



Corporate Political Spending: What It Includes, How It Is Defined¹

Overview

The Bipartisan Campaign Reform Act (BCRA) of 2002 was enacted, in part, to staunch the flow of corporate money into the political process. It prohibited unlimited (or soft money) contributions to national political parties and to committees controlled by federal officeholders. However, BCRA did not stop the flow of corporate money—it only changed the channels through which this money moves.

Today corporations remain free to contribute soft money to non-connected political committees, popularly referred to as 527s, to state and local candidates and to political committees, including party committees, at the state level. Corporations are also free to use trade associations and other tax exempt entities as vehicles for corporate political involvement.

As corporate political money routes continue to proliferate, the need for greater transparency and accountability on the part of the corporations increases. Companies have a responsibility to shareholders to ensure that corporate funds are being used in ways that advance the long-term interests of the company and enhance shareholder value. Boards of directors have a fiduciary responsibility to evaluate the risks involved with political spending and ensure that management's political expenditures align with shareholder interests. Finally, shareholders have a right to know how their money is being used politically and to hold the company accountable for its political activities.

To assure that transparency covers the full range of political spending, it is important to understand what that spending comprises and the various ways in which corporate money can be used for political purposes. **The purpose of this paper is to**

- define corporate political spending,
- provide an inclusive picture of the different routes that corporate money can take, and
- provide a map of corporate political spending, noting the significant breaks in transparency.

By working from a common understanding of what constitutes political spending, companies can create disclosure and approval policies that cover the relevant activities. Shareholders and other interested parties will know what is being disclosed.

Political Spending Defined

Using current regulatory definitions, including the Internal Revenue Service's (IRS) definition of political intervention, political spending comprises:

¹ The authors of the paper are Center for Political Accountability research director Jamie Carroll, co-director Bruce F. Freed and counsel Karl Sandstrom.

- **any direct or indirect contributions or expenditures on behalf of a candidate for public office or referendas,**
- **any payments made to trade associations or tax-exempt entities used for intervening in a political campaign, and**
- **any direct or indirect political expenditure that must be reported to the Federal Election Commission, Internal Revenue Service or state disclosure agency.**

This definition applies, but is not limited, to the following expenditures:

- Contributions to or expenditures on behalf of political candidates
- Contributions to or expenditures on behalf of political parties
- Contributions to or expenditures on behalf of political committees and other political entities organized and operating under 26 USC Sec. 527 of the Internal Revenue Code (i.e. Republican Governors Association and Democratic Governors Association)
- Any portion of any dues or similar payments made to any tax exempt organization that is used for an expenditure or contribution that if made directly by the corporation would not be deductible under section 162(e)(1) of the Internal Revenue Code
- Payment for advertisements, printing and other campaign expenses
- Donation of company products or services to a political organization
- Reimbursing someone for a political contributions

Political Spending and Disclosure Requirements

The political expenditures noted above are not disclosed in any central place. Companies are not currently required to disclose their political spending. Therefore, where—or if—the expenditures are disclosed depends on the nature of the expenditure and its recipient.

Following are typical corporate political expenditures and the relevant disclosure requirements:

Contributions to State and Local Candidates, Political Parties and Political Committees (including those supporting or opposing ballot initiatives)

State laws vary regarding corporate political spending. Roughly half the states allow corporate political contributions, with varying limitations on the allowable amounts. Few states obligate corporations to report. For the most part, state and local political contributions are reported by the recipient committees to the relevant state agency. These filings are available generally to the public.

Contributions to Other Political Entities Organized and Operating under 26 US Sec. 527 of the Internal Revenue Code

So-called **527s**² are allowed to receive unlimited corporate funds. These groups are required to report their contributions and expenditures to the Internal Revenue Service using Form 8872.³ These forms are available to the public. Companies are not required to report their contributions to 527s.

² This refers to political organizations which do not comprehensively report their activities to the Federal Election Commission or a state reporting agency.

³ Internal Revenue Service, Publication 557 (3/2005), Tax-Exempt Status for Your Organization, www.irs.gov/publications/p557/index.html

Political Payments to Trade Associations and Other Tax Exempt Organizations

Corporations can make unlimited payments to **trade associations and other tax exempt organizations**. Trade associations are not required to disclose their members, and companies are not required to disclose their trade association memberships.

Under **the tax code**, civic leagues and social welfare organizations (**501(c)(4) organizations**) and business leagues and trade associations (**501(c)(6) organizations**) may engage in political campaign intervention, so long as the political activity does not comprise the group's primary activity.⁴ Groups that do so are required to pay taxes on their political expenditures or their group's net investment income for the year, whichever is less.⁵

What Constitutes Political Intervention

According to the IRS, **political campaign intervention** includes any and all activities that favor or oppose one or more candidates for public office. For example:

- contributions to political campaign funds or public statements of position (verbal or written) made by or on behalf of an organization in favor of or in opposition to any candidate for public office are considered political intervention,
- distributing statements prepared by others that favor or oppose any candidate for public office is also considered political intervention, and
- allowing a candidate to use an organization's assets or facilities may also be considered political intervention.

Certain activities will require an evaluation of all the facts and circumstances to determine whether they result in political campaign intervention.⁶

Reporting to Companies

Trade associations are not required to tell companies the portion of their payments used specifically for political purposes. However, for tax purposes, they are required to tell companies the portion of their payments used for political *and* lobbying activities, unless the associations choose to pay a tax on this spending themselves.

⁴ Internal Revenue Service, Publication 557 (3/2005), Tax-Exempt Status for Your Organization, www.irs.gov/publications/p557/index.html

⁵ "Political Campaign and Lobbying Activities of IRC 501(c)(4), (c)(5), and (c)(6) Organizations," by John Francis Reilly and Barbara A. Braig Allen, Exempt Organizations-Technical Instructions Program for FY 2003, www.irs.gov/pub/irs-tege/eotopic103.pdf

⁶ Certain issue advocacy activity borders on political campaign intervention and requires a more thorough evaluation of the facts and circumstances. For example, even if a statement does not expressly urge votes for or against a specific candidate, according to the IRS, the statement might be considered political intervention if there is any message favoring or opposing a candidate. Even if the candidate is not identified by name, he or she can be identified by other means "such as showing a picture of the candidate, referring to political party affiliations, or other distinctive features of a candidate's platform or biography." Certain key factors that help determine whether the ad is political intervention are: whether the statement identifies a candidate; whether the statement is delivered close in time to the election; and whether the issue addressed in the communication has been raised as an issue distinguishing candidates for a given office. (Internal Revenue Service, Fact Sheet 2006-17, February 2006, Election Year Activities and the Prohibition on Political Campaign Intervention for Section 501(c)(3) Organizations, www.irs.gov/newsroom/article/0,,id=154712.00.html)

Tax Deductibility

Under the **Internal Revenue Code section 162(e)(1)**, members of trade associations cannot deduct the part of the dues or other payments to the group that is used for any of the following lobbying or political activities: influencing legislation; participating or intervening in a political campaign for, or against, any candidate for public office; trying to influence the general public, or part of the general public, with respect to elections, legislative matters or referendums (also known as grassroots lobbying); communicating directly with certain executive branch officials to try to influence their official actions or positions.⁷

As a result, trade associations are required by law to notify anyone paying dues the portion of their payments that the group estimates will be used for lobbying and political activities, as defined under section 162(e)(1). The associations are not required to provide a breakdown of these expenditures. As an alternative to giving the member companies this information, the trade association may choose to pay a tax—known as the “**proxy tax**”—at the highest rate imposed by the Internal Revenue Code.⁸

Company Knowledge of Trade Association Political Spending

Companies that are members of trade associations should therefore know the amount of their dues and other payments used for political and lobbying activities, unless the trade association is paying the proxy tax. Companies are not required to disclose that information to their shareholders or to the public.

Trade Association Political Disclosure: Minimal

Trade associations are required to disclose on their **Form 990s** the total dues received from members, the aggregate amount of lobbying and political expenditures, and the amount disclosed to members as the nondeductible portion of dues. However, the associations are not required to provide a breakdown of their section 162(e)(1) lobbying and political expenditures—only the aggregate amount is available.⁹

Trade associations are also required to disclose the aggregate amount used by the association for political expenditures on their Form 990s.¹⁰ The IRS defines a political expenditure as an

⁷ Internal Revenue Service, Publication 557 (3/2005), Tax-Exempt Status for Your Organization, www.irs.gov/publications/p557/index.html This rule includes an exception for local legislation expenses, such as: appearing before, submitting statements to, or sending communications to members of a local council with respect to proposed legislation of direct interest to the member.

⁸ Internal Revenue Service, Proxy Tax, www.irs.gov/charities/article/0,,id=112907,00.html and “Political Campaign and Lobbying Activities of IRC 501(c)(4), (c)(5), and (c)(6) Organizations,” by John Francis Reilly and Barbara A. Braig Allen, Exempt Organizations-Technical Instructions Program for FY 2003, www.irs.gov/pub/irs-tege/eotopicl03.pdf

⁹ “Political Campaign and Lobbying Activities of IRC 501(c)(4), (c)(5), and (c)(6) Organizations,” by John Francis Reilly and Barbara A. Braig Allen, Exempt Organizations-Technical Instructions Program for FY 2003, www.irs.gov/pub/irs-tege/eotopicl03.pdf

¹⁰ It is noted that many nonprofits that spend a significant amount on television ads and direct mailings and other expenditures during election campaigns still report \$0 for their political expenditures on their Form 990s. Many speculate that this reflects a failure on the part of the IRS to enforce the regulations. *Washington Monthly* editor Nicholas Confessore writes: “Given that there are 1.4 million tax-exempt organizations in the United States, and enough personnel to inspect about 2,000 of them per year, the chance of a random audit is about one in 700. In practice, the IRS rarely investigates a nonprofit unless somebody files a complaint. And even then, privacy concerns constrain the IRS from revealing whether or not it has opened an investigation, and indeed whether or not it has come to any judgment.” (“Bush’s Secret Stash: Why the GOP war chest is even bigger than you think,” *Washington Monthly*, May 2004) For

expenditure intended to influence the selection, nomination, election, or appointment of anyone to a federal, state, or local public office, or office in a political organization, or the election of Presidential or Vice Presidential electors. An expenditure includes a payment, distribution, loan, advance, deposit, or gift of money, or anything of value. It also includes a contract, promise, or agreement to make an expenditure.¹¹ Trade associations are not required to provide a breakdown of these expenditures.

Trade Association Segregated Funds: Different Reporting Requirements

Trade associations may establish separate segregated funds—such as a political action committee—which have their own reporting requirements. Trade associations may transfer dues or other payments to these funds. If those payments are used for political activities, that amount is taxable and should be reported on the trade association's Form 990 as part of the group's political expenditures.¹²

Conclusion: Implications for Companies and Shareholders

Corporate political spending can follow a variety of routes, some of which enable companies to limit and even escape disclosure of their political activity.

Corporate political contributions are not disclosed in any central place, leaving shareholders to scour countless state campaign finance reports and IRS filings. While campaign finance watchdog groups provide helpful information on corporate political giving, no one source provides a comprehensive picture of corporate political contributions.

Compounding the problem, corporations are allowed to funnel their political activity through trade associations and other tax exempt entities. As this paper details, under current tax laws corporate political spending can be run through a trade association with little risk that the corporate donors will ever be disclosed, and great risk that the corporate donors are not even aware of how their money is being used.

These gaps in transparency and accountability create serious financial, legal, and reputational risks for companies that make political contributions or that belong to politically active trade associations. In order to protect shareholder value and promote the company's best interests, companies should adopt approval, oversight, and disclosure policies that cover the full range of corporate political activity.

example, Public Citizen filed a complaint against the U.S. Chamber of Commerce and Institute for Legal Reform for failing to disclose political expenditures and grants to the IRS as required by law. In its complaint, the group states: "In each year from 2000 to 2003, the U.S. Chamber and ILR each did not report any political expenditures on line 81 of Form 990. These reports contradicted the groups' own assertions, facts asserted in press reports and records of advertisements that clearly conveyed, both in content and timing, activities designed to influence the outcomes of elections. The groups' failure to report political expenditures in the years 2000 to 2003 represents a clear violation and warrants an investigation by the IRS." (Public Citizen, Complaint to the U.S. Internal Revenue Service, Request for Investigation, Re: The U.S. Chamber of Commerce, EIN 53-0045720 and the Chamber's Institute for Legal Reform, EIN 52-2109035, www.citizen.org/documents/ACFIF3E.pdf)

¹¹ Internal Revenue Service, Instructions for Form 990 and Form 990-EZ, www.irs.gov/instructions/i990-ez/ar02.html#d0e4574

¹² "Political Campaign and Lobbying Activities of IRC 501(c)(4), (c)(5), and (c)(6) Organizations," by John Francis Reilly and Barbara A. Braig Allen, Exempt Organizations-Technical Instructions Program for FY 2003, www.irs.gov/pub/irs-tege/eotopicl03.pdf