

NONPROFIT ADVOCACY
— AND —
THE POLICY PROCESS
A SEMINAR SERIES

*Structuring the Inquiry
into Advocacy*

VOLUME 1

Edited by
Elizabeth J. Reid



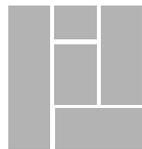
The Urban Institute

NONPROFIT ADVOCACY
— AND —
THE POLICY PROCESS
A SEMINAR SERIES

*Structuring the Inquiry
into Advocacy*

VOLUME 1

Edited by
Elizabeth J. Reid



The Urban Institute

Acknowledgments

We wish to thank the seminar cohosts, Evelyn Brody and Frances Hill, the authors and seminar participants, and many others who contributed valuable insights to the seminars and to the volume. Maria Montilla, Jeff Krehely, Nick Stengel, and Pho Palmer all provided valuable assistance to the project. We are grateful for the support of the Robert Sterling Clark Foundation, the Nathan Cummings Foundation, and the Surdna Foundation, Inc.

Nonprofit Advocacy and the Policy Process: A Seminar Series Advisory Panel Members

Audrey Alvarado
*National Council for
Nonprofit Associations*

Elizabeth T. Boris
Center on Nonprofits and Philanthropy

Evelyn Brody
*Chicago-Kent College
Illinois Institute of Technology
School of Law*

Rosemary E. Fei
Silk, Adler & Colvin

Frances Hill
*University of Miami
School of Law*

Leslie Lenkowsky
*Indiana University
Center on Philanthropy*

Debra Minkoff
*Yale University
Department of Sociology*

John Pomeranz
Alliance for Justice

Elizabeth J. Reid
*Center on Nonprofits and Philanthropy
The Urban Institute*

Peter Shiras
Independent Sector

C. Eugene Steuerle
The Urban Institute

Copyright © October 2000. The Urban Institute. All rights reserved. Except for short quotes, no part of this book may be reproduced or utilized in any form or by any means, electronic or mechanical, including photocopying, recording, or by information storage or retrieval system, without written permission from the Urban Institute.

The nonpartisan Urban Institute publishes studies, reports, and books on timely topics worthy of public consideration. The views expressed are those of the authors and should not be attributed to the Urban Institute, its trustees, or its funders.

Contents

Foreword	v
Schedule of Seminars	vi
Executive Summary	vii
1 Understanding the Word “Advocacy”: Context and Use	1
<i>by Elizabeth J. Reid</i>	
2 Political Parties, Interest Groups, and Congressional Elections	9
<i>by Paul S. Herrnson</i>	
3 The Uses of Section 527 Political Organizations	23
<i>by Rosemary E. Fei</i>	
4 The Practical Economics of “Pay to Play” Politics	35
<i>by Fred S. McChesney</i>	
Appendix: Additional Discussions	51
List of Seminar Attendees	55
About the Editor	57
About the Contributors	59
About the Cohosts	61
About the Center on Nonprofits and Philanthropy	63

Foreword

The Center on Nonprofits and Philanthropy has embarked on a series of 10 seminars to explore the engagement of nonprofit organizations in the policy process and the regulation of their political activities. **Nonprofit Advocacy and the Policy Process: A Seminar Series** examines the current regulation of nonprofit advocacy, proposed reforms, and the impact of regulation on nonprofit contributions to civic and political participation, policymaking, and representative democracy.

This publication, *Structuring the Inquiry into Advocacy*, is the first of four reports on the seminar series. It covers the first three seminars, held during the winter and spring of 2000 at the Urban Institute. The series began in February 2000 and ends in December 2001.

Each seminar addresses a different aspect of nonprofit advocacy and features discussion of commissioned papers. Authors present their draft papers at the seminars, followed by an open, roundtable discussion in which participants offer their insights and experiences. A diverse, bipartisan audience of approximately 40 policymakers, members of the academic and research communities, and nonprofit practitioners from a variety of organizations attends each seminar.

An evolving discussion paper, “Nonprofit Advocacy and the Policy Process,” provides background information for the 10 seminars. It introduces concepts and information related to each of the seminar themes, allowing participants to enter the seminar process at any point in the series with a common frame of reference. The paper is updated periodically to include new insights from the seminars. It will be published in its final form in the last seminar volume, but it is accessible on the Web in its current form at <http://www.urban.org/advocacyresearch>.

Two scholars from the field of nonprofit law, Professors Evelyn Brody of the Chicago-Kent College of Law and Frances Hill of the University of Miami School of Law, cohost the series. The project is guided by an advisory committee whose members represent a wide variety of disciplines, backgrounds, perspectives, and organizations and is managed by Elizabeth Reid of the Center on Nonprofits and Philanthropy at the Urban Institute.

This seminar series begins to explore the complex issues and tap the wealth of expertise that can inform dialogue about nonprofit advocacy. I hope that the papers presented in this series will stimulate discussion long after the seminars conclude. I would like to thank the cohosts, the authors, and the seminar participants for their thoughtful contributions to the discussions and to this publication.

Elizabeth T. Boris
Director of the Center on Nonprofits and Philanthropy

REPORTS ON
NONPROFIT ADVOCACY
— AND —
THE POLICY PROCESS
A SEMINAR SERIES

THIS VOLUME

Structuring the Inquiry into Advocacy

- SEMINAR 1
February 18, 2000 Nonprofit Advocacy: Practices and Perspectives
- SEMINAR 2
April 7, 2000 Regulating Nonprofit Advocacy: The Rules, Rationales,
and Practices
- SEMINAR 3
June 2, 2000 Politicians, Parties, and Access in the Policy Process

FORTHCOMING

*Volume II: The Fall/Winter 2000–2001 Series:
Exploring the Organizations*

- SEMINAR 4
September 22, 2000 Advocacy Strategies and Influence
- SEMINAR 5
December 8, 2000 Financing Nonprofit Advocacy
- SEMINAR 6
January 19, 2001 Representation, Participation, and Accountability

FORTHCOMING

*Volume III: The Spring/Summer 2001 Series:
In the States, across the Nation, and Beyond*

- SEMINAR 7
March 16, 2001 Nonprofit Advocacy in the States
- SEMINAR 8
May 18, 2001 Nonprofit Advocacy in Global Perspective
- SEMINAR 9
September 14, 2001 Constitutional Perspectives on Nonprofit Advocacy

FORTHCOMING

Volume IV: The Role of Nonprofits in Democratic Governance

- SEMINAR 10
December 7, 2001 Nonprofit Advocacy and Democracy
Final discussion paper “Nonprofit Advocacy and the Policy Process”

Executive Summary

Structuring the Inquiry into Advocacy, the Spring/Summer 2000 series, introduced advocacy as a concept, highlighted the experiences of different kinds of advocacy organizations, identified structural gaps in current regulation, and examined how groups adapt political practices in the political system. The series comprised three different seminars.

The first seminar looked at the diverse meanings of the concept of advocacy and the wide variety of activities and organizational practices through the experiences of five nonprofit organizations: the YMCA of the United States, the Concord Coalition, the Advocacy Institute, the American Society of Association Executives, and the AFL-CIO. The second seminar examined the structure of nonprofit political regulation under federal tax and election law and several controversial advocacy practices developed by nonprofit organizations. The emergence of the so-called “new” Section 527 organizations was the focal point of the discussion during this seminar. The third seminar examined the practice of soliciting money and services for campaigns in a pay-to-play system and the evolving relationship between nonprofit organizations and political parties in candidate-centered and money-driven elections.

Four papers, summarized below, were presented during the Spring/Summer 2000 series. This volume contains the complete text of each paper and three separate appendixes with summaries of related discussions. Each session brought together persons of diverse experiences and new perspectives around nonprofit advocacy issues. We hope that the themes discussed in this volume will lead toward a multidisciplinary framework for policy analysis and further research.

Summary of Chapters

Understanding the Word “Advocacy”: Context and Use

Elizabeth Reid, of the Urban Institute, explores differences in how the term “advocacy” is used in nonprofit studies, regulation, and practice. The paper introduces the reader to advocacy in a variety of contexts. The term may refer to activities influencing policymaking; specific activities subject to regulation; types of nonprofit organizations active in shaping public information, policy, and programs; and venues for social and political change. Because advocacy can describe such a wide range of activities, the paper urges those engaged in dialogue, law, and research about the nonprofit sector’s role in social and political change to understand the versatility of the term and the variety of meanings it conveys.

Political Parties, Interest Groups, and Congressional Elections

Paul Herrnson, of the department of government and politics at the University of Maryland, addresses changes in political parties in response to changes in the political environment, especially campaign finance. He discusses how nonprofit organizations, including parties and groups, have adapted to and altered the legal framework that regulates contemporary congressional campaign finance. Parties and groups have created new spending mechanisms and organizational entities that enable them to pursue their goals by spending money both within and outside the confines of the law. Herrnson concludes that these changes have transformed certain aspects of the candidate-centered congressional election system, weakened political

representation and accountability, and increased the influence of wealthy individuals and groups at the expense of others.

The Uses of Section
527 Political
Organizations

Rosemary Fei, of Silk, Adler & Colvin, begins her paper with a review of the history and context of Section 527 of the Internal Revenue Code, the tax-exempt category for organizations whose purpose is to influence the election of candidates to public office. Fei describes tax lawyers' creative use of these political organizations, beginning with the 1996 elections and continuing through early 2000, that allowed some donors to evade campaign finance disclosure laws by forming a new type of Section 527 group. After heightened media exposure of these "new" 527 groups' influence during the 2000 presidential primaries, in July 2000 Congress enacted legislative changes imposing reporting requirements on so-called "stealth PACs" of their funding sources and expenditures, similar to those required by campaign finance laws. While this paper was written only months prior to the new legislation, it sets the stage for and foresees the regulations' passage, even attempting to predict how major donors and their legal counsel might react to them.

The Practical
Economics of
"Pay to Play" Politics

Fred S. McChesney, of Northwestern University Law School, discusses the idea that political participants pay to play. Using the economic theory of rent seeking, McChesney discusses first the "pay" and then the "play." Amounts contributed to politicians have risen for two decades, although the term "contributions" is a misnomer. He suggests that firms, trade groups, unions, advocacy organizations, and other contributors are buying something—but what? Conventional wisdom says special interests are buying favors. Sometimes they are. But a great deal of money is paid not for favors, but to avoid disfavor. Politicians use various legal mechanisms to extort money from potential victims of harmful legislation that is proposed but then withdrawn—for a price. Contributors, McChesney suggests, pay to avoid the harm politicians can inflict through legislative action.

1 Understanding the Word “Advocacy”: Context and Use

E L I Z A B E T H J . R E I D

Advocacy is a word that is up for grabs in public discourse, research, and policy. Journalists, activists, academics, lawyers, government officials, classifiers, nonprofit managers, and others use the word differently in their professions. “Advocacy” describes a wide range of individual and collective expression or action on a cause, idea, or policy. It may also refer to specific activities or organizations. Sometimes a distinction is made between advocacy on behalf of others and grassroots advocacy or civic and political participation. The word is often modified to describe the venue for political action.

Discussion about nonprofit advocacy that reaches across academic disciplines and professions often encounters definitional problems. Does the word “advocacy” clarify or confuse this discourse? Does the word have negative or positive attributes? How does it compare to other words that describe civic and political engagement, words like social action, political action, public voice, social capital, mobilizing, or organizing? Is it a useful word for research and analysis? Do regulatory constraints associated with nonprofit lobbying and political activities create confusion about its meaning and application to nonprofit practices?

To lessen ambiguity in research and regulation about nonprofit advocacy, it is important to define which activities are advocacy activities, what advocacy activities are regulated and why, and which organizations are advocacy groups. Sorting through definitions and use of “advocacy” clarifies discussions about the role and behavior of nonprofits as social and political actors, nonprofit impact on governance and citizen participation, and the scope and rationale of regulation for nonprofit political activities. Some of the more common entanglements in defining and using the term in research and regulation are noted below.

Advocacy Activities and Organizations

Advocacy activities can include public education and influencing public opinion; research for interpreting problems and suggesting preferred solutions; constituent action and public mobilizations; agenda setting and policy design; lobbying; policy implementation, monitoring, and feedback; and election-related activity. However, there is no agreement on which activities constitute advocacy, and no one source gives a full account of the many kinds of activities and strategies groups use to leverage

influence in the policy process. Each research project must define the activities important to the question under study. Further, there must be continual clarification about what kinds of activities are subject to regulation.

Although data on organizations are available through a variety of sources, it is difficult to use them for the study of nonprofit advocacy. When researchers operationalize advocacy as a broad set of activities (Boris and Mosher-Williams 1998), data collection and classification of advocacy activities can be difficult and imprecise. When research focuses on a smaller subset of activities, such as lobbying or litigation (Salamon 1995), the empirical profiles often provide only a partial picture of the wider phenomena. Internal Revenue Service (IRS) data for advocacy analysis are limited to the collection of information on lobbying expenditures. Definitional problems come into full play when data are combined from diverse sources, such as lobbying disclosure data, Federal Election Commission (FEC) data, Encyclopedia of Organizations data, and surveys. Additionally, the significance of any data set can be overstated in paper titles such as “Explaining Nonprofit Advocacy” or “Nonprofit Advocacy Organizations.”

It is also important to clarify which groups are “advocacy” organizations. All nonprofits build organizational capacity and infrastructure to meet their missions, although groups that engage in advocacy are likely to strengthen their organizations in ways most useful to achieving their political goals. Groups engage in advocacy activities to various extents: as the primary focus of their work, as a regular part of their overall activities, and on occasion when an issue spurs them to action. Some groups have specific organizational structures and decisionmaking processes to accommodate their political affairs; others join coalitions or policy networks to increase their capacity to advocate effectively.

There are over 1.5 million nonprofit organizations grouped into classification schemes of many shapes and sizes offering different windows into nonprofit advocacy. The federal tax code separates nonprofits into 21-plus categories of tax-exempt organizations, and permissible political activities vary by category. Using IRS taxonomy of organizations and data helps us understand levels of expenditures for certain kinds of legislative and political activities. It also structures the use of the tax-exempt form for political purposes. For example, social welfare organizations, 501 (c)(4)'s, may engage in unlimited amounts of legislative lobbying and thus serve as an organizational vehicle for citizens who wish to associate for public policy purposes. Other tax-exempt groups, such as trade and professional associations, veterans groups, and labor unions, share the same benefits of association and latitude of political action and are also active political players.

Charitable groups or 501 (c)(3) organizations are limited by the IRC in the amount they can spend on lobbying. Since they are primarily service organizations, other classification systems offer ways to collect information about the services they provide to the public. These classification systems can also show us information about advocacy in relation to program services. The National Taxonomy of Exempt Entities (NTEE) has a common code for advocacy called Alliance/Advocacy Organizations. The Program Services Classification system incorporates coding to indicate advocacy as one of the services groups perform as part of their mission. The IRS uses activity codes that include advocacy as one of the organizational activities that groups

may self-select to describe their affairs at the time of yearly Form 990 filing. However, it is generally thought that limits on 501 (c)(3) advocacy discourage these nonprofits from using the word “advocacy” to describe their affairs. Thus it is hard to get a full picture from these data and classification schemes about the extent to which groups interface with the process of policy development and policymaking.

Most analysis of the nonprofit sector requires a rigorous look at the links between specific activities and specific organizations. Advocacy activities are embedded in distinct organizational models, setting boundaries around the practice of advocacy and participation in the political process by insiders and outsiders alike (Minkoff 1999). Interest groups, political organizations, mobilizing groups, public interest groups, citizen organizations, multi-issue organizations, social movement organizations, and other descriptions of nonprofit organizations as policy actors fill our democratic vocabulary and adopt different advocacy activities and strategies. Jeffrey Berry points out, “It is not their tax status that distinguishes them from other nonprofits, but rather it’s that they are openly and aggressively political” (Berry 1999).

Other social science research contributes to our understanding of organizations and activities. For example, interest groups have been studied at the national level to determine how patrons shape their advocacy practices (Walker 1991). Social movement organizations mobilize resources from their broader environment; over time, the loose alliances and protests of social movements evolve into more routine advocacy in nonprofit organizations (Zald and McCarthy 1987). Some research asks which groups are effective advocates, what kinds of activities are effective, and at what stages of the policy process groups are most successful (Rees 1998; Berry 1999).

Representation and Participation

Nonprofit organizations are intermediaries between citizens and other institutions of government and business. They deepen the ways in which people are represented and participate in democracies. Contrasting advocacy as organizational representation with advocacy as social and political participation can be a useful way to describe how nonprofit organizations relate to the body politic.

Nonprofit advocacy as representation evokes the familiar phrase “on behalf of.” This interpretation draws meaning from the Latin word *advocare*—coming to the aid of someone. A strong tradition of case advocacy exists in the United States. Advocates appeal through court action on behalf of individuals and classes of people whose interests are underrepresented in government. Case advocacy may open the political system to new voices and interests as the courts redefine the rights of individuals and the roles of state and society in addressing social problems.

When advocacy is viewed as representation of interests, values, or preferences, questions may arise about the legitimacy of organizations to represent us. Nonprofits that are regular players in policy and politics may or may not include citizens in their internal organizational affairs or engage citizens in public action. Further, organizational styles of advocacy vary and the nonprofit community can be divided in its approaches to social reform. Social justice advocates prefer their efforts not to be associated with special interest lobbies or inside political operators striking deals with

little public consent or exploiting the political system to serve a narrow interest. Community organizers, who urge citizens to come together and speak out about their concerns, prefer not to be confused with the paternalistic styles of professional do-gooders.

Advocacy, examined as social and political participation, emphasizes how people take action “on their own behalf.” Nonprofit advocacy as participation refers to collective action and social protest as well as the face-to-face contact of people and their political leaders. Language about the practice of advocacy as participation includes grassroots action, civic voice, public action, citizen action, organizing, mobilization, and empowerment. We look to participation indicators to judge the health of our democracy, but whether or not we are currently in a participatory drought depends on the indicator. If voting is a measure, we are about to die of thirst. If volunteering is a measure, we have found an oasis. If campaign donations are a measure, we are in a flash flood.

Nonprofit organizations are central to civic engagement, especially churches, unions, and other groups that link citizens to governance. Social networks that develop norms of trust and reciprocity among citizens—social capital—may shape the conduct of citizens in democratic decisionmaking (Putnam 2000). Advocacy as participation addresses the ways organizations stimulate public action, create opportunities for people to express their concerns in social and political arenas, and build the resources and skills necessary for effective action (Verba, Scholzman, and Brady 1995). Professionalized advocacy organizations and political consultants may have replaced earlier traditions of civic engagement and political action (Skocpol and Fiorina 1999).

The distinction between advocacy as organizational representation and as participation has led to the contradictory use of the terms “direct” and “indirect” advocacy in practice and research. In research, indirect advocacy may describe the participatory aspects of nonprofit advocacy, particularly the capacity of groups to stimulate individual citizens to take action on their own behalf. In contrast, direct advocacy may refer to lobbying and other appearances before key decisionmakers by organizational representatives on behalf of others (McCarthy and Castelli 1996). Adding to the confusion, the IRS calls lobbying on specific legislation “direct advocacy,” while community organizers call mobilization “direct action.”

Government-Centered and Society-Centered Advocacy

Government-centered advocacy and society-centered advocacy suggest different venues are available for building the political will to leverage policy change. In the American political system, the organization of interests is often described as an interaction of three sectors—government, society, and business—with competition and cooperation among these sectors when matters of public concern need attention. Global advocacy in the international system refers to advocacy among organizations and their networks in civil society, international institutions, and national governments.

Advocacy is often modified to describe the venue of action, and the resulting terms may be used interchangeably in law, research, and practice to describe either

activities or venues. Policy advocacy most frequently refers to advocacy that influences government policymaking. But Craig Jenkins's definition of policy advocacy as "any attempt to influence the decisions of an institutional elite on behalf of a collective interest" (Jenkins 1987, p. 297) encompasses decisionmaking in any kind of institution inside and outside of government.

Administrative advocacy, judicial advocacy, and legislative advocacy can help us focus on the uniqueness of decisions and processes in the different branches of government (OMB Watch 2000). Administrative advocacy and program advocacy focus on advocacy during the implementation phase of the policy process, when rules and regulations are promulgated and service delivery systems designed and put in place, sometimes with feedback from citizen groups (Reid 1998). Program advocacy is also used to describe the everyday work of organizations carrying out their charitable missions or providing services, as long as the activities are not outside the realm of protected speech; does not refer to specific legislation; and does not become partisan activity (Hopkins 1993). This interpretation shifts the focus to society.

Society-related advocacy suggests that nonprofits have an important role to play outside government in shaping public opinion, setting priorities for the public agenda, and mobilizing civic voice and action. Society-centered advocacy most often describes advocacy as social action, social change, or social movements. Nonprofits are vehicles for developing common visions and social missions, and advancing common interests and values collectively. They analyze, interpret, and convey information in society and thus create the context for government policy.

State and local advocacy is often distinguished from national advocacy because organizational resources, opportunities, and practices differ. Most grassroots advocacy takes place at the state and local level, yet national organizations are often the focus of research and media exposure. Organizational networks and practices are less formal at the local level. Advocacy may still be contentious or competitive, but the intimacy of the local setting means that activists and government officials may have more access to one another and may share social networks and contacts that mediate conflict. National-level advocacy, by comparison, involves larger, more formal organizations, structures, and practices. The links between national and local organizations may influence whether local voice has an organizational route to national decisionmaking.

Nonprofit advocacy advances the interests or values of a group that stands to benefit from action in the policy process or elsewhere. One measure of advocacy effectiveness is the extent to which a group succeeds in shaping new policy that directly benefits its constituency. Public interest advocacy makes broad public claims in the policy process on behalf of consumers and citizens. Organizations advocating for the disabled, the elderly, or an ethnic group, for example, may be more narrowly defined by their constituencies. Beneficiaries of advocacy, or those who stand to gain from policy change, may be the organizations themselves (through contracts) or groups of citizens (through public programs), or the public (through widely applicable policy). Self-defense advocacy is lobbying on issues necessary to an organization's survival.

None of these definitions are much help in understanding the wide range of nonprofit behaviors that make groups weak or powerful voices in policymaking. They do, however, help us locate where the advocacy is occurring and think about how

advocacy used in one arena might affect outcomes in another. Although the definitions say little about how groups acquire access or influence decisions in any one arena, they do lead us to think about the processes for decisionmaking in each arena that may affect opportunities for access or make one kind of activity more influential than another.

Lobbying and Advocacy

The IRS identifies the practice of nonprofit advocacy with specific organizational activity conducted by 501(c)(3) groups: direct lobbying (organizational lobbying for or against legislation) and grassroots lobbying (encouraging others to contact legislators to support or oppose legislation). Yet the language of advocacy remains problematic for regulators and practitioners. Independent Sector and the Alliance for Justice, groups that represent the interests of many nonprofits, have been instrumental in training groups to understand that regulated legislative advocacy is generally limited to specific types of lobbying activities and that simplified reporting procedures are now available to charitable organizations that lobby.

In April 1999, the General Accounting Office (GAO) issued a report on lobbying definitions in the Lobby Disclosure Act and the Internal Revenue Code Sections 4911 and 162(e). Their findings indicate that agencies use lobbying language to describe different sets of activities at the national, state, and local levels. These differences were found to affect registration and reporting requirements as well (GAO 1999).

Adding to the confusion, government and private funding agencies send mixed messages to contractors and grantees about the permissibility of engaging in advocacy and about reporting it. For example, IRS guidance indicates that lobbying is permissible because it is limited but not prohibited. Some agencies and foundations discourage the use of “advocacy” to describe organizational mission and activities. Foundations may use restrictive grant language that unnecessarily discourages grant recipients from engaging in advocacy when they are legally permitted to do so under the law.

The FEC uses “express advocacy” to define a bright line for partisanship that triggers reportable expenditures and limits. It requires that communications expressly advocate the election or defeat of a candidate by using language that instructs the voter to vote for or against a specific candidate. Thus, express advocacy is clearly and narrowly defined as a band of partisan communications regulated under federal election law. Issue advocacy, on the other hand, is an advocacy activity that has been a source of contention in law and practice because it generally falls outside the scope of either the IRS or FEC regulation as public education. Yet it is a powerful tool for groups advocating reform and favoring candidates with positions compatible with their organizational interests.

In conclusion, the term advocacy has multiple meanings depending on the context in which it is used. It broadly describes the influence of groups in shaping social and political outcomes in government and society. In law and regulation, advocacy refers to types of reportable activities, but regulatory agencies may differ on their use of the term. In research, advocacy may describe both the representational and

participatory aspects of groups as intermediaries between citizens and decision-makers, types of organizations and their capacity to advocate, and strategies of action in different venues.

No one definition of advocacy suffices to help us understand how groups influence policymaking or how regulation can best be designed to protect against political abuses yet not inhibit public engagement in the political life of the nation. Yet the term can be used broadly as an umbrella for cross-cutting discussion from different perspectives and expertise to help inform regulation and practice. If discussions about nonprofit advocacy practice and regulation are to bridge discourse across academic disciplines, organizational expertise, and regulatory perspectives, participants will have to be precise about the meaning of advocacy.

- REFERENCES
- Berry, Jeffrey. 1999. *New Liberalism: The Rising Power of Citizen Groups*. Washington, D.C.: Brookings Institution.
- Boris, Elizabeth T., and Rachel Mosher-Williams. 1998. "Nonprofit Advocacy Organizations: Assessing the Definitions, Classifications, and Data." *Nonprofit and Voluntary Sector Quarterly* 27 (December): 488–507.
- Hopkins, Bruce. 1993. *Charity, Advocacy and the Law*. New York: Wiley.
- Jenkins, Craig. 1987. "Nonprofit Organizations and Policy Advocacy." In *The Nonprofit Sector: A Research Handbook*, edited by Walter W. Powell (297). New Haven: Yale University Press.
- McCarthy, John D., and Jim Castelli. 1996. "Studying Advocacy in the Nonprofit Sector: Refocusing the Agenda." Draft paper prepared for the Independent Sector Spring Forum.
- Minkoff, Debra C. 1999. "Organizational Barriers to Advocacy." Paper presented to the Nonprofit Sector Research Fund Strategy Group, Wye River, Maryland.
- OMB Watch. 2000. "Reflections on Public Policy." <http://ombwatch.org/npt/resource/reports/reflect.html#top>.
- Putnam, Robert. 2000. *Bowling Alone*. New York: Simon and Schuster.
- Reid, Elizabeth J. 1998. "Nonprofit Advocacy and Political Participation." In *Nonprofit and Government: Collaboration and Conflict*, edited by Elizabeth Boris and Eugene Steuerle (291–325). Washington, D.C.: The Urban Institute Press.
- Rees, Susan. 1998. *Effective Nonprofit Advocacy*. Washington, D.C.: Aspen Institute.
- Salamon, Lester M. 1995. "Explaining Nonprofit Advocacy: An Exploratory Analysis." Draft paper prepared for the Independent Sector Spring Research Forum.
- Skocpol, Theda, and Morris P. Fiorina. 1999. *Civic Engagement in American Democracy*. Washington, D.C.: Brookings Institution Press.
- United States General Accounting Office (GAO). 1999. *Federal Lobbying: Differences in Lobbying Definitions and Their Impact*. Washington, D.C.: GPO.
- Verba, Sidney, Kay Lehman Schlozman, and Henry Brady. 1995. *Voice and Equality: Civic Voluntarism in American Politics*. Cambridge: Harvard University Press.
- Walker, Jack L. 1991. *Mobilizing Interest Groups in America*. Ann Arbor: University of Michigan Press.
- Zald, Mayer, and John McCarthy. 1987. *Social Movements in an Organizational Society*. London: Transaction Publishers.
-

2 Political Parties, Interest Groups, and Congressional Elections

PAUL S. HERRNSON

Political parties and interest groups have developed dramatically over the course of the twentieth century. Demographic transformations, technological advancements, and political reform have forced them to adapt to changes in the environment in which campaigns are waged and politics more generally are conducted. This paper provides a brief overview of these environmental changes and some of the adjustments that parties and organized groups have made in response to them. It also outlines party and interest group activities in recent congressional elections and discusses the impact that a relatively new form of campaign activity—party and interest group “outside spending”—has on congressional election outcomes.

Changes in the Political Environment

Over the course of the twentieth century, numerous changes have taken place in the environment in which political parties, interest groups, candidates, and individuals who participate in federal elections operate. Declining immigration, increased education, and out-migration from ethnic urban enclaves to the suburbs diminished the bases of political support on which old-fashioned political machines that once dominated election politics depended. Political reforms, including some the parties imposed on themselves, led to participatory primary nominations, banned patronage, and limited the political participation of government employees. These reforms stripped the machines of some of the major instruments they had used to dominate elections. The development of the mass media, the introduction of modern public relations techniques, and the emergence of a core of professional political consultants provided candidates with the ability to form personal organizations they could use to mount their campaigns in lieu of party committees. These changes combined to give rise to a high-tech, cash-driven, candidate-centered federal election system. Candidates are largely self-selected and responsible for the conduct of their own campaigns under this system. Parties and interest groups play supporting roles in it; they do not dominate elections, as parties did during the era of political machines.¹

The Federal Election Campaign Act (FECA) of 1974 codified into law certain aspects of the candidate-centered system. It introduced contribution limits for individuals, parties, and interest groups and prohibited corporations, unions, trade associations, and other groups from contributing their treasury funds to federal candidates.² The act created a campaign finance system funded solely with money that originated as relatively small contributions from individual donors (often referred to as “hard money”). The system limited the role of any one individual, party, or interest group in financing a federal election campaign. Although portions of the act were declared unconstitutional in *Buckley v. Valeo*, and it was amended in 1976 and 1979, the regulatory regime it introduced remained largely intact into the mid-1990s. It was not until the 1996 election cycle that parties and interest groups spent substantial amounts of money outside that regime (sometimes called “soft money”) to influence the outcomes of specific federal elections.³ The FECA, its amendments, and other changes in the regulatory regime introduced through Federal Election Commission advisory opinions and court challenges encouraged donors and recipients of political contributions to work both within and around the law, and to avoid breaking it. However, individuals and groups did not sit idly by and watch the regulatory environment change; the efforts of some of those making or collecting campaign contributions expanded the realm of campaign finance activity that was considered legal.⁴

Objectives and Organizational Development

Political parties in the United States are concerned first and foremost with electing candidates to public office. They seek to maximize the number of elected executive and legislative posts under their control. Enacting public policy is a secondary concern for U.S. parties. When a party does promote major policy change, such as during the New Deal era and the “Republican Revolution” of 1995, elections are usually the driving consideration behind its policy agenda.

Parties strive to achieve their seat maximization goals by recruiting strong candidates, influencing the campaign agenda, providing candidates in competitive elections with money and other forms of campaign assistance, mobilizing resources on these candidates’ behalf, communicating messages designed to win the support of undecided voters, and turning out their supporters on Election Day. Parties have had to make structural adjustments in order to perform these tasks in the contemporary political environment. The parties’ national, congressional, senatorial, and some state campaign committees, for example, have hired highly skilled political consultants and become important centers of campaign expertise.⁵

Party organizations that wish to contribute to federal candidates have had to create segregated accounts in order to carry out different election activities without violating the FECA or state laws governing campaign finance. The parties have used hard money accounts to contribute to federal candidates and make independent expenditures. They have used soft money accounts, consisting of funds raised from sources and in amounts prohibited by the FECA, to contribute to state and local candidates and to finance party-building activities, generic party-focused campaign ads, and voter mobilization drives. Soft money has most recently been used to pay for “issue advocacy ads,” including some ads that are intended to influence the outcomes of spe-

sific federal elections and feature the names or likenesses of individual candidates, but that fall short of explicitly calling for the candidates' election or defeat.

Interest groups also are concerned with elections, but their primary goals involve enactment of their preferred public policies. Whereas parties view policies primarily as a means for winning electoral support for their candidates, interest groups participate in elections because they want the government to enact specific policies. The differences in the organizations' goals are reflected in the fact that interest groups are more often involved in lobbying, court cases, and political protests than are parties.⁶

Interest groups have used elections to advance their goals in a variety of ways. Some groups use ideological or election-oriented strategies that are designed to maximize the number of members of Congress who share their overall policy orientation or positions on key issues. These groups, like parties, focus their efforts on competitive elections. A number of these groups recruit candidates, make campaign contributions, and carry out other campaign activities similar to those conducted by the parties.⁷

Groups that use access-oriented strategies view elections as the initial step in a larger strategy designed to open the doors of legislators' offices to a group's lobbyists. They contribute mainly to incumbents who are in a position to pass legislation that is of importance to the group. Considerations of electoral competition are not among their primary decisionmaking criteria.

Groups such as labor unions that use mixed strategies incorporate elements of the two strategies. They support candidates who share their ideological orientation or issue positions. Within this subset of candidates, they aid those involved in close elections and incumbents who hold influential positions in Congress.

Interest groups, like parties, have had to adapt to the constraints imposed by the political environment. Many have complex interconnected organizational structures that enable them to participate effectively in many aspects of the political process without violating the FECA or the Internal Revenue Code. Some groups form 501(c)(3) organizations to collect tax-deductible contributions to spend on research and educational activities, 501(c)(4) tax-exempt organizations to raise and spend money for a broader range of political activities, and political action committees (PACs) to raise hard money to contribute to candidates for federal office or make independent expenditures to expressly advocate a candidate's election or defeat. Despite the fact that some of these efforts are financed with soft money and made by organizational entities that are not supposed to engage in partisan politics, they all have the potential to influence a candidate's election prospects.

The most recent type of interest group organization to appear on the political scene for the purpose of influencing federal elections without adhering to the FECA's guidelines is the so-called new "527" group. Traditionally, federal candidate campaign committees and other organizations that fell into Section 527 of the tax code operated within the realm of the FECA. Recently, however, some individuals and interest groups, with the support of members of Congress and party committees, have created Section 527 organizations for the purpose of influencing federal elections while operating outside of federal campaign finance law. These groups are allowed to engage in more political activity than 501(c)(4) organizations. Until recently, they

were not required to disclose their fund-raising or spending activities and did not even have to publicly report their own existence, if they did not expressly advocate the election or defeat of individual federal candidates. These new 527 organizations represent a new vehicle for spending soft money.⁸

Campaign Activities

Agenda Setting Contemporary congressional elections are usually fought on local issues, and when congressional candidates discuss national issues they usually emphasize their local implications. Nevertheless, candidates can reap distinct advantages when the public focuses on national issues that are favorably associated with their party.⁹ Since the early 1980s, Democratic and Republican congressional leaders have distributed issue handbooks, press releases, and “talking points,” and broadcast generic party-focused issue advertisements designed to influence the national campaign agenda and to enable congressional candidates and local party activists to draw connections between local issues and national concerns.¹⁰ In 1994, the House Republican leadership succeeded in setting a national agenda focused on the ethical and policy failures of the Clinton administration and the popular 10-point program embodied in their Contract with America.¹¹ This helped the GOP win control of both houses of Congress for the first time in 40 years.

The 1996 and 1998 elections were less nationalized than the elections of 1994. In both of these contests, the Democrats sought to focus public attention on issues that traditionally have worked to the advantage of Democratic candidates, including education, environmental protection, health care, and the social safety net. The Republicans tried to set a political agenda that revolved around a balanced budget, tax cuts, crime and drug prevention, and traditional family values—issues that are favorably associated with the GOP. Despite spending millions of dollars of soft money on these ads, neither party succeeded in dominating the political agenda. Divided government—a Democratic president and a Republican-controlled Congress—made it impossible for either party to receive full credit or place full blame for the performance of the federal government and the state of the nation.

Interest groups have also sought to influence campaign agendas in recent election years. During the 1996 and 1998 elections, unions and business groups, led by the American Federation of Labor-Congress of Industrial Organizations (AFL-CIO) and the National Federation of Independent Business, used the airwaves to disseminate issue advocacy ads that focused on issues of concern to workers and small-business owners. The Sierra Club and the League of Conservation Voters sought to focus voters’ attention on environmental issues. U.S. Term Limits and Americans for Limited Terms conducted an extensive issue advocacy campaign for capping the length of service for members of Congress and state legislatures. These and other groups focused most of their agenda-setting efforts on a narrower set of interests and a smaller number of states and congressional districts than did the two major parties.

The Distribution of Campaign Resources Contemporary congressional elections require money and proficiency in the areas of campaigning requiring technical expertise and political research. Most candidates assemble campaign organizations consisting of paid staff and specialized con-

sultants to wage their campaigns. Candidates in competitive contests typically attract money, strategic advice, and campaign services from their parties' congressional, senatorial, or state committees. In 1998, party committees distributed roughly \$33.5 million in contributions and FECA Section 441(a)(d) expenditures (commonly called "coordinated expenditures") to their candidates. Most of these funds were distributed in accordance with national strategies devised by the parties' congressional and senatorial campaign committees (sometimes referred to as the Hill committees because they were originally located in congressional office space on Capitol Hill). Each Hill committee creates a list of "opportunity" or competitive elections and seeks to deliver as much money and other resources to those races as possible. In 1998, the parties distributed 80 percent of their House contributions and 90 percent of their Senate contributions to candidates in elections decided by 20 percent or less of the two-party vote.

Parties have developed several creative approaches to deliver hard money to candidates in close elections. Under one arrangement, when a state party is short on cash, the party's congressional, senatorial, or national campaign committees make an agency agreement allowing the committee to assume the state party's contribution or coordinated expenditures.¹² Under a second approach, national party organizations increase the amounts of hard money they can contribute to congressional races by exchanging their soft money for hard money raised by state party committees.¹³ A third type of transaction consists of a senatorial campaign committee contributing to a House candidate or a congressional campaign committee contributing to a Senate candidate. A final arrangement that is usually brokered by a national party organization features state party committees making contributions to one or more congressional candidates running outside their borders.¹⁴ These and other contribution schemes have enabled national party organizations to focus resources in close races, impose a national campaign finance strategy on congressional elections, and influence some state and local contests.¹⁵

As a group, PACs spend significantly more money in congressional elections than do parties. In 1998, PACs contributed about \$203.6 million to major-party House and Senate contestants. Business-related PACs, including corporate and trade association committees, distributed the vast majority of these funds, followed by labor PACs and nonconnected PACs (which have no sponsoring organization). Business PAC contributions reflected these groups' access-oriented strategies. Business PACs devoted approximately 85 percent of their House contributions to incumbents, giving roughly half of those funds to House members who held safe seats. They devoted roughly 70 percent of their Senate contributions to incumbents, donating three-quarters of those funds to senators who appeared to be virtually guaranteed reelection. Labor PAC contributions reflected unions' mixed strategies. Almost all of their money flowed to Democrats in close races or to those who held influential positions in Congress. Finally, most nonconnected PACs, such as the National Right to Life PAC and EMILY's List, which supports pro-choice Democratic women candidates, pursued ideological or mixed strategies.¹⁶

The Hill committees, some state party organizations, and some PACs also deliver campaign services to congressional candidates, including assisting with hiring campaign consultants, planning and adjusting their campaign strategies, raising money, researching issues, investigating their opponents' backgrounds, gauging public opin-

ion, buying mass media ads, and mobilizing voters. Party or PAC staffs furnish some of these services directly. They contract other campaign services from political consultants and redistribute them to candidates. Both approaches enable these organizations to provide candidates with support that is appraised well below market value and to exercise some influence over how candidates wage their campaigns.¹⁷

The Mobilization of Campaign Resources

In addition to delivering campaign contributions and election services directly to their candidates, parties act as brokers between candidates and the PACs, individual contributors, political consultants, and powerful incumbents who possess some of the money, political contacts, and campaign expertise candidates need.¹⁸ The Hill committees give candidates fund-raising lists, organize fund-raising events, and circulate fund-raising letters on behalf of competitive contestants. All four Hill committees make meeting rooms and telephones available to facilitate PAC fund-raising, which cannot be conducted legally on the Capitol grounds.

The Hill committees also manipulate the environment in which PACs make their contributions by publishing targeting lists, issuing press releases, meeting with political journalists, and briefing PAC managers. Hill committee staffs organize functions that offer PAC managers, lobbyists, and other individual donors access to congressional leaders in return for large contributions. The Hill committees also call on senior incumbents to host receptions and to help junior members of Congress and competitive nonincumbents solicit contributions from PACs. Candidates who appear on a Hill committee's opportunity list derive significant fund-raising advantages. However, party communications to PACs and other wealthy donors are controversial because contributors have been known to refuse to make contributions to candidates specifically because their names were omitted from such lists.¹⁹ As a result, these candidates were unable to raise the money needed to wage competitive campaigns.

During the 1998 congressional elections, the Hill committees and the parties' legislative caucuses played a critical role in redistributing campaign funds from safe incumbents to candidates in closely contested elections. The House Democratic Caucus and the House Republican Conference required incumbents to pay dues to their parties' congressional campaign committees and encouraged senior members to raise millions of dollars for these organizations. The parties' conferences in the Senate encouraged similar behavior. These funds were contributed primarily to candidates for marginal seats. The Hill committees also convinced incumbents, congressional retirees, and current and former members of Congress to donate \$16.0 million from their campaign accounts and the "leadership" (or "member") PACs they sponsor to House and Senate candidates. These funds generally were contributed in close contests, but the distribution of funds favored incumbents, reflecting some of the donors' interest in collecting favors from colleagues.²⁰

Some PACs, referred to as "lead PACs," also use a variety of means to steer the flow of campaign money to their preferred candidates. Like parties, these PACs organize fund-raising events and use other means to influence the information that other PACs and individuals use when making campaign contributions. For example, in 1998, EMILY's List bundled \$6.7 million in individual contributions for pro-choice Democratic women candidates, while directly giving them less than

\$224,000.²¹ WISH List, the GOP counterpart of EMILY's List, contributed and bundled substantially less money to pro-choice Republican women candidates.

Voter Mobilization

Party organizations assist candidates with registering voters, delivering them to the polls, and carrying out other grassroots campaign activities.²² Some of this activity is organized and paid for by the state and local party organizations. However, a significant portion is funded with soft money raised by party committees in Washington and transferred to state party committees. Most of this "coordinated campaign" activity takes place in states and localities that are critical to the success of a party's presidential, senatorial, or congressional candidates. Expenditures on voter list development, targeting, direct mail, and telephone banks enable party organizations in the nation's capital to influence locally executed grassroots activities that benefit the entire party ticket.²³ The Democratic national, congressional, and senatorial campaign committees spent a record \$40 million on coordinated campaigns in 1996.²⁴ Their Republican counterparts spent a record \$48.3 million that year.²⁵ Both parties spent substantially less during the 1998 midterm elections: The Democrats managed to spend about \$8 million and the Republicans spent almost \$26 million.²⁶

Many interest groups also spend large sums on voter mobilization. The AFL-CIO typically leads the pack, spending almost \$19 million to mobilize labor voters in 1998.²⁷ The Christian Coalition spent \$3.1 million to turn out conservative religious voters that year. Environmental, business, and a host of other groups also invested significant funds in the ground war.

Outside Spending on Campaign Communications

Following the Supreme Court's 1996 ruling in *Colorado Republican Federal Campaign Committee v. Federal Election Commission*, the parties were in a position to make independent expenditures for or against federal candidates.²⁸ PACs had been allowed to make them since the mid-1970s. Because the law requires independent expenditures to be made without the knowledge of a candidate or members of the candidate's campaign committee, parties and groups go to great lengths to give the appearance of divorcing their independent expenditures from their other operations. The National Republican Senatorial Committee, for example, has assigned some personnel to an independent expenditure group located outside its headquarters buildings. Its Democratic counterpart has not followed suit, but it claims to have established a firewall between party officials who directly assist a particular candidate's campaign and those involved in making independent expenditures.²⁹ Because the political community is not very large, it is natural to suspect that some communication about individual campaigns occurs among regular party staff, aides who make independent expenditures, PAC managers, and political consultants who work in campaigns.³⁰

During the 1996 and 1998 elections, parties spent unparalleled amounts of soft money outside of the campaign finance system. Some of these funds were spent on party building, grassroots party activities, and party-focused generic advertising, activities that were permitted under the 1979 amendments to the Federal Election Campaign Act. The parties also made unprecedented expenditures on agenda-setting activities and campaign communications intended to influence the election prospects

of specific candidates. The latter forms of communication, often referred to as issue advocacy ads, bore striking similarities to candidate-sponsored campaign ads, but they were substantially more negative than candidate ads.³¹

In October 1995, the Democratic National Committee began a \$42 million issue advocacy ad campaign to boost President Clinton's public opinion ratings and to label Republican members of Congress as radical extremists who sought to help the wealthy at the expense of working Americans. They also sought to focus voters' attention on issues that favored Democratic candidates. The Republicans aired \$20 million in issue advocacy ads between late March and their August 1996 convention to boost the campaign of Sen. Robert Dole, their presumptive presidential nominee. Both parties' Hill committees spent millions of dollars to set the campaign agendas in the most competitive congressional races and to praise their candidates and attack their opponents.³² During the 1998 elections, the Hill committees spent even more on issue advocacy ads. Many of these ads were tailored to suit individual House and Senate elections. Virtually all of them were broadcast in localities with very close races.³³

Numerous interest groups also broadcast issue advocacy ads that were designed to advance the prospects of individual candidates in 1996 and 1998. Some of these ads were generic in nature and aired in many congressional races; others were customized and aired in only one race. Most of the ads appeared in districts holding close contests, but roughly one-fourth of the funds spent on them was used to support unsuccessful primary challengers or to attack safe incumbents who disagreed with the groups' positions.³⁴

Party and Interest Group Competition, Conflict, Cooperation, and Coordination

Political parties and interest groups compete and cooperate in elections and in politics in general. Parties and groups that consider each other to be allies, such as the Democrats and labor unions and the Republicans and the Christian Coalition, vie with each other over scarce resources when fund-raising and attempting to influence the political agenda. Although parties and allied groups usually support many of the same candidates in the general election, conflict can arise because most groups pursue specific policy goals, while the parties seek to maximize the number of elective offices they hold. Disagreements sometimes arise in primary contests because the parties seek to nominate the candidate they perceive to be the most likely to win the general election, whereas many interest groups back the candidate who will be the strongest advocate for their cause. Conflict usually occurs when interest groups try to nominate ideological extremists in districts that traditionally support moderate candidates. Different goals and perspectives also can cause allied parties and groups to work at cross-purposes when they mobilize resources for candidates they have prioritized differently.

Nevertheless, there are reasons for parties and groups to cooperate. First, party leaders and allied groups share many policy interests and tend to support similar candidates. Second, their staffs are occasionally intertwined. Many political operatives have gone back and forth between working for a party, interest group, or political consulting firm. Some individuals even have a major leadership role in, or work for, a party and an interest group or a political consulting firm simultaneously. House majority whip Tom DeLay (R-Tex.), for example, is the GOP's third-ranking House member, is a very active member of the National Republican Congressional Com-

mittee (NRCC), and heads the Americans for a Republican Majority (a leadership PAC) and U.S. Family Network (a 527 organization). Some of his top aides also have played important roles in more than one of these operations.³⁵ Third, party and interest group leaders recognize that their organizations have different assets and liabilities and when they work together the synergy that results can benefit a candidate's election prospects.

Parties and groups cooperate in many ways. For decades, party organizations have collected contributions from interest groups and PACs, enabling the parties to obtain resources for party-building and election programs and the interest groups to gain access to congressional leaders and other key policymakers. Party leaders also have helped allied groups form PACs and raise money. More recently, parties have contributed funds to interest groups. In 1996, the Republican National Committee contributed \$4.6 million in soft money to Americans for Tax Reform.³⁶ The group used the funds to mobilize voters who oppose tax increases, some of whom were considering abandoning Republican contestants in favor of Reform Party candidates. By contributing soft money to Americans for Tax Reform and other outside groups, both parties were able to help their candidates without violating federal regulations on the amounts of soft money national parties can spend in individual states.³⁷ The NRCC's transfer of \$500,000 to the nonprofit U.S. Family Network in 2000 is a more recent example of a national party organization contributing to an allied interest group.³⁸ Recent party financial transfers to interest groups represent a reversal of the traditional flow of money from interest groups to parties. However, both kinds of transfers are important in that they show that when they cooperate, the groups can help each other accomplish their mutual goals.

The Impact of Party and Interest Group Efforts on Election Outcomes

Congressional elections are influenced by many factors. Incumbency, the partisan makeup of the district, campaign spending, campaign strategy, and media coverage are important.³⁹ Most research shows that House incumbents begin the election season with tremendous advantages over their opponents. Most are recognized by their constituents, have good job approval ratings, and represent districts that favor their party. Moreover, the mere fact of their incumbency indicates that most district voters have supported them in previous elections. Incumbents enjoy tremendous leads in the "expectations game," reflecting their reelection rate of 90 percent or better. Not surprisingly, there is little most incumbents can do to significantly increase the percentage of the vote they receive.⁴⁰ Overall spending, spending on campaign communications, and strategic decisions about targeting and issue selection do not help incumbents increase their vote shares.⁴¹

House challengers, on the other hand, begin the election season at a tremendous disadvantage in terms of name recognition, political experience, money, voter support, political expectations, and virtually every other predictor of election outcomes. For most challengers, the level of support is so low that it can only go up. Challengers in most House elections can control a number of factors that increase their vote shares. Challengers win substantially more votes than do others if they pick their

opponents carefully (running against first-term incumbents or members implicated in a scandal), spend a great deal on campaign communications, carefully target party members and independents, run on issues that are favorably associated with their party, and cultivate good relations with the local media. Nevertheless, few are able to overcome their opponent's daunting advantages and go on to win.⁴²

One of the more unusual aspects of the 1998 congressional elections was that parties and interest groups spent large amounts on televised issue advocacy ads and independent expenditures in competitive races.⁴³ These outside campaign communications changed the fundamental dynamics of the House contests in which they were aired. Challengers in districts that featured heavy outside spending on campaign communications experienced both costs and benefits. They benefited from this spending because it directly correlated with an increase in their vote shares. The downside was that outside campaign spending often overwhelmed the candidate's own campaign communications. Thus, when parties and groups saturated a district with independent expenditures and issue advocacy ads, their communications combined to drown out those disseminated by candidates, taking away from challengers the most potent tool they had in their campaign arsenal: the ability to use their message to win votes. Outside spending by parties and groups had a major impact on the conduct of some campaigns and may have been decisive in determining the outcomes of several competitive House and Senate elections.⁴⁴

Conclusion

Political parties and interest groups have adapted to the changes in the political environment that took place over the course of the twentieth century, including changes in the rules governing campaign finance. Some of their adaptations involved creating new programs and modifying existing organizations. Others involved creating new organizations that are connected with existing ones. Some of these organizational changes increased the level of cooperation between parties and interest groups; others increased the level of competition between these organizations.

Political parties, interest groups, individual donors, and candidates also have altered the political environment, often through challenging aspects of election law in the courts. The parties' most recent success in weakening the law, in the *Colorado* case, promises to allow them to spend more hard money on coordinated expenditures.⁴⁵ This decision could contribute to a recent trend that has made some congressional campaigns less candidate-centered. Reformers' first successful effort in 21 years to strengthen the regulation of money in federal elections, enacted in July 2000, requires the new 527 committees to disclose their donors and expenditures. It does not prohibit them from spending soft money, nor does it eliminate their influence on congressional elections. It is too soon to know the ultimate impact of the *Colorado* case or the laws intended to affect 527 committees. Moreover, these changes have yet to be subjected to full judicial scrutiny. Regardless of the impact of these recent developments, it is clear that political parties and interest groups have adapted to the contemporary political environment and have assumed more prominent roles in congressional elections, and will probably continue to do so in the twenty-first century.

The rise of party and interest group soft money, issue advocacy advertisements, and other forms of outside spending has broad implications for American democracy. When parties and groups broadcast issue ads and independent expenditures, they make it difficult for voters to discern candidates' campaign platforms, thus reducing voters' abilities to cast their ballots on the basis of the candidates' issue positions and to hold elected officials responsible for fulfilling their campaign promises. This weakens representation and accountability in government. Soft money contributions and expenditures also increase the political influence of the individuals and groups that can afford to participate in these transactions at the expense of those who cannot. Recent transformations in the campaign finance system have undoubtedly contributed to the decline in the level of trust that citizens have in their government. It is unlikely that anything short of a major overhaul of current campaign finance law will reverse this situation.

NOTES I wish to thank Michael Malbin for his helpful comments and suggestions.

1. See, for example, Sorauf 1980.
 2. Several aspects of the law, including limits on candidate contributions, were overturned in *Buckley v. Valeo*, 424 U.S. 1 (1976).
 3. The term "soft money" was coined by Elizabeth Drew in *Politics and Money: The New Road to Corruption* (New York: Macmillan, 1983), esp. 15. See also Alexander and Colorado 1995; Biersack 1996; Federal Election Commission 1999; Magleby 2000.
 4. Herrnson, forthcoming in 2001.
 5. Herrnson 1988.
 6. See, for example, Maisel 1999.
 7. Sabato 1981.
 8. Eilperin 2000; Fei 2000; Marcus 2000.
 9. Petrocik 1996.
 10. Herrnson, Patterson, and Pitney 1996.
 11. Gimpel 1996; Kolodny 1996.
 12. Herrnson 1988, 43–44.
 13. Barnes 1996; Dwyre 1996.
 14. Herrnson 1992.
 15. Bibby 1996.
 16. Herrnson 2000, 133–37.
 17. A few candidates have complained that the parties and groups that distribute campaign services have played too intrusive a role in their campaigns. See Salmore and Salmore 1989.
 18. Frantzich 1989; Herrnson 1988.
 19. Herrnson 1988, 2000.
 20. Herrnson 2000.
 21. Stephanie Kahn, communications director, EMILY's List, interview, Aug. 9, 1999 (Web site: <http://www.emilyslist.org/el-about/index.html>).
 22. Caldeira, Patterson, and Markko 1985; Cotter et al. 1989; Goodhart 1999; Huckfeldt and Sprague 1992; Krassa 1988; Wielhower and Lockerbie 1994.
 23. See, for example, Goodhart 1999.
 24. Don Fowler, national chairman, Democratic National Committee, interview, Feb. 23, 1997. Cited in Herrnson 1998.
 25. Haley Barbour, "Memorandum to Republican Leaders," Nov. 4, 1996.
-

26. Joseph Hansen, national field director, Democratic Senatorial Campaign Committee, interview, July 9, 1999; Johanson, political director, Democratic Congressional Campaign Committee, interview, July 9, 1999. Cited in Herrnson 2000; Nicholson 1999.
27. Bernstein and Dunham 1998; Lambro 1998.
28. *Colorado Republican Federal Campaign Committee v. Federal Election Commission*, 116 S. Ct. 2309 (1996).
29. None of the party's other Washington-based organizations made independent expenditures.
30. Herrnson 2000; Kolodny and Logan 1998.
31. Corrado et al. 1997; Goldstein et al., forthcoming in 2000; Herrnson and Dwyre 1996; Magleby 2000.
32. Herrnson 1998.
33. Ibid., 114.
34. Ibid., 142–43.
35. "Full Disclosure" 2000.
36. Babcock 1997; Barbour, "Memorandum to Republican Leaders"; Carr 1997.
37. The ratio of soft to hard money that a national party can spend in a state is determined by the number of state and federal elections held in the state in a given election. See, for example, Dwyre 1996, 411.
38. Chappie 2000 (April).
39. Jacobsen 1980; Kahn and Kenney 1999; Segal 1992.
40. For a different viewpoint, see Krasno and Green 1988.
41. Herrnson 2000.
42. Ibid., 231–35.
43. Party and interest group independent expenditures and issue advocacy spending were combined because of multicollinearity. For some excellent case studies of outside campaign spending in 1998, see Magleby 2000.
44. Herrnson 2000.
45. Chappie 2000 (May).

REFERENCES

- Alexander, Herbert E., and Anthony Corrado. 1995. *Financing the 1994 Election*. Armonk, N.Y.: M.E. Sharpe.
- Babcock, Charles R. 1997. "Use of Tax Exempt Groups Integral to Political Strategy." *Washington Post*, Jan. 7.
- Barnes, James A. 1996. "New Rules for the Money Game." *National Journal*, July 6.
- Bibby, John F. 1996. "The New Party Machine: Information Technology in State Political Parties." In *The State of the Parties*, edited by John C. Green and Daniel M. Shea (69–85). Lanham, Md.: Rowman and Littlefield.
- Bernstein, Aaron, and Richard S. Dunham. 1998. "Laboring Mightily to Avert a Nightmare in November." *Business Week*, Oct. 19.
- Biersack, Robert. 1996. "The Nationalization of Party Finance." In *The State of the Parties*, edited by John C. Green and Daniel M. Shea (108–24). Lanham, Md.: Rowman and Littlefield.
- Caldeira, Gregory A., Samuel C. Patterson, and Gregory A. Markko. 1985. "The Mobilization of Voters in Congressional Elections." *Journal of Politics* 47 (June): 490–509.
- Carr, Rebecca. 1997. "Tax-Exempt Groups Scrutinized as Fundraising Clout Grows." *Congressional Quarterly Weekly Report*, Feb. 22.
- Chappie, Damon. 2000. "U.S. Family Network Faces More Scrutiny." *Roll Call*, April 6.
- . 2000. "Party Spending Could Explode: Court Ruling Strikes Key Funding Limit." *Roll Call*, May 11.

- Corrado, Anthony, Thomas E. Mann, Daniel R. Ortiz, Trevor Potter, and Frank J. Sorauf, eds. 1997. *Campaign Finance Reform: A Sourcebook*. Washington, D.C.: Brookings Institution.
- Cotter, Cornelius P., James L. Gibson, John F. Bibby, and Robert J. Huckshorn. 1989. *Party Organizations in American Politics*. Pittsburgh, Pa.: University of Pittsburgh Press.
- Dwyre, Diana. 1996. "Spinning Straw into Gold: Soft Money and U.S. House Elections." *Legislative Studies Quarterly* 21 (August): 409–24.
- Eilperin, Juliet. 2000. "Secret, Unrestricted Gifts Finance New GOP Groups." *The Washington Post*, Jan. 8.
- Federal Election Commission. 1999. "FEC Reports on Political Party Activity for 1997–98." Press release, April 9.
- Fei, Rosemary E. 2000. "The Uses of Section 527 Political Organizations." Presented at the Urban Institute Seminar on Regulating Nonprofit Advocacy Groups, Washington, D.C., March 30.
- Frantzich, Stephen E. 1989. *Political Parties in the Technological Age*. New York: Longman.
- "Full Disclosure." 2000. *Roll Call*, April 6.
- Gimpel, James G. 1996. *Fulfilling the Contract: The First 100 Days*. Boston: Allyn and Bacon.
- Goldstein, Kenneth M., Jonathan S. Krasno, Lee Bradford, and Daniel E. Seltz. Forthcoming in 2000. "Going Negative: Attack Advertising in the 1998 Elections." In *Playing Hardball: Campaigning for the U.S. Congress*, edited by Paul S. Herrnsen. Saddle River, N.J.: Prentice Hall.
- Goodhart, Noah J. 1999. "The New Party Machine: Information Technology in State Political Parties." In *The State of the Parties*, edited by John C. Green and Daniel M. Shea (120–34). Lanham, Md.: Rowman and Littlefield.
- Herrnsen, Paul S. 1988. *Party Campaigning in the 1980s*. Cambridge, Mass.: Harvard University Press.
- . 1992. "National Party Organizations and the Postreform Congress." In *The Postreform Congress*, edited by Roger H. Davidson (59–60). New York: St. Martin's Press.
- . 1995. *Congressional Elections: Campaigning at Home and in Washington*, 2nd ed. Washington, D.C.: CQ Press.
- . 1998. *Congressional Elections: Campaigning at Home and in Washington*, 3rd ed. Washington, D.C.: CQ Press.
- . Forthcoming, 2001. "The Money Maze: Financing Congressional Elections." In *Congress Reconsidered*, 7th ed., edited by Lawrence C. Dodd and Bruce Oppenheimer. Washington, D.C.: CQ Press.
- Herrnsen, Paul S., and Diana Dwyre. 1996. "Party Issue Advocacy in Congressional Elections." In *The State of the Parties*, edited by John C. Green and Daniel M. Shea (86–104). Lanham, Md.: Rowman and Littlefield.
- Herrnsen, Paul S., Kelly D. Patterson, and John J. Pitney Jr. 1996. "From Ward Heelers to Public Relations Experts: The Parties' Response to Mass Politics." In *Broken Contract? Changing Relations between Citizens and Government in the United States*, edited by Stephen C. Craig (251–67). Boulder, Colo.: Westview Press.
- Huckfeldt, Robert, and John Sprague. 1992. "Political Parties and Electoral Mobilization: Political Structure, Social Structure, and the Party Canvass." *American Political Science Review* 86 (March): 70–86.
- Jacobson, Gary C. 1980. *Money in Congressional Elections*. New Haven, Conn.: Yale University Press.
- Kahn, Kim Fridkin, and Patrick J. Kenney. 1999. *The Spectacle of U.S. Senate Campaigns*. Princeton, N.J.: Princeton University Press.
- Kolodny, Robin. 1996. "The Contract with America in the 104th Congress." In *The State of the Parties*, edited by John C. Green and Daniel M. Shea (314–27). Lanham, Md.: Rowman and Littlefield.
-

- Kolodny, Robin, and Angela Logan. 1998. "Political Consultants and the Extension of Party Goals." *PS: Political Science and Politics* 31 (June): 155–58.
- Krasno, Jonathan S., and Donald Philip Green. 1988. "Salvation for the Spendthrift Incumbent." *American Journal of Political Science* 32 (November): 844–907.
- Krassa, Michael A. 1988. "Context and the Canvass: The Mechanisms of Interactions." *Political Behavior* 10 (May): 233–46.
- Lambro, Donald. 1998. "AFL-CIO's Election Day Effort Paid Off Big for Democrats." *Washington Times*, Nov. 5.
- Magleby, David B. 2000. *Outside Money: Soft Money and Issue Advocacy in the 1998 Congressional Elections*. Lanham, Md.: Rowman and Littlefield.
- Maisel, L. Sandy. 1999. *Parties and Elections in America*. Lanham, Md.: Rowman and Littlefield.
- Marcus, Ruth. 2000. "Flood of Secret Money Erodes Election Limits." *The Washington Post*, Jan. 15.
- Nicholson, Jim. 1999. *1998 Chairman's Report to the Members of the Republican National Committee*. Washington, D.C.: Republican National Committee.
- Petrocik, John R. 1996. "Issue Ownership in Presidential Elections, with a 1980 Case Study." *American Journal of Political Science* 40 (August): 825–50.
- Sabato, Larry J. 1981. *The Rise of the Political Consultants: New Ways of Winning Elections*. New York: Basic Books.
- Salmore, Barbara G., and Stephen A. Salmore. 1989. *Candidates, Parties, and Campaigns: Electoral Politics in America*, 2nd ed. Washington, D.C.: CQ Press.
- Segal, Jeffrey A. 1992. *Senate Elections*. Ann Arbor, Mich.: University of Michigan Press.
- Sorauf, Frank J. 1980. "Political Parties and Political Action Committees: Two Life Cycles." *Arizona Law Review* 22 (April): 445–64.
- Wielhower, Peter W., and Brad Lockerie. 1994. "Party Contacting and Political Participation, 1952–90." *American Journal of Political Science* 38 (February): 211–29.
-

3 The Uses of Section 527 Political Organizations

ROSEMARY E. FEI

CAVEAT: This paper was drafted before, and does not reflect, the July 1, 2000, enactment of legislation amending Section 527 and other sections of the Internal Revenue Code, with the effect, among others, of requiring disclosure of contributions to and expenditures by Section 527 organizations similar to that imposed by the Federal Election Campaign Act (FECA) on political action committees.

U ntil 1975,¹ no provisions of the Internal Revenue Code addressed the tax status of essentially political entities, and they fell through the statutory cracks, neither clearly taxable nor tax-exempt. In practice, political parties, candidate campaign committees, and political action committees paid no tax on their income from any source,² and, as an administrative matter, the Internal Revenue Service (IRS) did not require them to file returns. This result arose from the view that the typical sources of income to political organizations were in the nature of gifts not subject to inclusion in gross income of the donee under general federal tax law.³ In 1974, however, the IRS proposed to tax political organizations on their net investment income, and in 1975, Congress responded by enacting Section 527.⁴

Section 527 exempts political organizations⁵ from tax on their income from political contributions, dues, political fund-raising events or sales, and bingo games, *provided* the income is used to influence the selection of candidates for public office. In other words, to escape taxation, a political organization's income must pass two tests: one as it comes into the organization, and another as it goes out.⁶ Each test turns on the core purpose that forms the basis for a political organization's exemption: to engage in politics.

Section 527(e)(2) defines politics—the “exempt function” of a political organization—as legally⁷ influencing or attempting to influence the selection, nomination, election, or appointment of any individual to any federal, state, or local public office or office in a political organization, or the election of presidential or vice-presidential electors.⁸ The regulations⁹ abbreviate this as “the selection process.” This concept of exempt function applies regardless of whether the political organization is a political party, a candidate campaign committee, or an affiliated or freestanding political action committee.¹⁰

On the income side, the definition generally means that if income is derived from traditionally political sources, it is exempt. Political contributions, dues, gifts, or ticket sales made in response to political fund-raising efforts and sales of political campaign materials (but not in the context of a trade or business) all fall within this concept of exempt function income. What does not qualify as exempt function income is revenue earned by the political organization on its investments or through a trade or business. Net income from these sources of more than \$100 per year must be reported to the IRS¹¹ and is taxed under Section 527, generally at the highest corporate rate. The income side of the exemption test is relatively straightforward and seems to have generated fewer definitional and interpretive problems than the expenditure side.¹²

Once an incoming dollar meets the exempt function income test by arising from a political source, that dollar must still be “segregated for use only for the exempt function of the political organization” under Section 527(c)(3). This means that that dollar must be kept in a separate bank account, and eventually be spent by the political organization on an exempt function activity or (the statute implies) it will be taxed. And it is in this area—on the expenditure side—where interpretive problems arise more frequently,¹³ and where recent developments in the use of Section 527 political organizations, discussed further below, are occurring.

So what expenditures of a political organization have traditionally not qualified as being for an exempt function? First, public education on issues that is not biased for or against, explicitly or implicitly, any candidate, group of candidates, or political party is presumed not to influence the selection process within the meaning of Section 527.¹⁴ Second, lobbying the legislature (whether directly or through activating grassroots pressure on legislators) or the public on a ballot measure is generally presumed to be directed at changing the law, rather than influencing the candidate selection process.¹⁵ More than an insubstantial level of expenditures for such nonexempt activities in any year will disqualify an organization from exemption under Section 527 entirely,¹⁶ with the result that the organization will be taxable.¹⁷

To this point, this discussion of Section 527 has not distinguished among political parties, candidate campaign committees, and independent or affiliated political action committees, all of which are, for the most part, lumped together under the statute as political organizations. There are, however, some statutorily recognized subcategories. For example, unlike all other political organizations, which are taxed at the highest corporate rate, principal campaign committees of congressional candidates are subject to ordinary graduated corporate income tax rates.¹⁸ Newsletter funds also are subject to special provisions.¹⁹

Finally, a portion of Section 527 is directed at levying a tax, not on political organizations described in Section 527, but on organizations described in Section 501(c), such as labor unions, trade associations, chambers of commerce, or social welfare organizations, which make political expenditures within the meaning of Section 527.²⁰ Generally, the effect of Section 527(f) is to tax the 501(c) organization that engages in politics on the lesser of its political expenditures or its net investment income.²¹ The intent was to equalize the treatment of Section 527 political organizations and 501(c) organizations to the extent that they behave like political organizations, thus discouraging the use of 501(c) to avoid the taxes imposed by Sec-

tion 527. As an alternative to paying the 527(f) tax, the 501(c) organization can form a separate segregated fund (SSF) with as little formality as opening a bank account, and engage in politics strictly through the SSF, which will then be treated for purposes of Section 527 as a separate Section 527 political organization and taxed accordingly, instead of taxing the 501(c) organization.²² The catch is that, except where the 501(c) organization acts as a conduit for dues or contributions raised from members or donors for political 527 purposes and passes them promptly through to its SSF, any transfers from the 501(c) organization to its SSF will themselves trigger the 527(f) tax.

There is little evidence in the legislative history to show how Congress intended Section 527 to relate to the federal or state election laws applicable to the same political organizations. The statute does explicitly refer to election laws twice: once to define what qualifies as an SSF of a 501(c) organization,²³ incorporating both federal and state election law provisions; and again to define “principal campaign committee,” incorporating the federal election law definition.²⁴ One commentator has opined that while “[l]ittle thought was given [by Congress] to the relation between Section 527 and the new [Federal Election Campaign Act²⁵] . . . there appears to have been at least an implicit assumption that Section 527 organizations would be subject to the FECA.”²⁶ This assumption can explain the minimalist nature of the requirements for exemption under Section 527, both because more elaboration would be unnecessary, and because—ironically, as it turns out—Congress might have feared that detailed tax law provisions for political organizations would increase the potential for inconsistencies between the tax law and the FECA.²⁷

Whatever Congress intended, for a couple of decades after its passage, tax practitioners generally thought of Section 527 as the section of the Internal Revenue Code establishing the tax-exempt status to be assigned to political parties, candidate campaign committees, and political action committees regulated by federal and state election laws, and Section 527’s reach beyond them, if any, remained largely unexamined. Then, in the mid-1990s, nonprofit advocates began to make expanded use of Section 527 political organizations to influence the election of candidates for public office without engaging in express advocacy within the scope of the FECA. At least four factors converged to produce this trend.

First, the groundwork for these changes was laid when the courts drastically narrowed the jurisdiction of the Federal Election Commission (FEC) in *Buckley v. Valeo*²⁸ and its progeny, starting in the mid-1970s. These judicial interpretations have been incorporated into the FECA and regulations thereunder, resulting in the present-day regime, where only communications with an explicit and unambiguous electoral message—termed “express advocacy”—fall within the FEC’s regulatory authority.²⁹ It became obvious to tax practitioners (at least those few specialized in this area) that Section 527’s exempt function was left extending beyond the now severely truncated scope of the FECA.

Second, the Christian Coalition, formed in 1989, began aggressively distributing voter guides aimed at affecting the outcome of elections, continuing through the 1996 presidential elections. Despite an application filed in 1990, the IRS had refused to recognize the Christian Coalition’s exemption as a social welfare organization under Section 501(c)(4), apparently taking the position that its activities were primarily political.³⁰ The IRS’s continued reluctance in the Christian Coalition’s case indicated

to other advocacy groups that Section 501(c)(4) might have serious drawbacks as the vehicle for their election-related activities.³¹

Third, early in 1996, some 501(c)(4) groups and their cautious donors became concerned that the federal gift tax could apply to donations to 501(c)(4) organizations.³² If so, then while gifts of up to \$10,000 per year per donor per recipient are excluded from the gift tax,³³ the much larger amounts needed to purchase television time or newspaper space might constitute taxable gifts. As such, they will first reduce the donor's remaining estate and gift tax unified credit amount (currently \$675,000),³⁴ and thereafter trigger a gift tax liability, starting at 37 percent and climbing to 55 percent of the amount of the gift.³⁵ In contrast, contributions to Section 527 political entities are exempt by statute from the gift tax,³⁶ making them far more attractive and tax-efficient vehicles for wealthy donors desiring to affect elections, so long as the activity could be made to fit within Section 527 without triggering election law contribution limits. As noted above, tax practitioners had already observed that the Supreme Court's scaling back of the FECA left an area within Section 527 but outside the FECA. The question now focused on just how far Section 527 might reach, even beyond where the FECA began. Two private letter rulings issued by the IRS in 1996 and 1997 established, albeit nonprecedentially, that the gap was considerable.³⁷

In PLR 9652026, the IRS ruled favorably on Section 527 status for an SSF of a 501(c)(4) organization. The 501(c)(4) entity already had one SSF that engaged in reportable express advocacy or other activities within the jurisdiction of the FECA. Its new SSF would (pursuant to the Board resolution that established the entity) avoid any activity prohibited by the FECA or that would require FEC registration or reporting, but would engage in distribution of voting records and voter guides *unacceptable for a 501(c)(3) organization*.³⁸ The ruling's facts track closely the outline of the voter guides and voting records deemed acceptable for 501(c)(3) organizations in Revenue Rulings 78-248³⁹ and 80-282⁴⁰ by *negating* each of the specific factors the IRS cited as relevant to its decision. To give one example among many, in Revenue Ruling 80-282, which the IRS treated as a close call, the IRS relied on the fact that “[n]o attempt will be made to target the publication [of the voting record] toward particular areas in which elections are occurring nor to time the date of publication to coincide with an election campaign” in determining that the activity did not violate the 501(c)(3) electioneering prohibition. In PLR 9652026, in contrast, the representation was that “[d]istribution [of voting records] will be geared to the timing of the federal election” and “targeted toward congressional districts and states . . . primarily for political reasons.” The IRS states that “any activities constituting prohibited political intervention by a Section 501(c)(3) organization are activities that must be less than the primary activities of a Section 501(c)(4) organization, which are in turn, activities that are exempt functions for a Section 527 organization,” and concludes that, since distributing the voting records and voter guides would be prohibited for a 501(c)(3), their distribution is for an exempt function within the meaning of Section 527.

While it may already have been clear to the IRS, tax lawyers up to this point had not been sure exactly how far Section 527's exempt function reached in practice. A reasonable operating assumption had been that there were two lines, one delimiting 501(c)(3) nonpartisan activity at one end of the spectrum, and the other delimiting

527 political activity at the other end. The 1996 private letter ruling indicated that Section 527's reach extended all the way to the nonpartisan standard of Section 501(c)(3), meaning that there is only one line.

With this new perception that only a single line separated a 527 organization's exempt function from a 501(c)(3) organization's nonpartisan activity, the space between the two, where tax advisors had believed 501(c)(4) social welfare organizations or other 501(c) non-(3)s could operate, was eliminated. Contrary to much legal advice, it meant that any and every activity engaged in by a 501(c)(4) organization that was too political to be carried on by a 501(c)(3) charity was, in theory, subject to the Section 527(f) tax unless carried on in an SSF.

The next private letter ruling, PLR 9725036, took the development one step further. In a factual context apparently identical to that in the earlier letter ruling, one of the questions presented was whether grassroots legislative lobbying advertisements that describe a legislator's unsatisfactory or praiseworthy (in the eyes of the 501(c)(4) organization, at least) record on a particular issue, and then encourage the public to contact that legislator and urge him or her to vote on upcoming legislation on that issue in accordance with the organization's position, qualify as 527 exempt function activities if the legislator is also a candidate in an upcoming election. The IRS acknowledged the factual and educational content of the advertisements, but described them as having a "dual" character, both legislative and electoral. The IRS concluded that, so long as the requisite political motive was present, the added presence of a nonelectoral (i.e., lobbying) motive did not preclude qualification under Section 527. This raises the notion that an activity that could be acceptable for a 501(c)(3) organization if engaged in for purely legislative purposes could also be acceptable for a 527 organization if engaged in for electoral purposes. In the private letter ruling, it appeared that proof of electioneering intent need not be found within the four corners of the advertisement, but could instead be evident from when and where the advertisements were run, with timing and targeting engineered to maximize electoral impact.

In sum, in trying to solve the gift tax problem for major donors to 501(c)(4) organizations, tax lawyers pushed both donors and recipients further along the political spectrum, sometimes reluctantly, into forming Section 527 SSFs. Then, in an effort to make these SSFs as flexible as possible, tax lawyers substantially broadened the reach of Section 527, at least as it was commonly understood. While this approach was not driven by election law, it would, of course, attract the attention of election lawyers and their clients, with what some now see as dire election law consequences, undermining what was left of the scheme of contribution limits and disclosure of funding contemplated by the FECA. Whether tax lawyers intended, or could even have foreseen, these consequences is unclear.

This brings us to the fourth factor behind the increased operation of Section 527 organizations outside the FEC's jurisdiction in the mid-1990s. Despite the FEC's poor track record in the face of First Amendment challenges, the FEC and state election commissions continued trying to tighten enforcement of the remaining election laws relating to corporate contributions, contribution limits, and public disclosure. While direct challenges to these laws in court were often successful, court battles were expensive and extremely slow, and some donors and groups looked for ways to

circumnavigate election laws entirely. Tax lawyers' recent "discovery" of just how much broader was the IRS's tax law definition of political activities under Section 527 than that set forth by any election commission gave election lawyers just the opening they needed. Advocates found ample room to design programs to influence election outcomes without express advocacy of any candidate's election or defeat—independent of any candidate, party, or registered political action committee—and conduct those programs free of regulation under any election law, using a 527 political organization. Such political organizations are known informally as "soft PACs" because they do not receive "hard money" contributions that are subject to election law limits and disclosure.

As a result of these developments, since the 1996 elections, the term "issue advocacy" has taken on new meaning. Using Section 527 soft PACs, organizations have spent millions of dollars on televised messages to voters linking candidates to hot-button issues. Typically, the advertisement focuses on an incumbent candidate's record on a particular issue on which legislation is pending, such as family values, the federal budget, or the environment. The advertisement ends with a call to action, suggesting that viewers contact the legislator and urge him or her to vote a certain way on that pending legislation. The advertisement, considering its content only, might be an appropriate form of lobbying for a 501(c)(3) organization, but its timing (just before election day) and targeting (the message is run only in geographic markets where the incumbent is in a close race, where the candidates' positions on the issue to be addressed differ significantly, and where polling has shown that likely voters view the issue as important in deciding which candidate to support) indicate its political purpose. The PLR 9725036 ruling classified just this type of grassroots lobbying as a Section 527 political activity because it was "intended to have an effect on how the public will judge the positions of the incumbents and their challengers in November."

A 1999 private letter ruling took the limits of Section 527 yet another step further. As noted above, the exempt function of a 527 organization does not encompass legislative lobbying for its own sake. Tax practitioners generally understood this to preclude a ballot measure committee from qualifying under Section 527, since, as discussed above, a political organization's nonexempt functions must remain insubstantial in every year to maintain 527 status. Yet, particularly in states like California, with an initiative process running wild, donors wanted to be able to influence ballot measure outcomes as well as candidate elections, which in fact were often related in political terms anyway. Furthermore, state election laws frequently make little distinction between political committees formed to support or oppose a candidate and those formed to support or oppose a ballot measure, even though the IRS views the former as exempt under Section 527, while the latter generally fit under Section 501(c)(4), (5), or (6).

Faced with these circumstances, exempt-organization tax lawyers (who represent individual donors as well as the objects of their generosity) took the next logical step: using the approach in the 1996 and 1997 private letter rulings, but creating a free-standing 527 political organization instead of an SSF. This converted the 501(c) organization device revealed in the earlier rulings into a tool anyone, including an individual donor, can use. And, in light of the frequency with which ballot measures are—in the minds of their proponents and opponents, candidates and their political strategists, and the public—linked to candidate electoral outcomes, it made sense to

add to the new organization's political quiver the ability to work on ballot measures without the insubstantial ceiling, but as much as desired, so long as the candidate electioneering nexus can be credibly articulated and documented. Private letter ruling 199925051 was the result, providing a road map for doing just that.⁴¹

The next development in the Section 527 area may arise once again out of a desire by wealthy donors to minimize taxes, but this time it could be the capital gains tax at issue, rather than the gift tax. And the result may push the pendulum back toward 501(c)(4) organizations in some situations.

The exponential growth in the number of wealthy so-called “dot-commers” in Seattle and Silicon Valley—young, increasingly politically and charitably motivated multimillionaires, some of whom want to effect social change now and have the means to do it—has presented their tax lawyers with a new challenge. The problem is that their wealth is often nearly exclusively in the form of appreciated stock, and liquidating that stock produces taxable capital gains. While a large gift to a 501(c)(4) organization risks the gift tax, a gift of appreciated stock to a 527 organization is statutorily treated as if a sale of the stock at its fair market value occurred, followed immediately by a transfer of the stock's cash value to the political organization, making the donor taxable on the inherent capital gains.⁴² Gifts to a 501(c)(4) organization do not produce this result; rather, the 501(c)(4) organization takes the stock with a carryover basis from the donor⁴³ and realizes capital gains; but since 501(c)(4) organizations are not taxable on their investment income, the transaction is essentially capital gains tax-free. Suddenly, comparing the risk of gift tax to the certainty of capital gains tax, making the gift to the 501(c)(4) may be more attractive, especially if the donor is among the less tax-risk-averse.

If that hurdle can be surmounted, the next question is what kinds of high-political-impact activities are left that 501(c)(4) organizations can engage in, now that Section 527 may have squeezed them out. After all, if the only things the 501(c)(4) organization can do are activities acceptable for a 501(c)(3) organization, or excess legislative lobbying, why would the somewhat politically motivated donor not give the stock to a 501(c)(3) organization and get the charitable contribution income tax deduction?⁴⁴ Recall that, if the 501(c)(4) organization either spends the proceeds on electoral activities or gives the proceeds to its SSF, it will trigger the 527(f) tax.

But the 527(f) tax is levied only on the *lesser* of the 501(c)(4) organization's net investment income or the amount of the political expenditure. One solution, then, is to operate the 501(c)(4) organization so that it has no net investment income, or at least no *taxable* net investment income. The 501(c)(4) organization could keep its funds in a tax-exempt money market fund, earning a return, but one not subject to tax under Section 527(f). So long as the donor does not earmark the appreciated stock gift for Section 527 electioneering activity (which could conceivably cause the IRS to collapse the transaction and charge the donor capital gains tax), the 501(c)(4) organization may spend the contribution on Section 527 exempt functions with impunity.

On the other hand, the next big development in Section 527 may come from Congress. Reacting to numerous reports of how the new 527 organizations have been used as a loophole to escape the election laws, campaign finance reformers have proposed or are reported to be considering legislation to close the loophole, generally by

requiring Section 527 organizations to disclose their donors, finances, controlling interests, and political activities.

The problem with this approach is that Section 527 is not really a loophole, in the sense of a hole (intended or not) in the coverage of a law.⁴⁵ It is the tax category assigned to entities the nature of whose income is not appropriate to tax under general federal tax law, but whose activities are too political to qualify them under any other section of the Code as tax-exempt organizations. But the alternative to tax-exempt status is being taxable, and there is no limit on how political a taxable entity may be. Unless the tax exemption under Section 527 is highly valuable in terms of exempting from tax substantial income that would otherwise be taxable, a taxable entity could suffice. If, as it appears, the nature of political contribution income is such that it is not includable in gross income in the first place,⁴⁶ then the inability to deduct political expenditures as a business expense under Section 162(e) may not be a problem.⁴⁷ In other words, if legislative changes cause Section 527 status to cease offering the benefits now available, we may see a flight by political organizations out of Section 527 and into taxable corporations, where virtually all their income would come from political contributions, and so be free of corporate income tax. In fact, if a 527 organization has net investment or trade or business income, it pays tax at the highest corporate rate, while a business pays a graduated corporate income tax. It is therefore possible that Section 527 “exempt” status may actually be a burden, rather than a benefit, in some cases, so that any disincentives to use Section 527 will quickly outweigh its value, making other options more attractive.⁴⁸

A second problem with current legislative attempts to regulate Section 527 organizations is that, as it is now understood, the Section 527 category is simply enormous, not necessarily in the number of organizations involved, but in the range of activities it encompasses. So even if new legislation does not produce the flight from Section 527 discussed above, it will not necessarily produce the ends sought by campaign finance reformers: transparency, leading to less influence for money in politics. Any data reported by the universe of Section 527 organizations will include not only apples and oranges, but vegetables as well. Amounts spent on express advocacy, or attacks on a candidate’s positions or character falling just short of express advocacy, are not usefully lumped together with, or compared to, amounts spent on publicizing responses from all candidates in a race to a questionnaire on a narrow range of issues, or on regular and public distribution of voting records ranking legislators on how their votes on relevant legislation in the last legislative session compared to an organization’s agenda, or on a voter registration drive that uses specific issues to encourage civic participation without any reference to any candidate or party. Nor should campaign finance reformers be equally concerned with all the activities falling within the ambit of Section 527. Some new screen—coarser than the FECA, but finer than Section 527—will need to be developed before campaign finance reform based in tax law can be meaningful or effective.

In the family of tax-exempt organizations, the political organization may be seen as a stepchild of the shotgun wedding of the federal tax law to the federal election law. A recent extraordinary growth spurt has carried that child into unpredictable and irrational adolescence. What kind of adult the tax-exempt political organization will grow into remains unclear. We can only hope it outgrows its teenage awkwardness and becomes a responsible and productive member of tax-exempt society.

- NOTES The author wishes to acknowledge the contributions of Gregory L. Colvin to this paper.
1. This paper focuses on evolving issues in applying Section 527 of the Internal Revenue Code for the tax law practitioner, and the following general background discussion of Section 527 is short and simplified. For an excellent and comprehensive discussion and analysis of Section 527 well beyond the scope of this paper, and to which this paper is indebted, see Cerny and Hill (1996).
 2. *Communist Party of the U.S.A.*, 373 F.2d 682, 19 AFTR2d 613, 67-1 USTC ¶9208 (CA-D.C., 1967).
 3. I.T. 3276, 1939-1, Part 1 Cumulative Bulletin 108, and Section 102 of the Internal Revenue Code.
 4. All references to sections herein are to the Internal Revenue Code, unless otherwise indicated.
 5. It is not necessary to incorporate a political organization exempt under Section 527. Many are set up as unincorporated associations, and where the political organization is a separate segregated fund of a 501(c) organization (discussed at text accompanying note 21), it may be created with nothing more than a resolution of the 501(c) organization's board of directors. The 527 fund must have its own bank account and federal employer identification number, but no application to the IRS for recognition of exemption is required.
 6. This approach creates the anomaly that one cannot know whether a political organization's income is "exempt function income" and, thus, exempt from taxes, until it has been spent.
 7. Illegal expenditures by a political organization, or expenditures for an illegal activity, are not made for an exempt function. Reg. §1.527-5(a)(2).
 8. In 1988, Congress expanded the definition to include expenditures relating to a public office that, if made by the officeholder, would be deductible business expenses of the officeholder under Section 162(a). Section 527(e)(2).
 9. All references herein to the regulations are to the U.S. Department of the Treasury Income Tax Regulations unless otherwise indicated.
 10. It is perhaps inevitable that the use of the phrase "exempt function" to describe both the activities qualifying a Section 527 political organization for exemption and the activities qualifying a 501(c)(3) charitable organization for exemption will cause confusion, since the two meanings are nearly mutually exclusive.
 11. A Section 527 political organization, whether freestanding or affiliated with another organization, reports its taxable income by filing Form 1120-POL, which does not disclose anything about the political organization's activities, officers, directors, or donors and is not available to the public. If the political organization has less than \$100 in taxable net income for the year, no filing is required.
 12. For a recent example of interpretational issues on the income side, see PLR 9847006, in which proceeds from the sale of raffle tickets failed to qualify. The outcry this produced led the IRS to release a memorandum clarifying that if the raffle took place at a political event, the proceeds would be exempt function income. 27 *Exempt Organization Tax Review* 173 (January 2000). See also Rev. Rul. 80-103, 1980-1 Cumulative Bulletin 120, in which proceeds from the sale of art reproductions were deemed not exempt function income.
 13. For examples of some technical problems and anomalies in the definition of the Section 527 exempt function on the expenditure side, see Fei 1994.
 14. Regs. §1.527-2(a)(3); compare Regs. §1.527-2(c)(5), Example 8.
 15. Kindell and Reilly 1992, 451-52.
 16. Although no precedential guidance has been forthcoming from the IRS on the question of what is "insubstantial," an internal auditors' training article indicated that 5 percent
-

of total activities being nonexempt is probably acceptable, and the limit could go much higher. Kindell and Reilly 1992, 460.

17. Unless the level of nonexempt activities is so high as to become primary, the organization will not be able to qualify as exempt under any other section of the Internal Revenue Code due to excessive electioneering activity and will therefore be a taxable entity by default.
 18. Section 527(h)(1).
 19. Section 527(g).
 20. Section 527(f).
 21. If a 501(c) organization is subject to tax under Section 527(f), it must file Form 1120-POL on that taxable income, which is the same form filed by Section 527 political organizations and described at note 11.
 22. Section 527(f)(3).
 23. Section 527(f)(3).
 24. Section 527(h)(2)(A)(i).
 25. 2 U.S.C. 431 *et seq.*, 90 Stat. 490.
 26. Hill 1999, 205.
 27. Hill 1999b, 207.
 28. 424 U.S. 1 (1976).
 29. For a more detailed discussion of this evolution, see Hill 1999b, 212.
 30. Section 501(c)(4) organizations, like many other Section 501(c) organizations, are permitted to engage in 527 exempt function activities subject to the 527(f) tax discussed above, and only so long as such activities are not the primary activities of the organization. Candidate electioneering is not considered a social welfare activity by the IRS, so an organization primarily engaged in candidate electioneering would not qualify for exemption under Section 501(c)(4) as a social welfare organization. Rev. Rul. 81-95, 1981-1 Cumulative Bulletin 332.
 31. The Christian Coalition was eventually denied exemption under Section 501(c)(4) by the IRS (even though it prevailed, for the most part, over the FEC's claim that it had engaged in electioneering within the purview of the FECA) in a recent court test, *FEC v. The Christian Coalition*, 25 *Exempt Org. Tax Rev.* 471 (Sept. 1999). The IRS's decision has been challenged by the Coalition, is in litigation, and may well go to the Supreme Court. 2000 *Tax Notes Today* 41-49.
 32. Contributions to 501(c)(3) organizations are free of the gift tax under Section 2522, but contributions to other 501(c) entities may be subject to the gift tax under Section 2501(a)(1). The IRS's view that such gifts are taxable is stated in Rev. Rul. 82-216, 1982-2 Cumulative Bulletin 220. Nevertheless, the IRS's enforcement of the gift tax in this context appears to be almost nonexistent, and many donors choose not to pay the tax. The author is aware of two major accounting firms that are willing to take a reporting position that a gift to a 501(c)(4) ballot measure committee is not a taxable gift.
 33. Section 2503(b)(1).
 34. Sections 2505 and 2010.
 35. Sections 2502 and 2100.
 36. Section 2501(a)(5).
 37. For a thoughtful and provocative discussion in greater depth of each of the two rulings, see Hill 1999b, 208-10.
 38. Section 501(c)(3) organizations are prohibited from participating or intervening in candidate elections. The scope of this prohibition has been the subject of numerous Revenue Rulings, nonprecedential guidance from the IRS, and extensive discussion in the tax practitioner community, all of which is beyond the scope of this report.
 39. 1978-1 Cumulative Bulletin 154.
 40. 1980-2 Cumulative Bulletin 178.
-

41. This ruling is discussed in greater detail in Hill 1999b, 210–12. Hill expresses concern over the ruling’s reliance on various admittedly vague indicia of political intent as determinative of whether activities that may be neutral on their faces are in fact appropriately housed in a Section 527 political organization. On the other hand, Hill has argued the importance of intent as evidenced by the contemporaneous statements of agents of a 501(c)(3) organization with respect to violation of the 501(c)(3) electioneering prohibition (Hill 1997, 1999a). The substantiation methods discussed in the letter ruling were designed to create exactly the kind of detailed, contemporaneous written record of credible political motivations present in the Gingrich matter, as discussed in Hill 1997.
42. Section 84.
43. Section 1015(a).
44. Of course, gifts to 501(c)(4) organizations still make sense if the donor’s interest is in influencing legislation and no 501(c)(3) organization with adequate lobbying capacity is available. And 501(c)(3) organizations considering such gifts might well be concerned that accepting them will taint their charitable activities with politics, ultimately resulting in fewer gifts from the purely charitably motivated donors who are the bread and butter of most charities.
45. As noted above, the problem with 527 organizations’ lack of disclosure arises from the truncated reach of campaign finance disclosure laws, rather than anything to do with tax law or tax-exempt status.
46. See note 3 and accompanying text.
47. On the other hand, it is not clear to the author what the IRS’s position is on whether a taxable entity whose business is influencing candidate elections would be able to deduct political expenditures in calculating its taxable income under Section 162(e)(5)(A). That topic must await another paper.
48. Alternatively, recent IRS actions, while nonprecedential, and even disavowed by the IRS, may cause reexamination of Section 501(c)(3) as vehicles for some aspects of political movements. See Hill 1999b, note 12, and materials cited therein. And, as discussed briefly above, in some situations Section 501(c)(4) may make a comeback as well.

- REFERENCES
- Cerny, Milton, and Frances R. Hill. 1996. “Special Report: The Tax Treatment of Political Organizations.” *Tax Notes Today* 85–74 (April 29): 651.
- Fei, Rosemary E. 1994. “Non-exempt Function Expenditures Can Hold Serious Consequences for Political Organizations.” *Journal of Taxation of Exempt Organizations* 6 (1, July/August): 45.
- Hill, Frances R. 1999a. “Can Arguments about Subjective Intent Eliminate the Political Prohibition under Section 501 (c)(3)?” *Journal of Taxation of Exempt Organizations* 10 (4, January/February): 147.
- . 1999b. “Probing the Limits of Section 527 to Design a New Campaign Finance Vehicle.” *The Exempt Organization Tax Review* 26 (2, November): 205–19.
- . 1997. “The Role of Intent in Distinguishing between Education and Politics.” *Journal of Taxation of Exempt Organizations* 9 (1, July/August): 8.
- Kindell, Judith E., and John F. Reilly. 1992. “Election Year Issues.” *IRS Exempt Organizations Continuing Professional Education (CPE) Technical Instruction Program (1992)*, 400–93.
-

4 The Practical Economics of “Pay to Play” Politics

F R E D S . M C C H E S N E Y

*Money don't get everything, it's true,
But what it don't get I can't use.¹*

—Barrett Strong

Once upon a time, at least in popular imagination, politics was about public service, rather than personal aggrandizement. Political service was something that individuals did in addition to, rather than instead of, their jobs as butchers, bakers, and candlestick-makers. But as G. K. Chesterton noted, the notion of politics as a substitute for, rather than a complement to, ordinary economic pursuits has changed in the past century.

The mere proposal to set the politician to watch the capitalist has been disturbed by the rather disconcerting discovery that they are both the same man. We are past the point where being a capitalist is the only way of becoming a politician, and we are dangerously near the point where being a politician is much the quickest way of becoming a capitalist.

One way for politicians to become capitalists is to sell access to their political services, a transaction sometimes termed “pay to play,” in other words, money for a chance to transact in the political marketplace.

This chapter discusses some ways in which political office enables its holder to become a capitalist. As will be explained, it is typically assumed that what is being sold in political markets is special favors for special interests. The political game being played, however, is more complex than that suggested in this black-hat/white-hat characterization. That private interests pay politicians—for political access, influence, or favors—is undeniable. But it is less obvious what sort of play private interests are buying when they pay.

The “Pay to Play” Phenomenon

Background: Pay Concerns about “pay to play” begin with the first part, “pay.” The role of money in politics seems to be growing. It is difficult to establish this thesis rigorously, for no one has ever known exactly how much is paid to politicians, either in the past or now.² Even modern campaign disclosure laws do not require reporting of every check

written to every candidate. Moreover, payments may be both monetary and in-kind. For a political candidate needing a car to tour his district or state at election time, the loan of a car is just as valuable as a check that would go to rent a car from Avis.

Nonetheless, from what can be documented, growth in political contributions seems apparent. The most powerful fund-raising organizations for the past generation have been political action committees (PACs), creatures of the 1970s revolution in campaign finance laws.³ As figure 4.1 shows, the growth in PACs from the mid-1970s through the mid-1980s was substantial, particularly the growth in the number of corporate PACs. In 1974 (not shown), there were fewer than 1,000 PACs (Sabato 1984). By 1977, the first year shown in figure 4.1, the number had risen to well over 1,000. By 1985, the effects of the 1970s campaign law changes had produced a new, and apparently stable, equilibrium. The total number of PACs in 1985, just short of 4,600, was virtually the same as that in 1997.

However, these figures may be somewhat deceiving. While the 1980s saw equilibrium established in the sheer number of PACs, the amount of money they collect and disburse, plus the amount they hold in reserve for future elections, has grown substantially. This growth, which is shown in table 4.1, can be summarized for the period 1985–86 to 1997–98 as follows.⁴

Growth in PAC receipts	42.2%
Growth in PAC contributions to candidates	57.3%
Growth in cash on hand	99.9%

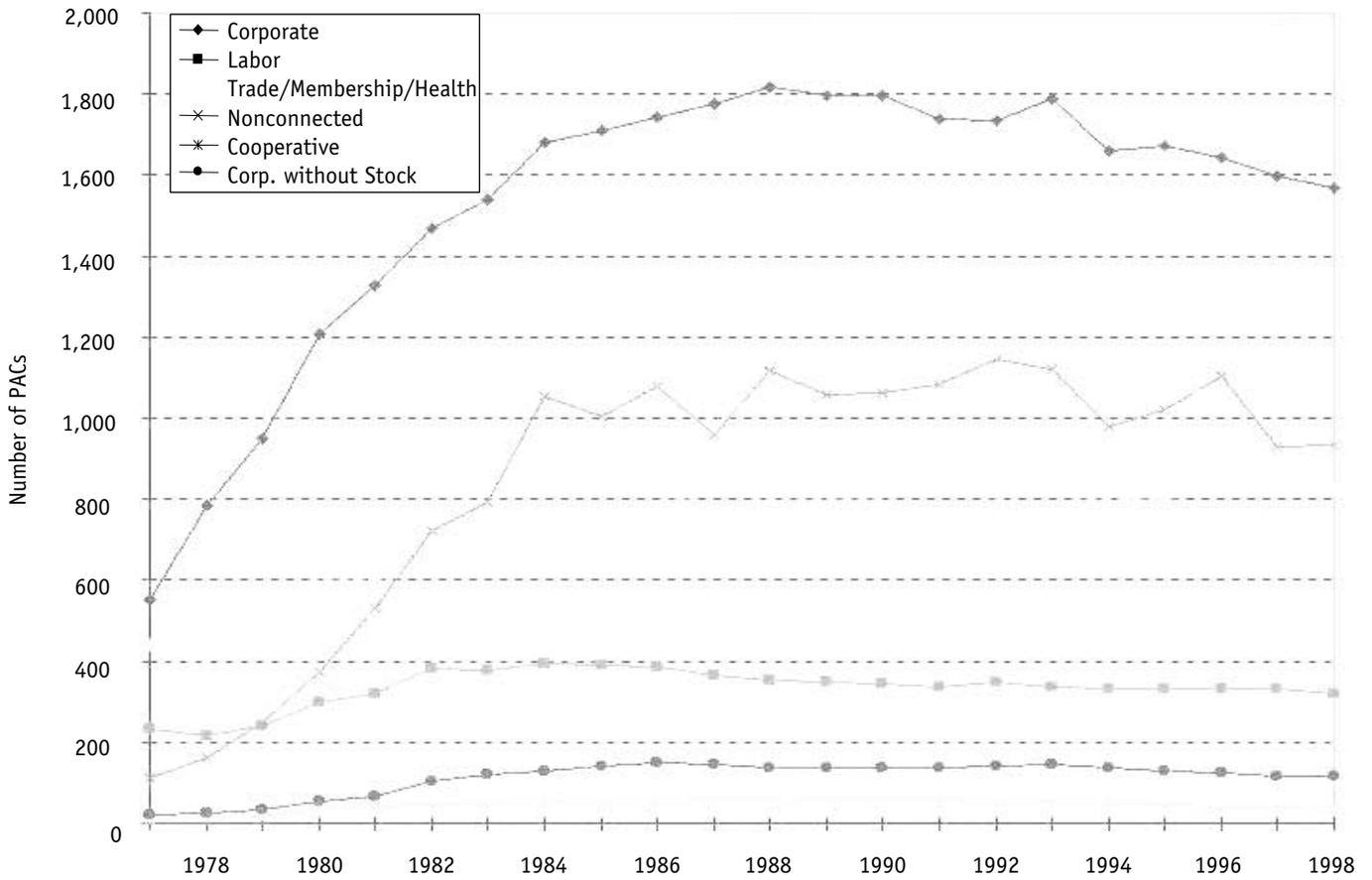
To put the numbers from table 4.1 in perspective, the figures from 1997–98 represent an average contribution to PACs of \$939,396 for the 535 House and Senate seats, and PAC disbursements of \$411,109 per seat. Ignoring the handful of open seats, incumbents receive some 82 percent of the money disbursed, meaning that incumbents receive on average \$338,126 in PAC contributions per two-year election cycle.⁵

The previous sentence adopts the terminology used popularly (as well as by the Federal Election Commission) in referring to money paid to politicians as campaign “contributions.” Campaign “donations” is another term often used. Both terms suggest that checks are written to politicians and political candidates in the same way that checks are written for philanthropic reasons to Boys Town, the United Negro College Fund, or the Red Cross. The terms connote eleemosynary motives and self-denial, rather than personal motives and self-interest.

Despite the nomenclature, however, it is safe to say that few people believe today (if they ever did) that political contributions are truly donations. Discussing PAC contributions and other soft money payments, Common Cause recently opined, “the soft money system taints everyone in it—the givers, the candidates, and the parties. . . . [T]hanks to soft money, the public now sees parties largely for what they, sadly, have become: mail drops for special interest money.”⁶

This, then, is the origin of concern over “pay.” If contributions were truly donations made without expectation of reward, presumably concerns about the money being paid to politicians would diminish. But as indicated by Common Cause’s reference to “special interest money” (another popular phrase today), the general sense is that altruism plays little role in campaign contributions.

Figure 4.1 PAC Count—1977 to Present



The Issue: Play Although the “pay” phenomenon seems well established, what is meant by “play” is not so clear. What is it, exactly, that contributors are thought to be paying for? What game, that is, are they playing?

For the most part, commentators content themselves with describing payments as made for “access.” To quote Common Cause again, “corporations, unions, and

Table 4.1 PAC Activity, 1985–86 to 1997–98

Year	No. of PACs	Receipts	Pct. Change	Contributions to Candidates	Pct. Change	Cash on Hand	Pct. Change
1985–86	4,596	\$353,429,266		\$139,839,718		\$69,062,430	
1987–88	4,832	\$384,617,093	8.82%	\$159,243,241	13.88%	\$88,963,751	28.82%
1989–90	4,677	\$372,091,977	-3.26%	\$159,121,496	-0.08%	\$103,340,543	16.16%
1991–92	4,727	\$385,530,507	3.61%	\$188,927,768	18.73%	\$95,155,888	-7.92%
1993–94	4,621	\$391,760,117	1.62%	\$189,631,119	0.37%	\$98,967,582	4.01%
1995–96	4,528	\$437,372,321	11.64%	\$217,830,619	14.87%	\$103,907,879	4.99%
1997–98	4,599	\$502,576,840	14.91%	\$219,943,566	0.97%	\$138,046,331	32.85%

wealthy givers know that big money can result in extraordinary access and influence for their interests. Today, in Washington, if you want to be heard, it's much easier if you have a big soft money check that can help pave the way."⁷ It is suggested in this paper that that approach—viewing payments as made for “access”—obscures rather than clarifies the nature of the game being played. For, in fact, two very different games are being played when private interests make payments (“contributions”) to gain access to politicians.

The Orthodox Story: Rent Creation

In referring to private-donor money buying “access and influence for their interests,” Common Cause presents the orthodox version of the game that private interests and politicians are thought to play (Stigler 1971). It is a process known in economics (and, increasingly, in other social sciences and law) as rent creation, “rent” referring to returns available through the political process rather than through private-market exchanges.⁸

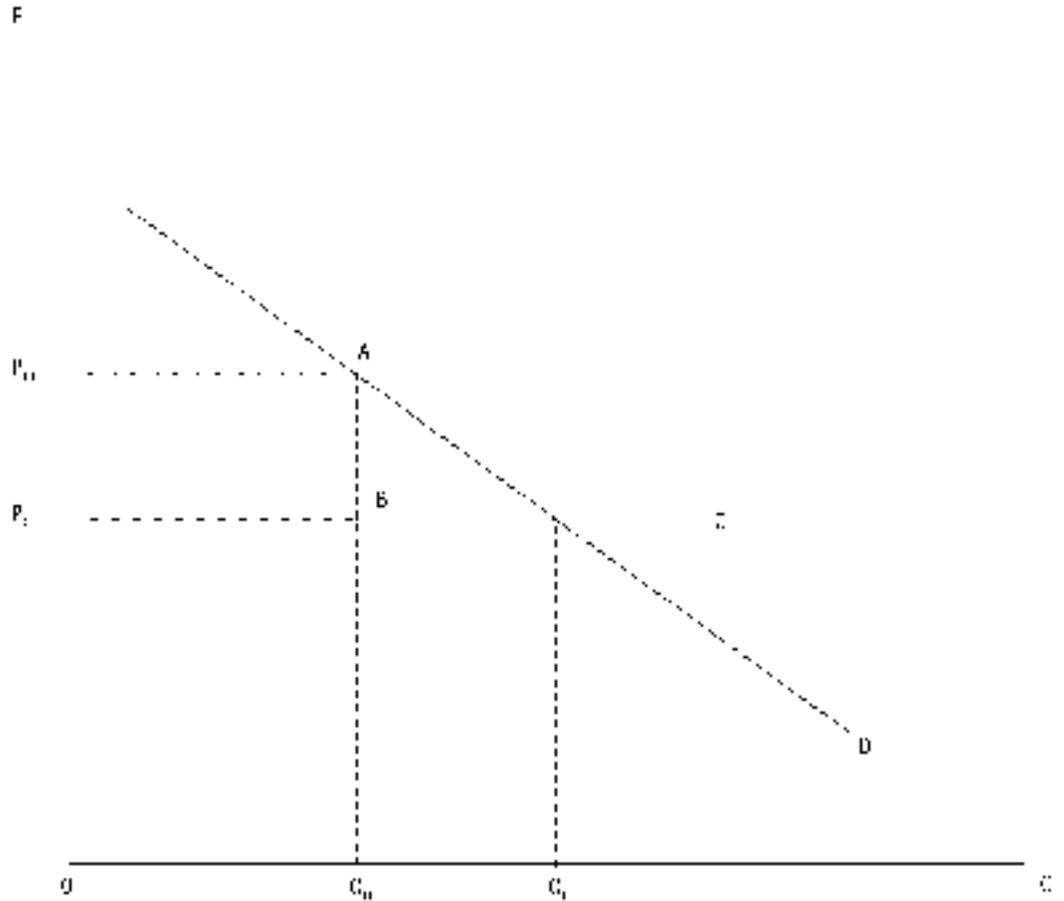
The process is straightforward, but is usefully illustrated by a standard economic diagram of a government-created (or -sustained) monopoly. In figure 4.2, the demand for some good or service—let it be milk—is shown by downward-sloping curve *D*. As price *P* (vertical axis) declines, the quantity *Q* (horizontal axis) of milk demanded increases. The per-unit cost of milk (including a competitive rate of return on investment) is a constant amount. In a competitive marketplace, the price (P_c) would equal cost (*C*), with Q_c milk being sold.

Assume now that government allows producers legally to collude to raise prices (or to limit quantities produced, which is the same thing). Milk producers will choose some higher price (P_m). The difference between this higher price and the competitive price, multiplied by the quantity sold at the higher price (Q_m), is rent to milk producers. Area $P_c P_m BA$ represents those rents.

Of course, these kinds of rents don't just happen inadvertently in Washington (or in state capitals or in city halls). Private interests and politicians intentionally make them happen. Knowing that gains are available if politicians can be persuaded, private interests will seek out politicians to create them (Tullock 1967, 1993). Politicians willing to create the milk cartel (or allow it to function unmolested by antitrust law) expect to be compensated for their services. Competition among private interests to be the favored firms or interests (so-called rent seeking) ensures that politicians will in fact be paid.

Legalized price-fixing of the sort illustrated in figure 4.2 has occurred frequently in this country. The Depression-era National Industrial Recovery Act (NIRA) mandated industry codes, which in turn had producers in a particular industry fix prices.⁹ More recently, trucking regulation under the Interstate Commerce Commission (ICC) and airline regulation by the Civil Aeronautics Board (CAB) likewise were just elaborate schemes of legal price-fixing.¹⁰ But legal price-fixing is only one way of creating political rents. Midwestern producers of ethanol seeking government-mandated inclusion of their product in gasoline, bar associations seeking state restrictions on entry to practice by new lawyers, farmers looking for crop subsidies or payments not

Figure 4.2 *Rent Creation*



to grow crops, and city contractors or union locals seeking “set-aside” legislation or closed-shop laws to favor themselves are all engaged in rent seeking. The means may differ, but the ends are the same: increased returns through success in the political, not economic, marketplace.

Rent seeking is the process that concerns those worried about money and access to the political process that money facilitates. Private interests pay to play the rent-seeking game, hoping to come away winners in the competition for political returns. The winners in the process are the notorious special interests; the losers are the little folks, consumers who pay the higher prices because of the politically created rents. The little folks have no PACs, contribute little or nothing to politicians, and so can expect to be excluded from the political game (Olson 1965).

Belief that this is the game being played in Washington (or Albany, or Sacramento) leads to a simple rule of thumb, based on a series of seemingly logical propositions. First, you have to pay to play: Politicians do not provide something for nothing. Second, those contributing to politicians are paying for special treatment, which must come at the expense of those who are not paying (or not paying enough)

to be real players in the game. Third, one can identify those getting special treatment by examining the extent to which they pay to play. Or so it seems.

By this view, the game is akin to a contract. Rent seekers pay politicians for political returns not available in the economic marketplace. Both sides are better off as a result, just as in the standard contract. And, as long as the contract is concluded within existing legal parameters, such as those specified in the federal campaign laws, the contract is perfectly legal.¹¹

But recognizing the political bargain forces realization as well that contract is not the only way that human beings interact. Much human interaction is not mutually sought, nor does it result in mutual advantage. Rather, it results from one party interfering with the rights of another. In their first year of law school, budding lawyers study not just contracts but torts. Some torts (traffic accidents) may be unintentional, but many, including crimes (theft, murder), are intentional. Both types of tort are distinguished, however, by the fact that while one party may be better off, the other is worse off.

In the rent-seeking game that private interests sometimes pay to play, both parties are made better off by the contract that ensues. But the question arises whether something analogous to torts sometimes occurs in political games, just as it does in life outside politics.

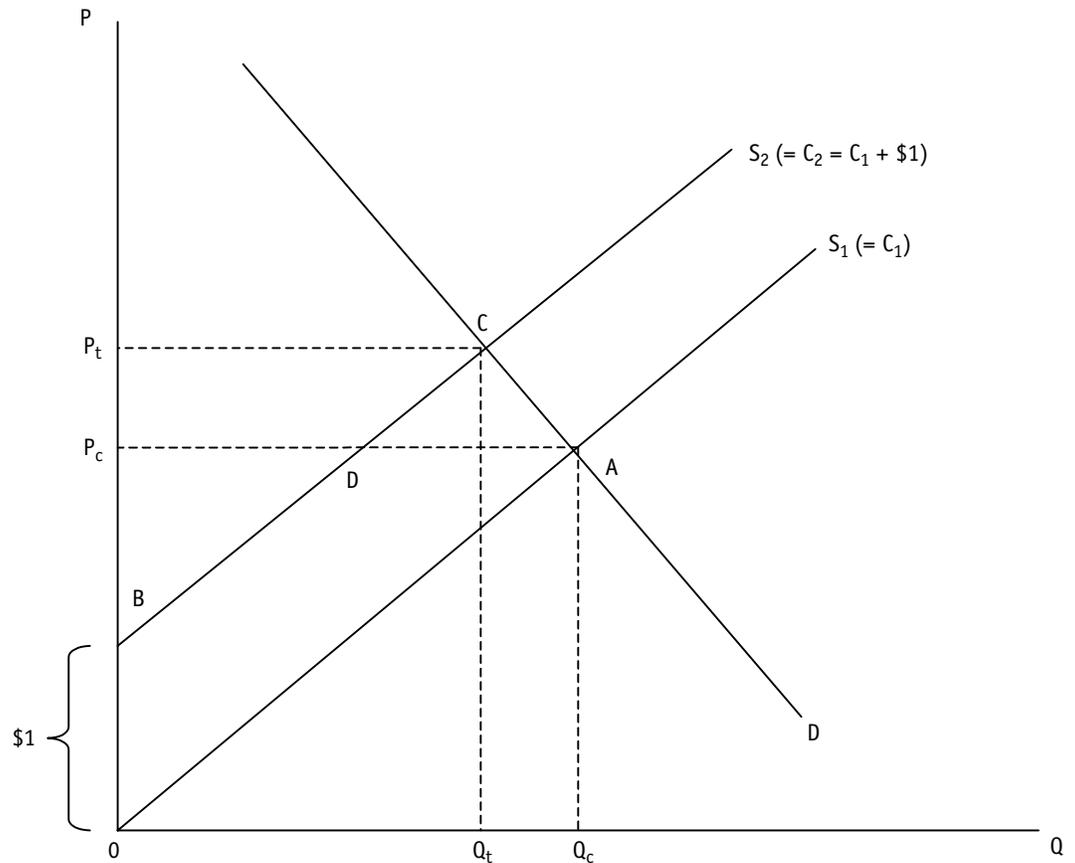
Rent Extraction and Pay to Play

Rent Extraction as Extortion

Consider figure 4.3, which portrays a different industry (say, beer) from that shown in figure 4.2. Figure 4.3 alters one aspect of figure 4.2. Now the industry supply curve (S_1) is upward sloping, reflecting marginal costs (C_1) that rise with quantities produced, rather than the constant costs portrayed in figure 4.2. As always, the competitive price (P_c) is determined by the intersection of supply and demand (D). Quantity (Q_c) will be sold at that price. Producers' total revenues are $0P_cAQ_c$, while total costs are only $0AQ_c$. Producers earn a return over cost of $0AP_c$, because at levels of production below Q_c , price exceeds cost of production. These returns, known in economics as quasi-rents, are not the result of political rent seeking.¹² Rather, they arise in competitive markets because of factors affecting costs of production at different levels of output.

Such returns are economically important. They are available to compensate producers' fixed-cost investments (e.g., plant, equipment, advertising) that by definition would not be compensated if revenues only equaled marginal costs of production. When firms cannot anticipate the revenue stream represented by the quasi-rent rectangle, beneficial fixed-cost investments will not be made.

Suppose, for example, that Congress contemplates imposing an excise tax of \$1 on a six-pack of beer. As figure 4.3 shows, the supply curve would shift from S_1 to S_2 , the difference at every level of output being the \$1 excise tax. Once taxed, beer will sell for price P_t , cutting quantity sold to Q_t . Of particular concern to brewers will be the loss of quasi-rents caused by the higher price and reduced quantity sold. Quasi-rents shrink from $0AP_c$ to BCP_t .

Figure 4.3 *Rent Extraction*

Faced with this threatened loss, producers will realize two things. First, they would be willing to pay up to the amount of the net revenues they will lose *not* to have the excise tax imposed. Second, the excise, if imposed, will be paid into the federal treasury. But if payments are made to senators and members of Congress *not* to impose the tax, those payments will go directly into the politicians’ own campaign treasuries—perhaps even into their own pockets.¹³ In many instances, both private interests and politicians are made better off if rent-extracting legislation is avoided by side payments from the would-be victims to the politician-victimizers. Either way, rents are extracted from private interests, whose concern is to minimize the extent of extraction.

Because they can gain by submitting legislation and then, for a price, withdrawing it (or allowing it to languish in committee), politicians routinely do so. In fact, among themselves they refer to such legislative proposals by names like “juice bills” (proposals intended to squeeze private interests for money), “milker bills” (proposals intended only to milk private producers for payments not to pursue the rent-extracting legislation), or “cash cows.” For example, by proposing product liability legislation annually, Washington politicians for years “have been feeding off the

contributions from political action committees,” so “product liability legislation will remain in legislative limbo—a cash cow with plenty of milk left.”¹⁴ Money has flowed from PACs on both sides of the issue, trial lawyers, and manufacturers. Ralph Nader observes, “The bill is a PAC annuity for members of Congress. It’s like rubbing the golden lamp.”¹⁵

Newsweek reports that legislation introduced only to menace and then extract rents is known in some locales as a “fetcher” bill, “introduced solely to draw—fetch—lavish treatment from lobbyists.”¹⁶ Reportedly, fetching is practiced often in Illinois. A study of the Illinois legislature noted legislators who “introduce some bills that are deliberately designed to shake down groups which oppose them and which pay to have them withdrawn.”¹⁷ Illinois legislators transplanted to Washington still practice the fetching art:

Rep. Jim Leach quietly introduced a bill a few days ago aimed at reducing speculation in financial futures. Barely 24 hours later, the Iowa Republican learned that Chicago commodity traders were gunning to kill his proposal. Rep. Leach said one Illinois lawmaker told him the bill was shaping up as a first-class “fetcher bill,” a term used in that state’s Legislature to describe a measure likely to “fetch” campaign contributions for its opponents. Sure enough, one of the first to defend the traders was Democratic Rep. Cardiss Collins of Illinois, recipient of \$24,500 from futures-industry political action committees. She called on colleagues in the Illinois delegation to beat back the Leach bill and watch out for similar legislation.¹⁸

Any number of other examples could be cited. President and Mrs. Clinton’s threats in 1993 to impose price controls on the health care industry—proposed but ultimately abandoned—resulted in a flood of private money not to legislate. The *New York Times* reported in late 1993,

As Congress prepares to debate drastic changes in the nation’s health care system, its members are receiving vast campaign contributions from the medical industry, an amount apparently unprecedented for a non-election year. While it remains unclear who would benefit and who would suffer under whatever health plan is ultimately adopted, it is apparent that the early winners are members of Congress.¹⁹

The evidence of rent extraction is not just anecdotal. Sophisticated statistical (including econometric) analyses of legislation proposed and then withdrawn find that the process is not a neutral one, even if ultimately no legislation passes.²⁰ In the process, private wealth is transferred to politicians.

To return to the principal theme here, the rent extraction game being played is hardly one in which private interests pay for special favors in the political marketplace. Rather, they pay to avoid even greater extraction by politicians of wealth earned in the ordinary economic marketplace. The process is akin to extortion, except that it is legal. Not surprisingly, the rent-extraction game is particularly practiced by legislators on the principal tax and business regulatory committees. As one member of the House observed, “The only reason it isn’t considered bribery is that Congress gets to define bribery.”²¹

Paying to play the rent-extraction game is hardly the same as paying for special favors. Confronted by an armed thug demanding “your money or your life,” a man handing over his wallet would hardly be thought to be buying a special favor. Or, to use the example of two Nobel laureates, bribes paid by Jews in Nazi Germany to prolong their lives can hardly be regarded as payment for special favors.²²

Rent Extraction and Incentives to Organize

From the foregoing, pay to play now is seen to involve two different sorts of games: payments for political favors and payments to avoid political disfavors. One cannot infer from the fact that payments are made that those notorious “special interests” are subverting democracy. Rather, private interests often pay politicians just to be left alone, to be allowed to produce goods and services in the way one would want companies to do. Industries like toiletries and cosmetics, which are unregulated and seek no particular political breaks, “pump hundreds of thousands of dollars to federal candidates,” and millions more in states where regulation is threatened.²³ Other industries likewise seek just to be left alone.

The nation’s largest banking company [Citicorp] employs eight registered lobbyists in its Washington office. In addition, six law firms represent Citicorp’s interests on Capitol Hill. No one should judge this strike force ineffective by how little banking legislation gets through: The lobbyists spend most of their time blocking and blunting changes that could hurt Citicorp’s extensive credit-card operations, student-loan business or ever-broadening financial-service offerings.²⁴

The fact that private firms and industries organize to pay not to have their wealth extracted points up alternative strategies available in the face of politicians’ actual or anticipated extraction demands. One means of protection from some politicians’ extraction demands is to induce others to pass legislation forbidding payments to avoid extraction. If the law forbids making payments to avoid extraction, goes the logic, then politicians will have no incentive to threaten private wealth in the first place. So, for example, Nelson Rockefeller thanked Congress on behalf of his family (with its important financial and management interests in industries like banking, insurance, and transportation) for laws that restrained the Rockefellers’ ability to make political contributions.²⁵ Banks have sought from the Federal Election Commission regulations making it illegal to lend to politicians.²⁶ Bond dealers have collectively agreed to discontinue the practice of making large contributions to political campaigns.²⁷

Potential victims of politicians’ extraction tactics have an alternative strategy, particularly when, individually, they have relatively little wealth to extract. Imagine a lump-sum tax that would cost each of 275 million Americans \$1 each. The amount of money at stake is considerable in politicians’ eyes. If those who would be subject to the tax paid as little as 25 percent of what they would lose (\$275 million), the payments to the members of the House and Senate who would consider the tax would amount to almost \$130,000 per politician.

But how would a politician collect that \$130,000? There is no national organization of American citizens—no citizen PAC—that could collect and pay over to politicians the 25 cents per head needed to buy off the tax. The very act of organiz-

ing and collecting 25 cents per capita would certainly exceed the amount at stake. (Consider the multimillion-dollar cost to the Census Bureau of contacting 275 million Americans and inducing them to respond.) Aside from the basic transaction-cost problem, considerable free-riding predictably would also arise: Let my neighbor pay 50 cents for both of us, since he'll still be better off than paying the \$1 tax. If everyone reasons that way, no one pays.

When there are large numbers of persons, each with relatively small amounts at stake from potential political extraction, politicians have no credible way to imperil the collective wealth at stake. The costs of picking up the payments not to take the wealth are too high. And recognizing this, dispersed interests have an incentive to stay dispersed (i.e., not to organize into PACs or any other sort of organization). Lack of organization represents a strategy of refusing to negotiate.

That a party susceptible to being forced to bargain over conceding some of his wealth might intentionally put himself in a no-negotiation stance is well understood generally. Schelling (1963, p. 26) discusses the use of communications difficulties as a way to maintain a no-bargaining position that will ultimately lead to concessions from the other side. A person who is incommunicado cannot be deterred from his own commitment to stay out of the game. Analogous tactics have been analyzed in other contexts, where it can also be useful to be unable to organize.²⁸

Lack of organization, in other words, is a way to avoid being made to pay. But it also means not being able to play. If one wants to play—to avoid having wealth and rents extracted—organization is necessary. But organization is undertaken with the realization that politicians' extraction demands will follow.

The National Rifle Association (NRA) furnishes an excellent example. Long-gun owners are numerous and highly dispersed. Political threats to regulate or ban guns arise annually, at both state and federal levels. Yet, for the most part, when the dust settles, no legislation has been passed.

But in the process, much money has been transferred via the NRA from gun owners to politicians. NRA contributions to politicians are reported regularly, often in large headlines. Without the NRA, these transfers would not be economically feasible. It is cheaper for politicians to negotiate with the NRA (which has already collected the contributions from its members) than it would be for them to deal with millions of gun owners atomistically. In other words, the very existence of the NRA guarantees that politicians will practice more rent extraction than would otherwise be the case.

This is not to say that the NRA is a bad idea. If it did not exist—if politicians did not see rent-extraction possibilities in proposing a gun ban—then guns might well be banned. The point is, rather, that organization has its costs. It may well fend off more draconian political threats. But it also creates a means for politicians to extract wealth more cheaply. And so, politicians are more likely to attempt to do so.

Rent Extraction and the Petty Tyranny of Government

As participants in the practice themselves acknowledge, the rent extraction that goes on routinely in government is just legalized extortion. Euphemisms like “juice bills”

and “fetchers” may be used to cover up what goes on, but extortion by any other name would smell as noxious. The implications of politicians’ rent-extraction strategy are numerous. One, the fact of organizing in order to “pay to play,” has just been discussed. One more point is relevant.

The possibilities for extracting wealth are particularly useful for understanding, or at least reducing to an explanation based on rational human behavior, the never-ending acts and enactments of government seemingly designed more to annoy and harass citizens than to advance any useful purpose. Criminalization of victimless acts is one example. If both buyers and sellers in contracts for things like drugs and prostitution are made better off, why are those contracts outlawed legislatively—not to mention made criminal? Outlawing victimless crime seems especially unjustified when the prohibitions themselves lead to crimes with real victims, of which murder over illicit drugs seems a particularly common example.

Viewed through the lens of rent extraction, criminalizing victimless acts is easily explained as a way for law enforcers to extract the wealth generated by private, welfare-enhancing transactions. Not only does the illegality of drugs increase taxpayer-provided budgets for police departments, but police now are allowed to keep the proceeds of assets forfeited as a result of drug enforcement actions, increasing their discretionary budgets. Not surprisingly, police have responded to their ability to practice extraction legally with greater numbers of drug-related arrests.²⁹

Budget increases do not measure the personal gains available to police from keeping victimless crimes criminal. Police shakedowns of drug dealers and prostitution rings for cash are so common they are not even newsworthy. Almost anything can be made illegal, then used as the basis for rent extraction. The transvestite “Miss All-America Camp Beauty Pageant” and similar drag beauty contests of the 1960s were illegal, but nonetheless renowned in the transvestite community nationally. How did something illegal still become so well known and popular?

The organizer was Jack Doroshow, also known as Sabrina, who held 46 contests a year from 1959 to 1967 through his company, the National Academy, which in its heyday had 100 employees on the payroll. Mainstream America didn’t know it, but the nation had a flourishing drag subculture, and not just in the major cities. . . . Since local laws often prohibited cross-dressing, Mr. Doroshow would meet with officials and propose a donation to some unspecified charity. In return, the town would pass a variance allowing the contest to take place.³⁰

Closely related to criminalizing victimless acts as a way for politicians to extract wealth is licensing things like gambling, racing, and so forth. The need for a license to do business legally opens the door for a politician to demand a cut of the take. The recent conviction of former governor Edwin Edwards for taking payments in exchange for Mississippi riverboat casino licenses is just the latest example; a generation ago, it was Governor Marvin Mandel and horse racing. But the political practice of making private interests pay just to practice their skills in the economic marketplace has been around for a long time. Adam Smith observed in *The Wealth of Nations*,

In order to erect a corporation, no other authority in ancient times was requisite in many parts of Europe, but that of the town corporate in which it was established. In England, indeed, a charter from the king was likewise necessary. But this prerogative of the crown seems to have been reserved rather for extorting money from the subject. . . . Upon paying a fine to the king, the charter seems generally to have been readily granted.

Conclusion

It is a mistake to view “pay for play” as a single game in which those seeking special favors (political rents) pay politicians for the goodies they want. That game goes on, obviously. But the political terrain in which pay for play prevails is like a city big enough to support two baseball teams. The amount of money involved in the games played in Washington, state capitals, and city halls is big enough to support two political teams. One is playing rent creation, the other is playing rent extraction.

In his book *The Law*, the French politician and philosopher Frederic Bastiat summarized the two games being played: “As long as it is admitted that the law may be diverted from its true purpose—that it may violate property instead of protecting it—then everyone will want to participate in making the law, either to protect himself against plunder or to use it for plunder.” Nobel-prize-winning economist George Stigler made the same point.³¹ Like love, paying to play is a many-splendored thing.

NOTES

1. Janie Bradford and Berry Gordy, Jr., *Money (That's What I Want)* (BMI). Barrett Strong made the song popular in 1960.
 2. Although the expression “pay to play” is now creeping into the political lexicon, the saying’s increasing popularity may create an erroneous impression, suggesting that only recently has money tantalized politicians. Any such belief would, of course, be foolish. Politicians have always been as interested in money as anyone else is—which is to say, a good deal.
 3. “The Federal Election Campaign Act of 1971 . . . fundamentally changed the federal campaign finance laws. . . . [It] provided the basic legislative framework for corporations and labor unions to establish separate segregated funds, popularly referred to as PACs (political action committees).” Federal Election Committee Twenty Year Report, pp. 1–2 (www.fec.gov/pages/ch1.htm). Following Watergate, the act was amended to limit both contributions to candidates and expenditures by candidates. The latter sorts of restrictions were largely invalidated in *Buckley v. Valeo*, 424 U.S. 1 (1976), which also generally upheld the constitutionality of the former forms of restrictions.
 4. Figures are reported for two-year election cycles.
 5. The 82 percent figure for 1995–96 comes from a Federal Election Commission press release, “PAC Activity Increases in 1995–96 Election Cycle,” April 22, 1997. At least two caveats are in order. First, with six-year Senate terms, not all 535 seats are contested every two years. Second, there is considerable variance in the amounts that PACs pay individual politicians (senators and members of Congress), meaning that averages may not be as relevant as would otherwise be the case.
 6. Common Cause.
 7. *Ibid.*
-

8. Economists' use of the technical economic term "rent" for politically derived returns is unfortunate. Not only does that definition have nothing to do with the everyday meaning of the term, but economists also use it in different ways, not always consistently (Alchian 1987).
 9. For a good summary of the NIRA experience, see Bittlingmayer (1995).
 10. The fact that, in all these examples, price-fixing was legal actually is less important than the fact that it was legally *required*. Cartels are highly unstable and, even if legal, tend to collapse into competition. The NIRA, ICC, and CAB all required producers in the industry to work within the cartel and imposed penalties on those who did not.
 11. There are certain differences between contracts for exchange in the political market and those for exchange in economic markets. Economic contracts typically do not have third-party losers, the way consumers (in the example illustrated by figure 4.2) lose from the contract between rent seekers and politicians. And political contracts might better be described as "extralegal" in that, if breached by a politician refusing to provide the promised services, they cannot be enforced or yield a damage award judicially. Thus, parties to political contracts must and do find various mechanisms to ensure performance (McChesney 1997, ch. 5).
 12. Again, the economist must apologize for use of infelicitous terminology. See note 8.
 13. The rules concerning politicians' expenditures from campaign funds for seemingly personal reasons are remarkably fluid. Writing in 1994, one source reported, "In the 15 years that the personal-use prohibition has been on the books, the FEC has never punished anyone for violating it, and the broad power over how campaign money is used has remained one of lawmakers' most prized perks." See Wartzman 1994. Politicians have successfully justified as campaign rather than personal expenditures such things as country club dues, Kentucky Derby tickets, cars, football tickets, liquor, insurance for art works, trips abroad, tax-sheltered investments, bronze figurines for investment, and golf clubs. Campaign money has been used to defend against lawsuits alleging drunken driving, sexual harassment, and, ironically, financial transgressions. And campaign funds have been used for deceased politicians' funeral, cremation, and burial expenses. See McChesney (1997, pp. 49–50).
 14. Abramson 1990.
 15. Ibid.
 16. *Newsweek*, 1989, p. 6.
 17. Aranson 1981, p. 253.
 18. Jackson and Ingersoll 1987, p. 64.
 19. Lewis 1993, p. A1.
 20. See Beck, Hoskins, and Connolly 1992; McChesney 1997.
 21. Maraniss 1983, p. A1.
 22. Becker and Stigler 1974.
 23. Kaplan 1990, p. 1.
 24. Bacon 1993, p. A18. The article details how most of Citicorp's lobbying is aimed at getting politicians' permission to compete in various markets, not at obtaining special favors in markets where it already competes.
 25. Aranson and Hinich 1979.
 26. Langley and Jackson 1986.
 27. Fuerbringer 1993.
 28. See, for example, Schwartz 1988. "[N]umerous passive shareholders could do better when facing prospective buys than single owners of the same assets would do. An intuitive example of this result exists: Everyone knows that in some negotiations the ability to sit sphinxlike and let the other person make a series of proposals can yield useful information about the other person's views."
 29. Benson and Rasmussen 1997.
-

30. Grimes 1993, p. 13.
31. “The state—the machinery and power of the state—is a potential resource or threat to every industry in the society. With its power to prohibit or compel, to take or give money, the state can and does selectively help or hurt a vast number. . . . Regulation may be actively sought by an industry, or it may be thrust upon it” (Stigler 1971, p. 3).

REFERENCES

- Abramson, Jill. 1990. “Product-Liability Bill Provides Opportunity for Long-Term Milking of PACs by Congress.” *Wall Street Journal*, June 21, p. A16.
- Alchian, Armen A. 1987. “Rent.” In *The New Palgrave Dictionary of Economics*, vol. 4. New York: Stockton Press, p. 41.
- Aranson, Peter. 1981. *American Government: Strategy and Choice*. Cambridge, Mass.: Winthrop Publishers, p. 253.
- Aranson, Peter H., and Melvin H. Hinich. 1979. “Some Aspects of the Political Economy of Election Campaign Contribution Laws.” *Public Choice* 34 (4): 435.
- Bacon, Kenneth. 1993. “For Citicorp, Which Has Largest Lobbying Force in Banking Industry, Victories Are Won Quietly.” *Wall Street Journal*, Dec. 14, p. A18.
- Beck, Roger, Colin Hoskins, and J. Martin Connolly. 1992. “Rent Extraction through Political Extortion: An Empirical Examination.” *Journal of Legal Studies* 21 (January): 217.
- Becker, Gary, and George J. Stigler. 1974. “Law Enforcement, Malfeasance, and Compensation of Enforcers.” *Journal of Legal Studies* 3: 1, 6.
- Benson, Bruce L., and David W. Rasmussen. 1997. “Predatory Public Finance and the Origins of the War on Drugs: 1984–1989.” In *Taxing Choice: The Predatory Politics of Fiscal Discrimination*, edited by William F. Shughart II. New Brunswick, N.J.: Transaction Publishers.
- Bittlingmayer, George. 1995. “Output and Prices When Antitrust Is Suspended.” In *The Causes and Consequences of Antitrust: The Public Perspective*, edited by Fred S. McChesney and William F. Shughart II. Chicago: University of Chicago Press.
- “Buzzwords.” 1989. *Newsweek*, Nov. 20, p. 6.
- Common Cause. 2000. “A Message from Scott Harshbarger.” Press release, May 7 (www.commoncause.org/pressroom/).
- Fuerbinger, Jonathan. 1993. “17 Big Underwriters Bar Campaign Gifts Aimed at Bond Sales.” *New York Times*, Oct. 19, p. A1.
- Grimes, William. 1993. “‘The Queen’ on the Runway Again.” *New York Times*, March 27, section 1, p. 13.
- Jackson, Brooks, and Bruce Ingersoll. 1987. “Chicago Futures Industry, to Fend Off Attack, Rallies Lawmakers Who Received PAC Funds.” *Wall Street Journal*, Nov. 12, p. 64.
- Kaplan, Sheila. 1990. “How Cosmetics Lobby Maintains Its Luster: Even Distant Threat of Regulation Spawns Industry Scrambling.” *Legal Times*, April 30, p. 1.
- Langley, Monica, and Brooks Jackson. 1986. “Bankers Want Election Commission to Tighten Restrictions on Lending to Political Candidates.” *Wall Street Journal*, Sept. 23, p. 64.
- Lewis, Neil A. 1993. “Medical Industry Showers Congress with Lobby Money.” *New York Times*, Dec. 12, p. A1.
- Maraniss, David. 1983. “PAC Heaven: Commerce Committee Members Roll Up Corporate Contributions.” *Washington Post*, Aug. 21, p. A1.
- McChesney, Fred S. 1987. “Rent Extraction and Rent Creation in the Economic Theory of Regulation.” *Journal of Legal Studies* 16 (January): 101.
- . 1997. *Money for Nothing: Politicians, Rent Extraction and Political Extortion*. Cambridge, Mass.: Harvard University Press.
- Olson, Mancur. 1965. *The Logic of Collective Action: Public Goods and the Theory of Groups*. Cambridge, Mass.: Harvard University Press.
- Sabato, Larry J. 1984. *PAC Power: Inside the World of Political Action Committees*. New York: W.W. Norton.

- Schelling, Thomas C. 1963. *The Strategy of Conflict*. New York: Oxford University Press.
- Schwartz, Alan. 1988. "The Fairness of Tender Offer Prices in Utilitarian Theory." *Journal of Legal Studies* 17 (January): 165, 173.
- Stigler, George J. 1971. "The Theory of Economic Regulation." *Bell Journal of Economics and Management Science* 2 (Spring): 3.
- Tullock, Gordon. 1967. "The Welfare Costs of Tariffs, Monopoly, and Theft." *Western Economic Journal* 5 (April): 224.
- . 1993. *Rent Seeking*. Aldershot, U.K.: Edward Elgar.
- Wartzman, Rick. 1994. "Defending Football and Fancy Cars, Politicians Decry Effort to Limit Use of Campaign Money." *Wall Street Journal*, Jan. 12, p. A12.
-

Appendixes: Additional Discussions

SEMINAR 1

Nonprofit Advocacy: Practices and Perspectives

Advocacy is a broad concept that encompasses many activities ranging from education to lobbying to support for particular candidacies. Seminar 1 looked at the diverse meanings of the concept of advocacy through the experiences of five diverse nonprofit organizations: the YMCA of the United States, the Concord Coalition, the Advocacy Institute, the American Society of Association Executives (ASAE), and the AFL-CIO.

Several of the representatives of those organizations discussed the relationship between lobbying policymakers and organizing members. Several speakers addressed the importance of having a foundation of support in the population and of making policymakers aware of this broad support. One theme was the desirability of entering coalitions with membership organizations if an organization did not itself have members.

Questions of building capacity for advocacy were discussed. Several speakers addressed the concern that grassroots organizations lacked information about the permissible scope for lobbying and, as a result, avoided becoming involved in advocacy activities that are clearly allowed under current law. Several speakers expressed concern that foundation officers did not understand the permissible scope for advocacy and thus included language in grant agreements that unduly and unnecessarily restricted advocacy activities.

Several speakers addressed questions of organizational accountability and representativeness. Often, organizations that have members do not have mechanisms for consulting with them on advocacy positions and strategies. Participants discussed various elements of governance that might make member or supporter input more practical.

Some participants thought that the topic should address power more directly and urged organizations to understand or acknowledge that advocacy was about power. Several speakers called for even greater efforts to bring multidisciplinary perspectives to bear on these questions.

SEMINAR 2

Regulating Nonprofit Advocacy: Rules, Rationales, and Practices

Nonprofit organizations pursue their advocacy activities in an environment regulated by both tax law and election law. Although such regulation occurs at both the state and federal levels, this session focused on federal law. The meaning of either of these statutes and their accompanying regulations is often open to question, and the relationships between these two bodies of law can create unanticipated barriers or opportunities. This is an area of daunting complexity, but anyone interested in practice, policy, research, or theory ignores this area at their peril.

Although this seminar examined several concepts under tax law and election law, it did not claim to provide a comprehensive consideration of all of the relevant issues under either statute or of the issues arising from the intersection of the two statutes. The subsidy theory's role as a rationale for regulating nonprofit advocacy was questioned on both analytical and normative grounds. The conversation focused primarily on the current discussion over broadening the disclosure requirements relating to lobbying activities. Participants in the roundtable discussion questioned both the need for further disclosure and the effectiveness of disclosure as a method of enhancing accountability of nonprofit organizations.

The emergence of the so-called "new" Section 527 organizations was the focal point of the discussion. Several speakers and participants suggested that the new Section 527 organizations required a fundamental reconsideration of both tax law and election law. The participants generally agreed that the new Section 527 organizations are operating within the technical requirements of current law, but there was a broad discussion about the consequences of their roles. There was agreement that tax law provided for entity-level exemption from taxation and that the new Section 527 organizations were not subject to contribution limitations or the reporting and disclosure requirements of election law. Several participants asserted that the possibility of avoiding any disclosure under either tax law or election law was the primary factor accounting for the emergence of the new Section 527 organizations. Some participants saw no issues arising from the absence of disclosure, while others thought that these new Section 527 organizations should be subject to some form of disclosure. Some speakers and participants expressed concern that the new Section 527 organizations might displace Section 501(c)(4) organizations and perhaps even issue advocacy by Section 501(c)(3) organizations.

The participants of the roundtable took the view that the new Section 527 organizations would play a significant role in the 2000 election, but there was no consensus on that role or its consequences. Future seminars will address these consequences, as more information becomes available.

SEMINAR 3

Politicians, Parties, and Access in the Policy Process

Nonprofit advocacy takes place in contexts defined by other actors. Successful advocacy, particularly legislative and executive agency lobbying, requires access to decisionmakers and decisionmaking processes. How do the structures and processes of government shape nonprofit advocacy strategies? Do effective lobbying activities depend on supporting candidates who share an organization's policy positions? This seminar explored the concept of rent-seeking by officeholders and asked whether nonprofit organizations can gain the access needed for effective lobbying in a pay-to-play system. It also explored relationships between nonprofit organizations and political parties.

Several themes were echoed in the roundtable discussions. Some politicians hold sway over groups by using the threat or promise of action to induce money and services from organizations, yet many politicians are also earnest in their lawmaking responsibilities. Groups must contend with politicians who make their need for political capital clear, and must make decisions about the level of donations necessary to achieving their policy goals. Discussants considered the tradeoffs and consequences of policy participation in a pay-to-play political system, and most agreed that the lack of information on the source and flow of political dollars makes it difficult to determine the extent to which money shapes political motives and influences policy outcomes.

Several questions framed the discussion on the relationships between nonprofit organizations and political parties: Have political observers too hastily heralded the obsolescence of political parties? Or have parties cleverly adapted to the new candidate-centered and money-driven politics of the current elections? How has the relationship of nonprofit organizations and political parties evolved in the current election environment? How do the new practices affect democratic participation and nonprofit organizations?

Elizabeth Reid, a research associate at the Urban Institute's Center on Nonprofits and Philanthropy, captured this particular session's broader implications for the nonprofit sector, including the following issues related to citizen involvement in the political process:

- Political organizations—that is, the campaigns, parties, political action committees (PACs), and interest groups organized as exempt organizations—are vehicles for the acquisition, accumulation, and use of resources in elections. The organizations' election practices and the election laws regulating their activities shape our version of democracy: who takes part, with what resources and intensity, and, presumably, whose interests will be reflected in election outcomes and carried into the policy process.
- History can offer voters hope that popular politics, political parties, and organizations have a future together. In American democracy, social and political movements, pockets of intense activism, and even political outsiders and third parties have made issues public, built and transformed organizations, and stimulated public engagement.

- Some citizen-based organizations, including religious groups, unions, grass-roots community organizations, and public interest organizations of various stripes, can alter the participation ledger if they link their constituents to political activity, such as voting, communicating with elected officials, and becoming active in party caucuses, primaries, and conventions.
 - Nonprofits can develop better political communication with their constituents and build bridges with other like-minded groups for policy and electoral consensus, as well as examine their legitimacy with the broader public.
-

List of Seminar Attendees

Alan Abramson
The Aspen Institute
Nonprofit Sector Research Fund

Paul Accettura
Internal Revenue Service

Sean Aday
Annenberg Public Policy Center

Audrey Alvarado
National Council of Nonprofit Associations

Greg Anrig
Century Foundation

Steven Arkin
Internal Revenue Service

Nan Aron
Alliance for Justice

David Arons
Charity Lobbying in the Public Interest

Jan Baran
Wiley, Rein & Fielding

Jason Beal
Center for the Study of Elections and Democracy

Robert Biebel
Price Waterhouse Cooper

Robert Boisture
Caplin and Drysdale, Chartered

Elizabeth Boris
The Urban Institute

Evelyn Brody
Chicago-Kent College of Law

John Buckstead
National Association of Community Action Agencies

Maureen Burke
Advocacy Institute

Emmett Carson
The Minneapolis Foundation

Matt Carter
OMB Watch

Milton Cerny
Caplin and Drysdale, Chartered

Laura Chisholm
Case Western Reserve University
School of Law

Jim Clark
ASAE

Michael Cortes
University of San Francisco

Carmen Delgado Votaw
Alliance for Children and Families

Joanne Derwin
Georgetown University

Alan Dye
Webster, Chamberlain & Bean

Bob Edwards
East Carolina University
Department of Sociology

Rob Engler
Democratic National Committee

Rosemary E. Fei
Silk, Adler & Colvin

Janne Gallagher
Council on Foundations

Miriam Galston
George Washington University
National Law Center

Richard Grafmeyer
Joint Committee on Taxation

Kenneth Gross
Skadden, Arps, Slate, Meagher & Flom, LLP

Eden Fisher Durbin
YMCA of USA

Michael Foley
Catholic University of America

Deirdre Halloran
U.S. Catholic Conference

Matt Hamill
Independent Sector

Bristow Hardin
The Union Institute
Center for Public Policy

Gail Harmon
Harmon, Curran & Spielberg

Paul Herrnson
University of Maryland
Department of Government and Politics

Frances R. Hill
University of Miami
School of Law

Marianne Holt
Center for Public Integrity

Ron Jackson
D.C. Catholic Conference

Judith Kindell
Internal Revenue Service

Charles Kolb
Committee for Economic Development

Jeff Krehely
The Urban Institute

- Frances Kunreuther
Harvard University
Hauser Center for Nonprofit Organizations
- William J. Lehrfeld
Attorney at Law
- Harold Leibovitz
The Urban Institute
- Leslie Lenkowsky
Indiana University
Center on Philanthropy
- Spence Limbocker
Neighborhood Funders Group
- David Magleby
Brigham Young University
Political Science Department
- Michael Malbin
Campaign Finance Institute
- David Mason
Federal Election Commission
- Fred McChesney
Northwestern University
School of Law
- Debra Minkoff
University of Washington
- Maria Montilla
The Urban Institute
- Melissa Mueller
Rep. Lloyd Doggett
U.S. House of Representatives
- Norman Ornstein
American Enterprise Institute
- Marcus Owens
Caplin & Drysdale, Chartered
- Michael Petro
Committee for Economic Development
- John Pomeranz
Alliance for Justice
- Roni Posner
Alliance for Nonprofit Management
- Trevor Potter
Wiley, Rein & Fielding
- Elizabeth Reid
The Urban Institute
- John Reilly
Internal Revenue Service
- Jim Riker
The Union Institute
- Mark Rosenman
The Union Institute
- Seth Row
Federal Election Commission
- Lauri Rubenstein
U.S. Senate
Committee on Governmental Affairs
- Judith Saidel
State University of New York at Albany
Center for Women in Government
- Jocelyn Sargent
City University of New York (CUNY)
Howard Samuels State Management and Policy Center
- Holly Schadler
Perkins Coie LLP
- Howard Schoenfeld
Price Waterhouse Cooper
- Ron Shaiko
American University
Department of Government
- Peter Shiras
Independent Sector
- Lorie Slass
Annenberg Public Policy Center
- Robert Smucker
Charity Lobbying in Public Interest
- Nicholas Stengel
The Urban Institute
- C. Eugene Steuerle
The Urban Institute
- Thomas Stratman
George Mason University
Center for the Study of Public Choice
- Lisa Sullivan
LISTEN, Inc.
- Scott Thomas
Federal Election Commission
- Joseph Urban
Internal Revenue Service
- Elizabeth Van Benschoten
National Civic League
- Jennifer Wafford
AFL-CIO Organizing Department
- Fred Wertheimer
Democracy 21
- Louise Wides
Federal Election Commission
- Margaret Wyszomirski
Ohio State University
- Barnaby Zall
Law Offices of Barnaby Zall
-

About the Editor

Elizabeth J. Reid, of the Urban Institute's Center on Nonprofits and Philanthropy, conducts research on nonprofit advocacy. Ms. Reid has 20 years' experience in working with labor and community organizations, grassroots political education, leadership training, and involvement in civic and political affairs. She contributed a chapter on nonprofit advocacy and political participation to *Nonprofits and Government: Collaboration and Conflict* (Urban Institute Press, 1999). She served as national political director for the American Federation of Government Employees throughout the 1980s and taught courses in society and politics at the Corcoran School of Art in Washington, D.C., during the 1990s.

About the Contributors

Rosemary E. Fei is a principal at the law firm of Silk, Adler & Colvin, San Francisco. Her firm represents nonprofit and tax-exempt organizations exclusively, and her practice spans the full range of nonprofit and tax-exempt legal issues, with emphasis on political advocacy issues and nonprofit corporate governance. She is the chair of the Board of Redefining Progress; a member of Asian Americans/Pacific Islanders in Philanthropy and the Exempt Organizations Committee, Tax Law Section, American Bar Association; and a former director of CompassPoint Nonprofit Services and the Marine Mammal Center.

Paul S. Herrnson has served as an American Political Science Association Congressional Fellow and has received several teaching awards. He teaches in the government and politics department at the University of Maryland. He has written or edited several publications, including *Congressional Elections: Campaigning at Home and in Washington* (Congressional Quarterly Books, 2000), *After the Revolution: PACs, Lobbies, and the New Republican Congress* (Addison-Wesley, 1999), and *The Interest Group Connection: Electioneering, Lobbying, and Policymaking in Washington* (Chatham House, 1997).

Fred S. McChesney is professor of law at Northwestern University. His primary scholarly teaching interests are in the area of business and antitrust law and their intersection with economic theory. Before teaching, he worked as an associate director for policy and evaluation at the Federal Trade Commission. He has written or edited several publications, including *Money for Nothing: Politicians, Rent Extraction and Political Extortion* (Harvard University Press, 1997), *Causes and Consequences of Antitrust: The Public Choice Perspective* (University of Chicago Press, 1995), and *Economic Inputs, Legal Outputs: The Role of Economists in Modern Antitrust* (John Wiley and Sons, 1998).

About the Cohosts

Evelyn Brody is an associate professor of law at the Chicago-Kent College of Law, Illinois Institute of Technology, where she teaches tax courses. She is also an associate scholar of the Urban Institute, working on projects with its Center on Nonprofits and Philanthropy. Professor Brody writes and lectures on a variety of legal, economic, and social issues affecting individuals, businesses, and nonprofit organizations. In 1994, she served on the Clinton/Gore Transition Team (Treasury/Tax Policy Cluster), and in 1992 she taught a course on the tax treatment of financial products for the Taiwan Ministry of Finance. Previously, Professor Brody practiced with Arnold & Porter in Washington, D.C., and with Michael, Best & Friedrich in Madison, Wisconsin.

Frances Hill has written extensively on the role of nonprofit organizations in electoral campaigns. She has testified before Congress on legislation to require disclosure by certain Section 527 organizations that are not subject to Federal Election Commission reporting. She is active in the American Bar Association Section of Taxation's Committee on Exempt Organizations and is a member of the American Law Institute. Professor Hill frequently speaks on issues relating to tax-exempt organizations. She is a professor at the University of Miami School of Law, where she teaches courses in taxation, bankruptcy, and commercial law.

About the Center on Nonprofits and Philanthropy

The Urban Institute's Center on Nonprofits and Philanthropy (CNP) explores the role and impact of nonprofit organizations and philanthropy in democratic societies. By deepening the understanding of the multiple roles that nonprofits play—as service providers and as avenues of civic participation and public voice—CNP research endeavors to address the relationships among nonprofits, government, and the market from a variety of perspectives.

The Center strives to build the necessary research tools, contribute to sensible theory, and develop applications that illuminate both policy and practice in the nonprofit sector. CNP's research projects combine qualitative and quantitative data, the theoretical framework of civil society, and practical public policy considerations.

A major component of the Center is the National Center for Charitable Statistics (NCCS), which serves as the national repository of statistical information on the nonprofit sector from the Internal Revenue Service (IRS) and other sources. NCCS's mission is to build compatible national, state, and regional databases and to develop uniform standards for reporting on the activities of charitable organizations. These data enable researchers to develop a comprehensive picture of nonprofit-sector trends as well as in-depth analyses of financial data.

Together with the IRS and Philanthropic Research, Inc. (PRI), NCCS provides scanned images of IRS Form 990, the financial information report that tax-exempt nonprofit organizations file with the IRS. Information from the scanned images is being digitized to create the most comprehensive and highest-quality database ever available on nonprofit organizations. For information visit our Web site, <http://www.urban.org/centers/cnp.html>.

Dissemination of CNP research findings includes use of electronic publications on the Internet as well as policy briefs, working papers, and monographs. In addition to the *Nonprofit Advocacy and the Policy Process Seminar Series*, CNP holds regular seminars, discussion groups, and conferences to discuss research findings and topics of current interest to the field.

Elizabeth T. Boris is the first director of the Center on Nonprofits and Philanthropy at the Urban Institute and was the founding director of the Nonprofit Sector Research Fund at the Aspen Institute, where she worked from 1991 to 1996. Prior to 1991, she was vice president for research at the Council on Foundations, where she developed and directed the research program for 12 years. The author of many research publications and articles on philanthropy, including *Philanthropic Foundations in the United States: An Introduction*, Dr. Boris is also coeditor with Eugene Steuerle of *Nonprofits and Government: Collaboration and Conflict* (Urban Institute Press, 1999). She is active as a board member and advisor to many nonprofits and is also Insights editor for *Nonprofit and Voluntary Sector Quarterly*.



The Urban
Institute

2100 M Street, N.W.
Washington, D.C. 20037

Phone: 202.833.7200

Fax: 202.429.0687

E-Mail: paffairs@ui.urban.org

<http://www.urban.org>

Research Reports