Super PACs, Ballot Measures, and You—A Campaign Finance Primer for California Businesses

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When it comes to corporate money and politics, ambiguous rules and lax enforcement are the sad norm. But that does not mean the stakes are low. With the 2016 presidential campaign in full swing and the spotlight once again shining on political money, even innocent mistakes can make headlines and do significant damage to corporate brands, customer relationships, and share prices. It is thus a good time to brush up on the basics—and to dispel some of the myths–of federal and state campaign finance laws.

Super PACs, Super PACs, Super PACs!

These days, independent expenditure-only committees, commonly known as "super PACs," dominate the campaign finance conversation. That is not surprising, given the prominent role they are playing in the presidential race. According to the Wall Street Journal, presidential super PACs hauled in more than $250 million during the first six months of 2015—twice the amount raised by candidate committees.[1]

How did this happen? In 2010, the United States Supreme Court issued its opinion in *Citizens United v. Federal Elections Commission*, finding that under the First Amendment, the government cannot prohibit independent political expenditures by unions and corporations.[2] Shortly thereafter, the U.S. Court of Appeals for the District of Columbia cited *Citizens United* in invalidating federal contribution limits imposed on independent expenditure-only committees by finding such limits likewise violate the First Amendment.[3] Consistent with these decisions, the Federal Election Commission (FEC) has made clear that corporations, labor unions, political committees, and individuals can now make unlimited contributions to super PACs.[4]

Contrary to popular belief, though, these decisions did not open the floodgates for large donors. Even before *Citizens United*, corporations, unions, and wealthy individuals were writing large political checks to groups structured to be exempt from taxation under Internal Revenue Code (IRC) section 501(c)(4) (in the case of social welfare groups), 501(c)(6) (in the case of trade organizations), and 527 (in the case of political groups).[5] Prior to *Citizens United*, these tax-exempt groups could register voters and buy television ads, but they could not expressly advocate the election or defeat of a particular candidate or advertise close to election day. *Citizens United* and its progeny removed these restrictions and allowed unlimited spending on independent ads that encourage voters to support or oppose candidates right up to the election. This added flexibility made it easier for a small number of wealthy donors to influence the outcome of an election and led to the explosion of candidate-specific super PACs.

Of course, this sea change has not been without controversy. One area of debate is whether federal candidates are using super PACs to circumvent contribution limits applicable to their campaign committees. While super PACs can accept unlimited

sums from individuals, unions, and corporations, federal candidates are still prohibited from accepting any union or corporate money and can accept up to only $2,700 per election from individuals.[6] The challenge for regulators is how to maintain the principles underlying these limits in the face of seemingly incompatible rules that give unions, corporations, and wealthy individuals a way to spend unlimited sums.

The Supreme Court's answer to this dilemma was to point to the ethical line that prohibits super PACs from coordinating with federal candidates.[7] But in practice, that line has become blurred. It is now common to see candidates headline super PAC fundraising events, which the FEC has said is permissible as long as the candidates do not personally solicit contributions that violate the restrictions applicable to their campaign committees.[8] Candidates and super PACs are also finding creative ways to indirectly exchange information and strategies. For example, super PACs are often headed by individuals with close ties to their supported candidates.[9] Candidate committees are also publicly releasing polling results and advertising schedules so that their super PAC counterparts can avoid duplicative surveys and ad buys.[10] It remains to be seen whether future enforcement or legislative efforts will seek to curb these practices.

A second area of debate centers on disclosure. Super PACs, like other political committees, are required to disclose their donors. But that does not mean the public always knows the true source of a contribution. Super PACs can accept money from entities that are not legally required to disclose the source of their money, such as limited liability companies (LLCs) and tax-exempt social welfare organizations. In such cases, the super PAC will disclose only the name of the entity making the contribution, allowing the individual, corporation, or union actually funding that entity to remain in the shadows.[11] Media and public scrutiny of this issue has been mounting,[12] so we may soon see enforcement or legislative efforts to increase transparency.

Business lawyers should be aware of these issues when advising clients with respect to super PAC contributions. They also should be aware of the latent business risks associated with these contributions. Promoting a candidate or social cause invariably alienates shareholders or consumers with differing views.[13] As a result, many businesses have chosen to steer clear of super PACs. Indeed, of the hundreds of millions of dollars given to Republican presidential super PACs in the first half of 2015, only about $26 million came from corporations.[14]

Other Federal Rules Applicable to Businesses

Although super PACs are dominating the news coverage, businesses still use other, more traditional, avenues to participate in federal elections. Chief among them is the corporate PAC.

While a corporation cannot make direct contributions to federal candidates, it can establish a political action committee and solicit contributions from a restricted class of people that includes stockholders and management and their families.[15] Twice each year, a corporate PAC can also solicit contributions from non-management personnel and their families.[16] Contributions to corporate PACs are limited to $5,000 per year, although a spouse may make a separate $5,000 contribution.[17]

On the expenditure side, while corporate funds cannot go directly to federal candidates, they can be used to defray the costs associated with operating a corporate PAC, including rent, utilities, and salaries.[18] Such funds can also be used to pay for PAC fundraising events, although prizes and entertainment expenses are subject to the "One-Third Rule," which prohibits them from exceeding one-third of the total amount raised at the event.[19] There are no limits on the amount a corporation can spend on PAC overhead, and such disbursements are not reported to the FEC.[20]

As for contribution limits, corporate PACs that have at least fifty donors, have contributed to five or more federal candidates, and have been registered with the FEC for at least six months can give up to $5,000 per election to each federal candidate, $15,000 per year to each national party committee such as the Democratic Congressional Campaign Committee or the National Republican Senatorial Committee, and $45,000 per year to each national party account such as a presidential nominating convention.[21] Smaller corporate PACs that do not meet the above qualifications can give up to $2,700 per election to each federal candidate, $33,400 per year to each national party committee, and $100,200 per year to each national party account.[22]

Businesses also participate in federal elections through tax-exempt IRC section 501(c)(4) social welfare

organizations and 501(c)(6) trade associations. Like super PACs, these entities can solicit unlimited contributions, but, unlike super PACs, they cannot expressly advocate for the election or defeat of a particular candidate or use a majority of their funds for political campaign activities.[23] Yet even with these restrictions, 501(c)s still play a huge role in the political process, with some analyses showing that they outspent super PACs in each of the 2010, 2012, and 2014 election cycles.[24]

501(c)s remain popular despite the rise of super PACs for two reasons. First, unlike super PACs, 501(c)s do not have to disclose their donors to either the FEC or the IRS, allowing large donors to remain anonymous.

Second, the supposed line limiting the political activities of 501(c)s has become blurred. As noted, 501(c)s cannot fund ads that expressly advocate the election or defeat of a candidate, but they can use their money to fund "educational" ads, and it has become increasingly difficult to differentiate between an ad that seeks to educate and one that advocates the election or defeat of a candidate. In hotly contested races, it is now common to see 501(c)-funded attack ads that direct the public to contact a candidate without directly advocating for his or her defeat in an upcoming election. Arguably, these ads do not relate to an election. To the casual observer, however, the tone and timing suggest a clear intent to influence the outcome. Yet the law is far from clear. According to the IRS, an ad is "campaign-related" if it expresses a preference for or against a candidate.[25] Various factors are used to apply this standard to a particular ad, such as whether the ad identifies the candidate by name, is delivered close to the election, or addresses an issue that distinguishes the candidates.[26] However, in practice, this case-by-case approach has provided little guidance.

As a result, 501(c) groups continue to push the law's boundaries. For example, in 2012, two social welfare groups run by Karl Rove and the Koch brothers spent upwards of $300 million on ads attacking Democratic candidates.[27] And now, groups are emerging to support a single candidate, including a 501(c)(4) in North Carolina that spent virtually all of its money on ads to support one candidate for Congress.[28]

Efforts to reign in 501(c) political activity and require more disclosure have been met with stiff resistance.[29] So for this cycle, expect unlimited, anonymous contributions to continue pouring into 501(c)s.[30]

Again, though, business lawyers should be aware of the inherent risks associated with these contributions. Although the risks associated with contributions to 501(c)s may seem lower than with contributions to super PACs because 501(c)s are not legally required to disclose their donors, there is a growing media chorus to require more transparency.[31] In other words, anonymity cannot be guaranteed. Regulatory efforts or civil lawsuits could reveal the true source of a contribution. Media outlets may uncover it. Shareholder advocacy groups may demand it.[32] The potential harm to customer relationships and corporate brands should thus always be carefully weighed against the business objectives for making a contribution.

California Dreaming

In California, with nearly 40 million people, elections attract big money as well. On the extreme end, Meg Whitman's unsuccessful 2010 campaign for Governor cost $177 million.[33] Many down-ballot races typically run into the millions of dollars, too. In the 2013-14 election cycle alone, candidates and independent groups spent over $150 million on California State Assembly and Senate races.[34]

There are some key differences, though, between the rules applicable to federal elections and those applicable to California state elections. In state elections (but not federal elections), corporations can make direct contributions to candidates. Under current limits, individuals and corporations can give up to $4,200 per election to each Senate and Assembly candidate, $28,200 per election to each candidate for Governor, $7,000 per election to every other statewide candidate, and $35,200 per year to each state political party.[35]

Moreover, large donors have reporting obligations under California law. Any individual or business that contributes more than $10,000 in a calendar year to state or local candidates, ballot measure committees or other political committees qualifies as a "major donor committee" and must file semi-annual disclosure reports covering January 1 to June 30 and July 1 to December 31, respectively.[36] In odd-numbered years, major donor committees must also file reports covering January 1 to March 31 and July 1 to September 30, if they make more than $10,000 in contributions to elected state officers or their controlled committees.[37] And contributions of

$1,000 or more made within 90 days of an election must be disclosed immediately (within 24 hours of making the contribution).[38]

Aside from direct contributions, businesses can use their corporate treasuries to establish California independent expenditure committees (i.e., state-level super PACs). There are no expenditure limits applicable to these committees; however, as is the case with federal super PACs, their activities cannot be coordinated with any candidate or ballot measure committee. Moreover, expenditures must be periodically disclosed, and the independent expenditure committee's name and two largest contributors over $50,000 must be clearly identified on advertisements.[39]

Those wishing to spread the costs of political efforts more widely can instead establish a recipient committee. One common type is a "general purpose" committee, akin to a federal corporate PAC, formed to support or oppose more than one candidate or ballot measure. Contribution and expenditure limits applicable to general purpose committees vary based on how the money is spent. If the general purpose committee gives directly to state candidates, it cannot accept more than $7,000 per year from a single source and must abide by the same contribution limits applicable to individuals and businesses, namely $4,200 per election to each Senate and Assembly candidate, $28,200 per election to each candidate for Governor, $7,000 per election to every other statewide candidate, and up to $35,200 per year to each state political party.[40] Alternatively, if the general purpose committee spends money on other political causes (e.g., ballot measures, local candidates, independent expenditures, etc.), it can accept unlimited contributions. However, any contributions to the general purpose committee above $7,000 must be kept in a separate, restricted use account that cannot be used for state candidate contributions.[41]

Another common type of recipient committee is the "primarily formed" ballot measure committee. Ballot measures have become a way of life in California. More than a hundred potential measures have been filed for the 2016 ballot.[42] While only a fraction will qualify for the ballot, several look to attract substantial money both in support and opposition. A primarily formed ballot measure committee must begin reporting contributions and expenditures when the proponents of the measure begin circulating signature petitions.[43] While these committees can accept unlimited contributions, expenditures must be reasonably related to a political, legislative, or governmental purpose.[44]

Business lawyers should be aware that the naming of these committees can sometimes present issues, particularly for businesses that may want to support a measure without that support being readily visible. A ballot measure committee name must identify the ballot number or letter and the committee's position on the measure.[45] The ballot measure committee name also must identify any "sponsor" that contributes more than 80% of the committee's funds, collects payroll deductions for the committee, or provides nearly all of the committee's administrative services.[46] If a business meets one of these qualifications, that business' name must be included in the committee's name. If there is more than one sponsor and the sponsors are members of a common industry or identifiable group, the name can instead include a term that identifies that industry or group. Finally, the name must include a term that identifies the economic or special interests of contributors of at least $50,000.[47]

In making contributions to ballot measure committees, business lawyers should also be aware that ballot measure committee ads must identify the committee's top two donors of $50,000 or more.[48]

Summary

Campaign finance laws can be daunting due to their complexity, ambiguity, and relative lack of enforcement, and the willingness of many to push the envelope with respect to the scope of legally permissible activities. Yet missteps can be costly, particularly for businesses that rely on strong brands and customer loyalty. When approaching these issues, business lawyers should take special care to evaluate not only the legal limits, but also the business objectives and risks of the contribution.

Endnotes

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6 11 CFR sections 110.1, 114.2.

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16 11 C.F.R. § 114.6.

17 11 C.F.R. §§ 110.1(d), (i).

18 11 C.F.R. §§ 114.1(b), 114.5(b).

19 *See* 11 C.F.R. § 114.5(b)(2); FEC Advisory Opinion 2003-33.

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26 *Id*. at 3-4.

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37 Cal. Gov't Code § 84202.7.

38 Cal. Gov't Code §§ 82036; 84203.

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41 2 Cal. Code of Reg. § 18534. Note that while there are no state limits on general purpose committee receipts used for non-state candidates, advising lawyers should still consult local laws to ascertain whether any limits apply to local races.

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45 Cal. Gov't Code § 84107.

46 Cal. Gov't Code §§ 82048.7; 84102.

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