language in the definition of ‘publicly distributed’ operated much like an exemption to the definition of ‘electioneering communication.’” 70 Fed. Reg. at 49509. The district court found that the “for a fee” exemption exceeded the Commission’s clause (iv) authority to create exemptions, *see* 2 U.S.C. § 434(f)(3)(B)(iv), because the exemption could include communications that PASO a federal candidate. *Shays*, 337 F. Supp. 2d at 128–29. The D.C. Circuit agreed, finding that “[e]xempting all fee-free communications regardless of content...makes no pretense” of following the statutory restrictions on the Commission’s exemption authority. 414 F.3d at 109. The Commission further acknowledged in the NPRM that both the district court and the court of appeals held that the “for a fee” provision “is inconsistent with the plain text of BCRA and thus violated *Chevron* step one.” 70 Fed. Reg. at 49509 (citing *Shays*, 337 F. Supp. 2d at 129; 414 F.3d at 109).

In order to comply with district court's order in *Shays*, affirmed by the court of appeals, the Commission proposes to eliminate the phrase "for a fee" from the definition of "publicly distributed" at 11 CFR 100.29(b)(3)(i). 70 Fed. Reg. at 49509. The Commission seeks comment on whether removing the phrase "for a fee" from the definition of "electioneering communication" definition "would require extensive monitoring of radio and television programming to ensure that it either fits the statutory press exemption or otherwise avoids the reach of the 'electioneering communication' rules." *Id.* The Commission further inquires whether removing the phrase "for a fee" from the regulation would require the Commission to distinguish "commentary" from free time donated to political committees or candidates, which was approved in Advisory Opinions 1982-44 and 1998-17. *Id.*

We fully support the Commission's proposal to remove the "for a fee" language from the definition of "publicly distributed" and, by doing so, eliminate the blanket exemption in the current regulation for all unpaid advertising. Regarding the need for the Commission to "monitor" broadcast programming, the purported problem raised by the Commission is no different in form than the enforcement of longstanding law – to the extent it does so at all, the Commission has long been required to "monitor" broadcast programming to ensure that the programming either fits the statutory press exemption or otherwise avoids the reach of FECA's definition of "expenditure" at 2 U.S.C. § 431(9). The proposed elimination of the "for a fee" language simply requires the Commission to be cognizant of both the "expenditure" restrictions and "electioneering communication" restrictions applicable to corporations under FECA.

In Ad. Op. 1982-44, the Democratic National Committee ("DNC") and the Republican National Committee ("RNC") jointly sought the Commission's advice on the applicability of FECA to the acceptance by both the DNC and RNC of free air time offered by an incorporated television network. The Commission opined that the programs to be produced by the DNC and RNC qualified as "commentary" and, thus, fell within the "news story, commentary, or editorial" exemption of 2 U.S.C. § 431(9)(B)(i). The Commission explained its belief that the term "commentary" was intended to allow third persons access to the media to discuss issues. The Commission advised that the proposed corporate donation of air time to both political parties "is within the broadcaster's legitimate broadcast function and, therefore, within the purview of the media exemption" to the statutory definition of "expenditure."

Similarly, in Ad. Op. 1998-17, the operator of two cable television systems sought the Commission's advice on the applicability of FECA's corporate contribution prohibition to his corporations' provision of free television air time to all *bona fide* candidates for specified federal offices. The Commission cited Ad. Op. 1982-44 for the proposition that the "commentary" provision of the media exemption "allow[s] third persons access to the broadcast media to discuss issues from a highly political and partisan perspective." The Commission further noted that the broadcaster would be "performing a function that is contemplated as a public service function" under federal Communication Act provisions encouraging broadcasters to "to provide reasonable access to candidates on an equal opportunity basis to more fully inform voters." Importantly, the Commission advised:

Absent these [communications] laws and regulations ensuring that Daniels will provide equal opportunities to all qualified candidates, the Commission might

disapprove a similar request. The Commission cautions, however, that *activities by [the requestor] which reflect an intent to advance one candidate over another, or to give any preference to any candidate, will be deemed to fall outside the Act's media exception.* These equal access assurances take the Daniels proposal outside the realm of mere in-kind contributions of advertising space. Given these features, the Daniels proposal constitutes the performance of a media function encouraged and required under the Communications Act, and, in its similarity to the activity in Advisory Opinion 1982-44, it is considered to be commentary.

Ad. Op. 1998-17 (emphasis added).

We believe that these advisory opinions were properly decided, and that the analysis employed by the Commission in these opinions should be employed again in the context of similar requests involving the media exemption from the definition of both “expenditure” at 2 U.S.C. § 431(9)(B)(i), and “electioneering communication” at 2 U.S.C. § 434(f)(3)(B)(i). Specifically, the Commission’s requirement that all candidates and parties receive equal access when a broadcaster donates free air time is vital to the fair implementation of the “commentary” provision of the media exemption. We do not believe that removal of the phrase “for a fee” from the “electioneering communication” rule would require the Commission to alter its application of the “commentary” provisions contained in the media exemption.

Although not reflected in the proposed rule, the Commission is considering an alternative approach that would both delete the “for a fee” language and create a new exemption “for communications for which the broadcast, cable or satellite entity does not seek or obtain compensation for publicly distributing the communications, unless the communications promote, support, attack or oppose a Federal candidate.” 70 Fed. Reg. at 49509. The Commission attempts to justify this alternative proposal on the ground that:

broadcasters donate airtime to organizations to broadcast communications in the public interest, such as public service announcements promoting a wide range of worthy endeavors. Subjecting these communications to the electioneering communication regulations may discourage broadcasters from performing an important public service in providing free airtime for these ads. An exemption that is limited to non-PASO communications may, in practice, exempt comparatively few communications from the definition of “electioneering communications.”

Id.

We oppose this alternative approach, which functionally creates an exemption for unpaid non-PASO communications. The problem is again the one discussed above – this approach seeks to replace the Title II “bright-line” test with a PASO standard that is not appropriate for application to individuals and entities other than “major purpose” entities such as political committees.

Furthermore, the D.C. Circuit explicitly rejected the Commission’s stated rationale for this approach by noting that PSA ads might very well fall within the core concerns of Congress in enacting Title II:

[E]xcluding federal candidates from broadcasts promoting blood drives and other worthy causes for 90 days out of every two years (30 days before the primary plus 60 days before the general election) would hardly seem unreasonable given that such broadcasts could “associate a Federal candidate with a public-spirited endeavor in an effort to promote or support that candidate” — a risk the FEC itself acknowledged, in the very same rulemaking, in justifying its refusal to promulgate a general exemption for PSAs (whether paid or unpaid), *see* 67 Fed. Reg. at 65,202.

Shays, 414 F.3d at 109.

Organizations wishing to utilize donations of airtime to broadcast PSAs and other communications in the public interest during the 90 days out of the year covered by the “electioneering communication” restrictions can and should find spokespersons other than federal candidates to deliver their message.

Finally, any concern that the “electioneering communication” regulations will potentially sweep in incidental references to candidates on entertainment programs or in pre-election documentaries is adequately addressed by the statutory exclusion for news stories, commentary, or editorials. 2 U.S.C. § 434(f)(3)(B)(i); *see also* 11 C.F.R. § 100.29(c)(2). As for documentaries, the Commission has long interpreted the identical exclusion from the definition of “expenditure,” 2 U.S.C. § 431(9)(B)(1), to cover documentary programs, biographies, and similar broadcasts in order to broadly “preserve the traditional role of the press with respect to campaigns.”²⁷ And as for entertainment shows, the Commission has recently applied this exemption, as well as the identical exemption in Title II, to protect a television broadcaster’s fictional entertainment series about presidential elections. *See* Ad. Op. 2003-34. The Commission held that, as fiction, the series was not subject to the campaign finance laws, but also held that incidental references to real life candidates would be exempt “commentary” and thus constitute neither express advocacy nor “electioneering communications.” *Id.* The same reasoning would protect similar references to candidates in other entertainment shows as well.

VII. Eliminating All Regulatory Exemptions From the Electioneering Communications Restrictions

The Commission asks, as an alternative to the proposed modifications of 11 C.F.R. § 100.29(c)(6) described above, whether it should repeal both of the regulatory exemptions from the electioneering communications rules, 11 CFR 100.29(c)(5) and (6), and instead rely solely on

²⁷ FEC Ad. Op. 1996-48. The Commission has noted that the legislative history demonstrates that the press exemption “assures the unfettered right of the newspapers, TV networks and other media to cover and comment on political campaigns.” *Id.* (*quoting* H.R. Rep. No. 93-1239, 93rd Cong., 2d Sess. at 4 (1974)).

the exemptions that Congress established in BCRA. 70 Fed. Reg. at 49513. This proposed repeal includes both the section 501(c)(3) exemption, and the exemption for communications paid for by candidates for state or local office, in connection with a state or local election, that do not PASO any federal candidates.

As discussed above, we strongly support this proposal to repeal, in its entirety, the 11 C.F.R. § 100.29(c)(6) exemption for section 501(c)(3) organizations. Doing so would bring 11 C.F.R. § 100.29(c) into line with 2 U.S.C. § 434(f)(3)(B), and more faithfully implement the intent and purpose of this statutory section.

Although the repeal of 11 C.F.R. § 100.29(c)(5) — the exemption for communications by candidates for state or local office that do not PASO any federal candidate — would result in a regulation that permissibly interprets 2 U.S.C. § 434(f)(3)(B), we believe that repeal of this exemption is not necessary. The section 100.29(c)(5) exemption is a proper exercise of the Commission’s clause (iv) authority. Section 100.29(c)(5) properly incorporates the non-PASO restriction required by clause (iv), and applies the PASO standard to political committees — an approach which does not present the constitutional concerns raised by the application of the PASO standard to entities other than “major purpose” entities.²⁸

VIII. Exempting All Communications That Do Not PASO a Federal Candidate

The Commission also seeks comment on a proposed exemption from the definition of “electioneering communication” for “all communications that do not PASO a Federal candidate.” 70 Fed. Reg. at 49513.

We strongly oppose this proposed exemption, for the reasons stated above. This exemption would effectively replace the bright-line “electioneering communication” standard — the cornerstone of Title II — with a PASO standard which may not be constitutional as applied to entities other than “major purpose” entities such as political committees. As explained above, Congress recognized in Title II that application of the PASO standard to entities other than “major purpose” groups might raise concerns of constitutional vagueness, similar to the vagueness concerns that led the Supreme Court in *Buckley* to impose a bright-line “express advocacy” construction on the statutory phrase “for the purpose of influencing,” when the term “expenditure” is applied to entities other than “major purpose” groups such as political committees. *Buckley*, 424 U.S. at 77-79.

The *Buckley* Court, however, saw no need to narrowly construe the definition of “expenditure” as applied to political committees, because “[e]xpenditures of candidates and of ‘political committees’ ... can be assumed to fall within the core area sought to be addressed by Congress. They are, by definition, campaign related.” *Id.* at 79.

Based on this discussion in *Buckley*, Congress applied the PASO standard in Title I of BCRA to the activities of state political party committees — entities with a self-proclaimed

²⁸ The Commission also seeks comment on proposed revisions to the 11 C.F.R. § 100.29(c)(5) exemption for state and local candidates. We do not object to these proposed revisions.

major purpose of influencing elections — as a means of defining and regulating state party “federal election activity.” *See* 2 U.S.C. § 431(20)(A)(iii).

By contrast, in order to avoid potentially unconstitutional ambiguity, Congress enacted BCRA’s bright-line “electioneering communication” standard in Title II for individuals and entities *other than* “major purpose” entities such as political committees. The Supreme Court in *McConnell* found that BCRA’s definition of “electioneering communication” raises none of the vagueness concerns” that drove its analysis in *Buckley*. *McConnell*, 540 U.S. at 194. According to the Court, the definition of “electioneering communication” is “both easily understood and objectively determinable.” The Court concluded that “the constitutional objection that persuaded the Court in *Buckley* to limit FECA’s reach to express advocacy is simply inapposite here.” *Id.*

The Commission should not replace the clearly constitutional “electioneering communication” standard in Title II with a PASO standard, which is potentially unconstitutional as applied to entities other than political committees and other “major purpose” groups. Doing so would clearly undermine congressional intent to enact a bright-line, constitutional test for distinguishing between regulated electioneering speech and other speech not subject to regulation under federal campaign finance laws.

IX. Petition for Rulemaking To Exempt Advertisements Promoting Films, Books, and Plays

Finally, in response to a petition for rulemaking received by the Commission on August 26, 2004 — on a matter unrelated to the *Shays* litigation — the Commission is proposing a new regulatory exemption to the definition of “electioneering communication.” Proposed 11 CFR 100.29(c)(7) would exempt from the definition of “electioneering communication” any communication that “[p]romotes a movie, book, or play, provided that the communication is within the ordinary course of business of the person that pays for such communication, and such communication does not promote, support, attack or oppose any Federal candidate.” 70 Fed. Reg. at 49515.

Although we do not oppose an exemption along the lines proposed, we believe it should be re-framed to avoid a PASO test, for the reasons set forth above. Instead, the Commission should adopt the approach it recently followed in MURs 5474 and 5539, where it analyzed ads promoting the movie *Fahrenheit 911*. There, the Commission found the ads were not “electioneering communications” because there was no evidence they were broadcast within the applicable Title II windows.²⁹ The Commission, however, additionally analyzed whether the film or promotional materials constituted impermissible corporate “expenditures.”

In concluding they did not, the Commission applied a test developed in prior advisory opinions, *see* Ad. Op. 1994-30 (Conservative Concepts) and Ad. Op. 1989-21 (Create-a-Craft): whether the promotional materials constituted “bona fide commercial activity.” *Id.* at 13. Importantly, as the General Counsel Report notes, “An analysis of whether the feature-length film, movie trailers and Fahrenheit911.com are bona fide commercial activity does not turn on

²⁹ *See* First General Counsel’s Report in MURs 5474 and 5539 (May 25, 2005) at 9-11.

their content.” *Id.* at 14. In a fundamental way, this distinguishes a “bona fide commercial activity” standard from a PASO test, which *is* a content determination.

As the Report notes about prior applications of this test to the sale of merchandise:

[W]hether commercial activity results in an expenditure or contribution is very fact-specific and depends on an examination of a number of factors, including (1) whether the sales of the merchandise involve fundraising activity or solicitations for political contributions; (2) whether the activity is engaged in by the vendor for genuinely commercial purposes and not for the purpose of influencing an election; (3) whether the items are sold at the vendor’s usual and normal charge; and (4) whether the purchases are made by individuals for their personal use. *See* AO 1994-30 and 1989-21.

Id. at 14.

The Report then applied a “totality of circumstances” test to determine if the promotional activities at issue in the MURs demonstrated that the spenders “were engaged in bona fide commercial activity,” *id.* at 15, and found that they were. For instance, the Report noted:

These respondents are in the business of making, promoting, and/or distributing films, and no information has been presented to suggest that they failed to follow usual and normal business practices and industry standards in connection with Fahrenheit 9/11. Further, the transactions between Miramax, Fellowship, Lions Gate and IFC appear to have been profit-making, arm’s length commercial transactions in which these entities bought and sold a product that they are typically in the business of buying and selling.

Id. at 16.³⁰

If the Commission decides to adopt a new exemption for promotional advertisements, it should codify the approach taken in MUR 5474 and the advisory opinions it is based on. Instead of applying a PASO test to such ads, it should apply a test that combines the “bona fide commercial activity” and “ordinary course of business” analyses. This test will *not* involve a content analysis of the ads, but rather the type of “totality of circumstances” evaluation described above as to whether a genuine commercial activity is involved. This approach, if adopted by the Commission, should both provide ample protection to genuine commercial activity, and avoid the application of a PASO test to a non-“major purpose” entity.³¹

³⁰ “As an alternative,” the General Counsel’s Report also analyzed whether the promotional materials contained “express advocacy,” and found that they did not. *Id.* at 17-19.

³¹ The Commission seeks comment as to whether the regulation’s reference to “movie” should be understood to mean only movies appearing in theatres, or whether it should also apply to movies available for rental on DVD or video, or available on pay-per-view. 70 Fed. Reg. at 49514. We believe that the term “movie” should be understood to include not only movies appearing in theaters, but also movies available for rental on DVD, video, or pay-per-view.

The Commission asks whether the exemption should be based on the actual or projected release date of the movie or book, and whether the exemption should apply only to movies that are shown during, or are being released within six months of, the electioneering communication window and to books that are in print during, or within six months of, the electioneering communications window. 70 Fed. Reg. at 49514. We believe such a six month time period provision would be consistent with and would advance the purposes of the rule’s “ordinary course of business” provision.

The Commission notes that the proposed exemption applies only to persons acting in the “ordinary course of business,” and asks whether this limitation would unfairly exclude first-time distributors. The Commission further asks whether it should extend the exemption to any person who promotes movies, books or plays without regard to whether such advertisements are in the ordinary course of business. 70 Fed. Reg. at 49514. We strongly object to the elimination of the “ordinary course of business” provision from the rule. We believe that the “bona fide commercial activity” test we propose (in combination with an “ordinary course of business” standard) could extend the exemption to first time distributors who provide evidence to the Commission that they are engaged in a *bona fide* commercial endeavor.

We support the Commission’s proposal to limit the exemption to entities not directly or indirectly established, financed, maintained, or controlled by any federal candidate, individual holding federal office, or any political committee, including political party committees.

X. Conclusion

For the reasons set forth above, we urge the Commission to adopt, with the recommended amendments and omissions set forth above, the proposed “electioneering communication” regulations, in order to comply with the district court decision in *Shays* and to preserve the integrity of BCRA’s ban on the use of corporate treasury funds to pay for “electioneering communication.”

We appreciate the opportunity to submit these comments.

Sincerely,

/s/ Fred Wertheimer

/s/ J. Gerald Hebert

/s/ Lawrence M. Noble

Fred Wertheimer
Democracy 21

J. Gerald Hebert
Paul S. Ryan
Campaign Legal Center

Lawrence M. Noble
Center for Responsive Politics

Similarly, the Commission seeks comment on whether the exemption should apply only to printed books, or also to books that are made available in audio and on-line formats. 70 Fed. Reg. at 49514. We believe the exemption should apply to books made available in print, audio and on-line formats.

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HEADLINE: 2004 TNT 1-25 ATTORNEYS RAISE CONCERNS ABOUT REVENUE RULING ON ADVOCACY ADS. (Section 527 -- Political Organizations) (Release Date: DECEMBER 30, 2003) (Doc 2004-64 (4 original pages))

CODE: Section 527 -- Political Organizations

ABSTRACT: Gregory L. Colvin and Rosemary E. Fei of Silk Adler & Colvin, in a letter to the IRS's Judy Kindell, say a new revenue ruling that seeks to explain when expenditures for issue advertising by exempt organizations are taxable could lead to abuses.

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Exempt organizations

Industry Group:

Nonprofit sector

Cross Reference:

For the full text of Rev. Rul. 2004-6; 2004-4 IRB 1, see Doc 2003-27045 (9 original pages) or 2003 TNT 247-2.

Principal Cited Reference:

section 527;

section 501(c)(4);

section 501(c)(5);

section 501(c)(6);

section 501(c)(3)

TEXT:

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December 30, 2003

Judith E. Kindell, Esq.
T:EO:RA:G

Internal Revenue Service
1111 Constitution Ave., NW
Washington, DC 20224

Re: Revenue Ruling 2004-6

Dear Judy:

[1] Any time we get guidance from the IRS on political activities of exempt organizations, it is welcome and useful. This certainly includes Revenue Ruling 2004-6, announced December 23, 2003. We have to worry, though, in situations where the IRS appears to give a green light to a type of activity that could be exploited to intervene in candidate election campaigns. After the passage and recent validation of the McCain-Feingold campaign finance reform legislation (the Bipartisan Campaign Reform Act of 2002 or BCRA), tens of millions of dollars can be expected to pour into any promising loophole in the scheme of regulation.

[2] Specifically, we are concerned that the IRS may have inadvertently handed campaign strategists an enormous loophole in the form of Situation 2 of the new Revenue Ruling. We believe there is a very real possibility that, unless the IRS clarifies this example promptly, massive amounts of soft money will be used to pay for TV and radio ads in battleground states that meet the criteria of Situation 2. The contributions for these ads would not only be unlimited, but they would be anonymous and could even be tax-deductible.

[3] Situation 2 describes an issue ad targeted at voters in a state where a contested Senate primary election campaign is occurring. The Section 501(c)(6) organization paying for the ad favors international trade, and claims that the incumbent Senator has taken positions opposing international trade. The ad asks the audience to contact the Senator and tell him to vote for a trade bill that will be voted on before the election. The ad also asks people to donate to the organization. The example, unlike others in the Revenue Ruling, does not indicate that the organization has advertised in this state on this issue before.

[4] The IRS states that the ad would NOT be classified as a political exempt function expenditure under Section 527. Therefore, the ad would not need to be run by a separate 527 segregated fund, would not be subject to the 35% tax under Section 527(f), would be treated as a proper primary activity for a Section 501(c) organization, and could even be an appropriate activity for a Section 501(c)(3) organization.^{1/}

[5] Our basic concern arises from the vague and ambiguous phrasing of negative factor (c): "The communication targets voters in a particular election." That factor is explicitly present in all six examples, even the ones treated as permissible nonpolitical communications. If by this phrase the IRS means to say "the communication is disseminated broadly to the public in an area where an election is occurring," the factor may be negative but is fairly benign, in our view.

[6] However, for political strategists, the concept of "targeting" has an entirely different meaning. It refers to the selection of certain states or congressional districts, and not others, for activities such as the placement of issue ads, based on where close elections are occurring. Such intentional selection of "battleground" or "swing" states for issue advertising, to us, indicates that a significant, if not dominant, purpose of the ad is to influence the election of candidates in the targeted area. That should be enough, in our view, despite the presence of a grass roots lobbying message, to cause the communication to fall under Section 527 (see PLR 9725036).

[7] We doubt that the Service intended this result, but it is there, and the potential for abuse of the new Revenue Ruling has been greatly heightened by recent events outside of tax law. Here's why:

[8] The McCain-Feingold legislation contains a ban on corporate and labor payments for TV and radio ads that mention the name of a candidate within 60 days before a general election and within 30 days before a primary or caucus. That law, just upheld by the U.S. Supreme Court, applies right now to broadcast ads in Iowa and New Hampshire, due to the upcoming caucus and primary in those states, and most other states will be involved as the year unfolds. The ban applies to Section 501(c)(6), (c)(5), and most (c)(4) nonprofit corporations, but a Federal Election Commission regulation allows 501(c)(3) charities to run such ads, relying upon the IRS to ensure that charitable broadcast advertising will be nonpolitical.

[9] A 501(c)(3) charity might become the ideal vehicle for interventionist advertising, based upon Situation 2 in the new Revenue Ruling. All a charity needs to do is find a bill (related to its exempt purposes) that is coming up for a vote in Congress before the election, where the candidates have not been publicly known to be divided on the issue, and

where the incumbent is believed to be vulnerable. The charity can drop in to a specific state or district, run TV, radio, or newspaper ads attacking the incumbent's positions and calling on the audience to contact him or her to "vote right" on the bill. The charity can use tax-deductible funds for the ads, without disclosure of donors whose funds paid for the ads, treating the ads as grass roots communications within its lobbying limits. Under Revenue Ruling 2004-6, the IRS apparently does not mind if the organization selects only those states or districts where incumbents are facing hotly contested elections, so long as it appears the organization is "lobbying" them on issues. Whatever the IRS intended, practitioners and political strategists will read it that way.

[10] Even if a tax-deductible charity is not used as a vehicle for these issue ads, a 501(c)(4) social welfare organization could be used to run such ads as its primary activity in an election year and keep its tax-exemption, financing the ads with unlimited contributions from undisclosed donors.

[11] To prevent this abuse, the IRS should immediately clarify that the references to targeting voters in a particular election found throughout the new Revenue Ruling, and particularly in Situation 2, do not permit an organization to treat as nonpolitical those mass media ads run only in states or districts selected based on electoral criteria.

[12] The IRS should require the exempt organization in Situation 2 to do more to demonstrate that these ads are nonpolitical. For instance, the IRS could state either that the organization has a history of running such ads outside of election campaign periods, OR that it has a substantial program of similar advertising directed at incumbents in other states or districts who are not up for re-election or are not in a close election contest.

[13] Our law firm has a substantial practice in this area. We have always advised our Section 501(c)(3), (c)(4), and 527 clients that targeting ads that criticize or praise public officials solely to areas where they face close elections is political and not charitable. We would not have advised (c)(3) or (c)(4) clients that they could target ads as in Situation 2 as a nonpolitical activity, prior to the announcement of Revenue Ruling 2004-6. Perhaps we have been too cautious in our advice. If the IRS does not clarify this ruling soon, and especially if our clients' adversaries engage in targeted advertising as described in Situation 2, we will feel obliged to advise them that the IRS appears to condone such advertising.

[14] The IRS announcement of Revenue Ruling 2004-6 requested "comments on situations or factors that the public believes should be covered in future guidance." The ruling should be modified in future guidance -- fast, like next month -- to tighten up Situation 2 and to clarify what is meant by "targets voters in particular elections." If this could be done before publication in the Internal Revenue Bulletin, that would be ideal.

[15] We wanted to get this letter into your hands right away, since this possible misuse of Revenue Ruling 2004-6 would be extremely serious. We do have other comments to make on the new ruling, and we expect to send you a second letter sometime in the next two weeks.

Very truly yours,

Gregory L. Colvin

Rosemary E. Fei

cc: Lois Lerner, Esq.
Steven Miller, Esq.

FOOTNOTE

/1/While the Revenue Ruling does not explicitly address Section 501(c)(3) charitable organizations, the Service has said on many occasions that the line between political and nonpolitical activities for (c)(3) charities is the same as for (c)(4) social welfare groups and for Section 527 political organizations (with certain exceptions not relevant here). Therefore, especially in light of the lack of current 501(c)(3) precedential guidance on prohibited candidate electioneering, an IRS revenue ruling on political activities for non-(c)(3)'s will be read by practitioners as equally applicable to 501(c)(3) organizations. To depart from the identity of the (c)(3) and (c)(4) standards would be to create much confusion and disarray.

END OF FOOTNOTE

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