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Testimony of James Sample
Hearing Hosted by the office of New York Attorney General Eric Schneiderman
on Proposed Disclosure Requirements for 501(c)(4) Organizations

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Good morning. My name is James Sample.[*] I am an Associate Professor at the Hofstra Law School. As someone who has litigated and written in the areas of campaign finance, judicial elections, and public financing, I am acutely aware of the impact of money on our democracy, and particularly, its profound impact on politics at the state level. I would like to thank Attorney General Schneiderman and his office for inviting me to participate today.

I applaud this proposal and believe that it will be both substantively significant and symbolically important in drawing attention to the fact that we need more comprehensive and, more importantly, more effective federal rules governing disclosure in campaign finance.

**Section 2**

This regulation, if adopted creates the kind of dynamic we would like to see more often in our political process — a race to the top — establishing NY state as a leader and champion of disclosure, transparency and democratic accountability. Attorney General Schneiderman's proposed regulations along with other recent efforts by elected officials in New York government are welcome steps towards free and fair elections.

Money in politics corrupts. Democratic government requires that the citizenry elect representatives who, in turn, set the ground rules within which businesses and other economic actors profit maximize. Neither government nor economy can long survive if law is for sale – or even if public opinion can be massively distorted by pots of money creating the appearance of debate or consensus where there is none.

Disclosure can help mitigate some of the ills of money in politics. As Justice Brandeis said, sunlight is the best distinfectant. It is harder to manipulate citizens who understand that the speaker may be motivated by selfish economic interests – not the public good or pursuit of the truth. Businesses may be less likely to intervene inappropriately if they are aware that their

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customers, clients, employees and investors will know that the business is taking positions with which they may disagree. And politicians are more likely to maintain independence even from large and powerful donors or advertisers if they must pander in public.

We have seen an explosion in outside spending since the *Citizens United* decision, Disclosure rules have long been an important and necessary part of the campaign finance system.[1] But the national disclosure system has collapsed, leaving voters in a system that falls woefully short of providing transparency in our elections.[2]

501(c)(4)s are currently being used as a way to avoid disclosure requirements and to ensure individual and business donors can contribute unlimited amounts of money without having to disclose their identities or the causes they are financing.[3] This is not hyperbole. As a joint study by the Center for Public Integrity and the Center for Responsive Politics notes, while Super-PACs were cast as the big bad wolves of the 2010 election cycle, they were outspent by a 3-2 margin by secretive nonprofits.[4] In 2012 Super-PACs were the more substantial players but that is misleading because many Super-PACs used donations from 501(c)(4) organizations to completely and quite consciously obscure the real source of funding.

The proposed rule would serve the important purpose of helping to end the abuse of 501(c)(4)s as a mechanism for avoiding disclosure requirements. Corporate donors use money that derives from their customers, employees and investors – none of whom have a direct say in determining how their funds are uses. Requiring disclosure thus protects ultimate human donors who want to know how their money is used – a critical first step towards making business fiduciaries answerable for their trust.

Just as importantly, disclosure protects the electorate by providing necessary information about who is funding political messages and what those group's true motivations are.[5] Three factors produce profoundly pernicious effects: unlimited independent expenditures, undisclosed sources of funding, and woefully inadequate rules and enforcement of existing rules on coordination,.

The most effective solution to the disclosure problem would be Congressional action requiring disclosure by 501(c)(4) groups. However, both Congress and the Federal Election Commission (FEC) have failed to act.[6] AG Schneiderman's proposed rule cannot address the lack of transparency in federal elections (meaning Presidential, Senatorial, and Congressional

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[1] Buckley v. Valeo, 424 U.S. 1, 64-68, 84 (1976) (upholding disclosure requirements against a First Amendment challenge).

[2] Citizens United v. FEC, 130 S.Ct. 876 (2010); O'Brien & Fuller, *supra* note 139 (explaining how the Citizens United decision led to $933 million in new outside spending during the 2012 election).

[3] *What Super PACs, Non-Profits, and Other Groups Spending Outside Money Must Disclose*, THE CENTER FOR RESPONSIVE POL., http://www.opensecrets.org/outsidespending/rules.php (last visited Feb. 25, 2013).

[4] Michael Beckel, *Nonprofits Outspent Super PACs in 2010, Trend May Continue*, June 18, 2012, *available* at http://www.publicintegrity.org/2012/06/18/9147/nonprofits-outspent-super-pacs-2010-trend-may-continue

[5] Buckley v. Valeo, 424 U.S. 1, 64-68, 84 (1976).

[6] *H.R. 5175 -DISCLOSE Act*, OPEN CONGRESS http://www.opencongress.org/bill/111-h5175/show (showing how no progress has been made on the DISCLOSE Act since 2010)

races in New York would be unaffected by the rule). But it can greatly improve disclosure at the state level.[7]

Still, the rule may play an important role that goes well beyond requiring disclosure in state elections. The proposed rule will raise the profile of disclosure within the broader campaign finance debate. New York will serve the important (and admirable) goal of moving the discussion about disclosure forward and will provide an example of the type of disclosure requirements needed on a broader scale. By taking a lead in requiring disclosure, New York will show that states can mitigate the harms of undisclosed money.

By bringing further attention to the need for disclosure, New York will encourage other states, and perhaps even Congress, to act on disclosure requirements. While disclosure requirements in New York may not have a national effect, combined action by other states, hopefully spurred on by New York's lead, can have an appreciable and important effect on disclosure in the election process. The proposed rule is not a panacea for disclosure problems, but its true import extends well beyond just achieving disclosure in New York elections.

**Section 3**

The 2012 elections involved extraordinary expenditures by 501(c)(4)s – especially at the state level. As Attorney General Schneiderman has noted, large, undisclosed funding of campaign expenditures at the state level is actually of greater concern than at the federal level.[8] In the Presidential election, expenditures are so large and media coverage is so broard that it is difficult for any particular funder to skew the debate. State contests have smaller advertising pools and fewer reporters to catch distortions or bring them to public attention. The smaller the pond, the greater the potentially skewing impact of the expenditure.

Secret money is especially distorting and dangerous when the public is the last to know where the money is coming from. Let's not kid ourselves here: the big spenders know how to make their expenditures known to those who they want to know of them. It is worth emphasizing that this dynamic that applies not only to expenditures but merely even to the significant threat of such expenditures.

As Lawrence Noble, an attorney at Skadden Arps and former general counsel of the FEC recently told the *New York Times*, one reality of the current campaign finance landscape is that when it comes to lobbying on behalf of special interests, the known *capacity* to spend huge sums is a hugely potent threat regardless of whether the expenditures actually occur. In Noble's words, lobbyists can now say "'We have got a million we can spend advertising for you or against you — whichever one you want.'"[9] Such threats are all the more pernicious when the sources of funding are known to the players involved, but not the public at large.

2004 was the year of the 527 organization.[10] Named for the section of the IRS code under which they are organized, 527s frequently make independent expenditures to support or oppose

[7] 2 U.S.C. §453 (2012); 11 C.F.R. § 108.7(b) (2012).

[8] E.g. Thomas Kaplan, *Attack Ads, by Outside Groups with Murky Ties, Shape 3 New York Senate Races*, N.Y. Times, Oct. 16, 2012, http://www.nytimes.com/2012/10/17/nyregion/3-new-york-senate-races-flooded-by-money-from-outside-groups.html?_r=1&.

[9] David Kirkpatrick *Lobbyists Get Potent New Weapon in Ruling* , N.Y. Times, January 21, 2010, http://www.nytimes.com/2010/01/22/us/politics/22donate.html

[10] Richard Briffault, The 527 Problem…and the Buckley Problem, 73 GEO. WASH. L. REV., 949 (2005).

political candidates.[11] Estimates of spending by 527s in the 2004 federal election "amounted to at least $405 million."[12] 2004 also gave rise to the best-known 527 organization ever: the Swift Boat Veterans for Truth[13], whose campaign against John Kerry generated what pollsters described as a "staggering" awareness among nearly three out of four voters.[14]

Over the next election cycles, and particularly following *Citizens United*, we encountered the rise of Super-PACs. These groups, together with the 501(c)(4)s and 527s, have spent unprecedented amounts of money in federal elections. During the 2012 election cycle, these groups spent over $1.4 billion — a 400% increase from the outside spending during the 2010 and 2008 elections.[15] Of this $1.4 billion, $314 million was undisclosed.[16] That is $314 million that cannot be legally traced back to the donor. That is $314 million that could potentially be a source of corruption or illegal influence.

Amazingly, however, the 501(c)(4) entities potentially subject to the Attorney General's regulations, make the preceding organizations – including Super PACs – look, comparatively, like models of democratic transparency and accountability. When, from a transparency perspective, an organization makes a Super-PAC look good, that is, to borrow from academia, grading on an exceedingly generous curve.

501(c)(4)s were designed to split the gap between 501(c)(3) organizations, that cannot take part in politics, and 527 groups, which have politics as their main focus. 501(c)(4)s are supposed to operate "exclusively for the promotion of social welfare."[17] However, they are permitted to occasionally get involved in politics, so long as it is not their primary purpose.[18] As noted by witnesses at earlier hearings on this topic, "the IRS's record on enforcement of these rules has been spotty, and unscrupulous groups have exploited this lax enforcement, claiming (c)(4) status while spending substantial sums on politics and promoting no apparent 'social welfare' goals at all."[19] Because they are supposedly not primarily involved in politics, 501(c)(4) organizations are not subject to the disclosure requirements that apply to other organizations in the campaign finance system. Between violations of an underenforced law, and organizations that are large enough so that even "occasional" political involvement turns out to be significant, these groups have become very important in the political process.

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[11] James Sample, *Democracy at The Corner of First and Fourteenth: Judicial Campaign Spending and Equality*, 66 NYU ANNUAL SURVEY OF AMERICAN LAW 727, 741 (2010), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1662630.

[12] Stephen R. Weissman & Ruth Hassan, BCRA and the 527 Groups, in The Election After Reform: Money, Politics, and the Bipartisan Campaign Reform Act 79 (Michael Malbin ed., 2006).

[13] *See* John J. Miller, *What the Swifties Wrought*, NAT'L REV., Nov. 29, 2004, at 18.

[14] Public Release of National Survey Results, Fabrizio, McLaughlin & Associates, 527's Matter and Swift Boat Vets Top the Heap – Best Known, Most Impact and Highest Ad Recall (Nov. 4, 2004), *available at* http://www.fabmac.com/FMA-2004-11-04-527-Effects.pdf.

[15] *Total Outside Spending by Election Cycle, Excluding Party Committees*, CENTER FOR RESPONSIVE POLITICS, http://www.opensecrets.org/outsidespending/cycle_tots.php, (last visited Jan. 25, 2013).

[16] *2012 Outside Spending, By Group*, Opensecrets.org, http://www.opensecrets.org/outsidespending/summ.php?cycle=2012&chrt=D&disp=O&type=A (last visited Feb. 23, 2013).

[17] Testimony of David Early (citing 26 U.S.C. § 501(c)(4)).

[18] *26 U.S.C. § 501(c)(4).*

[19] Testimony of David Early

The funding by these increasingly influential groups is dangerously opaque.[20] There is currently no mechanism in place to determine if 501(c)(4) organizations are taking advantage of their status and spending a majority (or in some cases almost all) of their money on politics rather than "social welfare."

**Section 4**

Today, any campaign regulation inevitably will be challenged in court. The Attorney General's proposal has nothing to fear from such challenges. Because it focuses on disclosure and creates narrowly tailored rules it is on solid legal ground. As discussed above, disclosure requirements are already an important part of both state and federal campaign finance systems.[21] Disclosure requirements have been routinely upheld as constitutional by the Supreme Court since *Buckley v. Valeo*.[22] Disclosure requirements are upheld because they serve the important purpose of preventing corruption and informing the electorate of who is funding political activity.[23] Disclosure requirements do not stop any person from making a contributing to a political organization nor do disclosure requirements impose a ceiling or limit on political contributions.[24] Even in *Citizens United,* which can hardly be described as a pro-regulatory decision by a pro-regulatory Court, *eight* Justices voted to uphold disclosure requirements on the ground that the government has an interest in providing information about who is donating to political speech to the voters.[25] Disclosure also serves the three additional important purposes (1) preventing corruption, (2) preventing the appearance of corruption, and (3) making information available to ensure that no other election laws are violated, an interest often referred to as the anti-circumvention interest.[26]

The proposed rule also provides a spending threshold and a waiver option, both of which also help insure the constitutionality of the rule. By exempting groups that spend less than $10,000 on politics in a year, the proposed regulation only targets groups that make spend more than incidental amounts to influence elections. This exemption combined with the ability of any group to apply for and receive a waiver from disclosure if it can show that "such disclosure will cause undue harm, threats, harassment or reprisals to any person or organization"[27] protects groups and donors that could face harassment if disclosure was required.[28]

While the time window of 180 days in the proposed regulation is more expansive than the disclosure window at the federal level (for entities that, unlike 501(c)4s, are subject to disclosure), this window reflects the modern realities of today's campaigns. As an example, taken from an investigation by the Center for Public Integrity, even as of June 2012, long before the November general election, the group Crossroads GPS spent more than $44 million on ads critical of others President Obama and congressional Democrats such as Senators Sherrod Brown of Ohio, Jon Tester of Montana, and Claire McCaskill of Missouri. Because the bulk of the ads

[20] *Id.*
[21] Buckley v. Valeo, 424 U.S. 1, 64-68, (1976) (upholding disclosure requirements).
[22] *Id.*
[23] *Id.*
[24] Citizens United v. FEC, 130 S. Ct. 876, 914 (2010)
[25] *Id.*
[26] Buckley v. Valeo, 424 U.S. 1, 64-68, 84 (1976).
[27] Text of Proposed Regulations *available at* http://www.ag.ny.gov/sites/default/files/press-releases/2012/Text_of_Proposed_Rule.pdf
[28] *See* NAACP v. Alabama ex. rel.Patterson, 357 U.S. 449 (1958).

did not air within 30 days of a primary or 60 days of a general election, Federal law did not require the group to report that spending. Accordingly, Crossroads GPS filed reports with the FEC indicating that it spent less than $200,000.[29]

Note that we are talking about two entirely different types of disclosure: First, Crossroads didn't have to disclosure of expenditures on electioneering that were outside the 30 and 60 day windows. Second, as a (c)(4) they would not be required to disclose the sources of the funding even for expenditures *within* the window.

The New York law is narrowly tailored to address the specific problem of lack of disclosure by 501(c)(4) groups and as designed would likely stand up against any challenge.

**Conclusion**

The Attorney General's proposed rule addresses an important issue in the campaign finance system and is a significant step, both substantively and symbolically, in the push towards a more open, transparent, and accountable democracy. Thank you for this opportunity and for your work on this important issue. I look forward to your questions.

[29] Michael Beckel, *Nonprofits Outspent Super PACs in 2010, Trend May Continue*, June 18, 2012, *available* at http://www.publicintegrity.org/2012/06/18/9147/nonprofits-outspent-super-pacs-2010-trend-may-continue