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# Foreign Corruption of the Political Process Through Social Welfare Organizations

Norman I. Silber

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## FOREIGN CORRUPTION OF THE POLITICAL PROCESS THROUGH SOCIAL WELFARE ORGANIZATIONS

*Norman I. Silber*

**ABSTRACT**—Social welfare organizations are prohibited from channeling foreign contributions to favored political candidates. Prospects for enforcing this prohibition, however, are uncertain. Do federal election laws or tax laws provide effective tools? Are state authorities equipped to hold a nonprofit culpable as an entity, or to hold a manager or board member responsible? These questions are important to understand whether the existing rules safeguard the nonprofit community and the fairness of elections. This Essay concludes that federal tax and election rules are likely to be less effective than the authority vested with state attorneys general to monitor and hold accountable nonprofits and their officers and directors who become vehicles for foreign interference in national elections.

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## INTRODUCTION

Concern has mounted in recent decades about dark, publicly unattributed money contributed to political campaigns by extremely wealthy Americans, corporations, and unions. Frequently, dark money is lawfully transferred to candidates for office without public attribution of any source, through nonprofit conduits.<sup>1</sup> A body of literature addresses the wisdom of allowing nonprofits to facilitate dark money contributions, and there are good reasons to be concerned.<sup>2</sup> “In general, elected officials are warranted in

<sup>1</sup> See Trevor Potter & Bryson B. Morgan, *The History of Undisclosed Spending in U.S. Elections & How 2012 Became the “Dark Money” Election*, 27 NOTRE DAME J.L. ETHICS & PUB. POL’Y 383, 384–85 (2013) (explaining that dark money refers to when the sources of funds used to make election spending expenditures are not disclosed to the public).

<sup>2</sup> See LAWRENCE LESSIG, *REPUBLIC, LOST: HOW MONEY CORRUPTS CONGRESS—AND A PLAN TO STOP IT* 252–59 (2012) (discussing transparency in campaign contributions); Lloyd Hitoshi Mayer, *Disclosures About Disclosure*, 44 IND. L. REV. 255, 281–82 (2010) (proposing an increase in disclosure of information about substantial contributors); Michael R. Siebecker, *Political Insider Trading*, 85 FORDHAM L. REV. 2717, 2725 (2017) (“[T]o the extent corporations remain free to skulk about the political arena injecting dark money into campaigns under a cloak of anonymity, the electorate cannot effectively assess whether politicians remain in the pocket of corporate interests and shareholders cannot determine whether corporate managers use the corporate treasury to advance personal political interests.”); Linda Sugin, *Politics, Disclosure, and State Law Solutions for 501(c)(4) Organizations*, 91 CHI.-KENT L. REV. 895, 897 (2016) (“Dark money may be *solely* an election law problem . . . . However, if there are concerns about nonprofit organizations in politics that implicate the policies relating to nonprofits, there might be something beyond election law at issue that state nonprofit law might address.”); *New York Times* Editorial Board, Editorial, *The I.R.S. Gives Up on ‘Dark Money’*, N.Y. TIMES (July 25, 2015), <https://www.nytimes.com/2015/07/26/opinion/sunday/the-irs-gives-up-on-dark-money.html> [<https://perma.cc/737Z-WYEC>]. See generally JANE MAYER, *DARK MONEY: THE HIDDEN HISTORY OF THE BILLIONAIRES BEHIND THE RISE OF THE RADICAL RIGHT* 247–53 (2016) (explaining the role of dark money in the 2010 U.S. midterm elections); Ellen P. Aprill, *The Section 527 Obstacle to*

raising and spending as much money as possible,” because the “shorthand for political success—more money, more votes” has been generally validated,<sup>3</sup> as has the supposition that large campaign donors often get preferential treatment from the elected officials they support.<sup>4</sup>

The discussion which follows is a part of the dark money discussion, but it is not about eliminating *legal* dark donations to nonprofit conduits. It is about nonprofits that may handle *illegal* dark donations made principally by sending unlawful foreign contributions to favored candidates through 501(c)(4) nonprofits. While it is true that dark money given by U.S. citizens can unduly affect the outcome of political campaigns, the perils intrinsic to allowing foreign countries, foreign nationals, and foreign corporations to influence the U.S. electoral process are different and greater than the dangers posed by such legal dark money.<sup>5</sup>

This Essay addresses how to hold nonprofits and culpable officers, directors, and staff accountable for contributing dark money under federal and state law, and discusses the shortcomings with current approaches. Part I examines the incidence of unlawful foreign interference in political elections through the use of nonprofit conduits. Part II considers the implications of a federal law violation under Federal Election Law, criminal statutes, and the IRS. Part III addresses state law violations, along with the power of the state attorney general. Part IV addresses the overlay between state and federal authority. Finally, this Essay concludes that federal tax and

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*Meaningful Section 501(c)(4) Regulation*, 13 PITT. TAX REV. 43, 47 (2015) (highlighting intrinsic difficulties of regulating dark money through the Internal Revenue Code).

<sup>3</sup> Philip Bump, *Does More Campaign Money Actually Buy More Votes: An Investigation*, ATLANTIC (Nov. 11, 2013), <https://www.theatlantic.com/politics/archive/2013/11/does-more-campaign-money-actually-buy-more-votes-investigation/355154/> [https://perma.cc/CRV7-VB3U].

<sup>4</sup> See Tara Siegel Bernard, *A Citizen's Guide to Buying Political Access*, N.Y. TIMES (Nov. 18, 2014), <https://www.nytimes.com/2014/11/19/your-money/a-citizens-guide-to-buying-political-access-.html> [https://perma.cc/NG7Q-Z262]. The article reports on a study that discovered a positive correlation between campaign donations and access to politicians. See Joshua L. Kalla & David E. Broockman, *Campaign Contributions Facilitate Access to Congressional Officials: A Randomized Field Experiment*, 60 AM. J. POL. SCI. 545 (2016).

<sup>5</sup> Zephyr Teachout, *The Anti-Corruption Principle*, 94 CORNELL L. REV. 341, 352 (2009) (explaining that the Framers were particularly concerned with foreign corruption); Matt A. Vega, *The First Amendment Lost in Translation: Preventing Foreign Influence in U.S. Elections After Citizens United v. FEC*, 44 LOY. L.A. L. REV. 951, 959 (2011) (justifying statutory prohibitions on foreign contributions notwithstanding *Citizens United v. FEC*); Sean J. Wright, *Reexamining Criminal Prosecutions Under the Foreign Nationals Ban*, 32 NOTRE DAME J.L. ETHICS & PUB POL'Y 563, 584–86 (2018) (arguing for an urgent need to strengthen the ban on contributions from foreign nationals); Zachary J. Piaker, Note, *Can “Love” Be A Crime? The Scope of the Foreign National Spending Ban in Campaign Finance Law*, 118 COLUM. L. REV. 1857, 1857 (2018) (exploring whether intangibles, such as information about a political opponent, fall within the ban); see also Anna Su, *Speech Beyond Borders: Extraterritoriality and the First Amendment*, 67 VAND. L. REV. 1373, 1378 (2014) (excluding foreign campaign contributions from argument for extending extraterritoriality).

election laws are likely to be less effective than the power conferred on a state attorney general to supervise nonprofits in the public interest.

## I. BACKGROUND

Beginning in 1966, foreign contributions to domestic political campaigns were limited in order to protect national sovereignty and prevent foreign intrusion in domestic elections.<sup>6</sup> Since 1976, there has been an outright prohibition on foreign contributions to political campaigns.<sup>7</sup> In 2002, Congress strengthened these restrictions, and in 2012, the Supreme Court affirmed a decision declining to extend the reasoning of *Citizens United*<sup>8</sup> to invalidate the prohibition on foreign corporate contributions on First Amendment grounds.<sup>9</sup> As then-Judge (now Justice) Kavanaugh wrote,

It is fundamental to the definition of our national political community that foreign citizens do not have a constitutional right to participate in, and thus may be excluded from, activities of democratic self-government . . . [T]he United States has a compelling interest . . . in limiting the participation of foreign citizens in activities of American democratic self-government, and in thereby preventing foreign influence over the U.S. political process.<sup>10</sup>

Notwithstanding these legal prohibitions, foreign states, foreign corporations, and foreign nationals have channeled funds in an intentionally clandestine fashion through nonprofit political organizations, and other types of nonprofits, into the hands of political candidates running for office in the United States.<sup>11</sup> In 1996, for example, the Justice Department investigated

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<sup>6</sup> Bruce D. Brown, *Alien Donors: The Participation of Non-Citizens in the U.S. Campaign Finance System*, 15 YALE L. & POL'Y REV. 503, 508–10 (1997); 52 U.S.C. § 30121 (2012); see also *Foreign Nationals*, FED. ELECTION COMM'N, (June 23, 2017), <https://www.fec.gov/updates/foreign-nationals> [<https://perma.cc/7TSU-XVV7>].

<sup>7</sup> Brown, *supra* note 6, at 511. The view that a blanket ban on foreign contributions is unwise and unenforceable is offered by Jeffrey K. Powell, *Prohibitions on Campaign Contributions from Foreign Sources: Questioning Their Justification in a Global Interdependent Economy*, 17 U. PA. J. INT'L ECON. L. 957, 959 (1996). Internationally, Powell reported, most democratically governed nations have blanket prohibitions against foreign contributions to elections, including Japan, India, Spain, Mexico, and Canada, although Great Britain does not explicitly prohibit foreign contributions. *Id.* at 972–73.

<sup>8</sup> 558 U.S. 310 (2010).

<sup>9</sup> *Bluman v. FEC*, 565 U.S. 1104 (2012) (affirming 800 F. Supp. 2d 281 (D.D.C. 2011)). In 2002, U.S. law also prohibited foreign nationals from involvement in the management of a political committee, including any separate segregated fund-nonconnected committee, or the nonfederal accounts of any of these committees. 11 C.F.R. § 110.20 (2005).

<sup>10</sup> *Bluman*, 800 F. Supp. 2d 281 at 288.

<sup>11</sup> See Richard A. Oppel, Jr., *Democrats Are Fined \$243,000 for Fund-Raising Violations*, N.Y. TIMES (Sept. 21, 2002), <https://www.nytimes.com/2002/09/21/us/democrats-are-fined-243000-for-fund-raising-violations.html> [<https://perma.cc/6DPE-JCNL>]; Bob Woodward & Brian Duffy, *Chinese Embassy Role in Contributions Probed*, WASH. POST (Feb. 13, 1997), <https://www.washingtonpost.com/archive/politics/1997/02/13/chinese-embassy-role-in-contributions->

whether the Chinese military schemed to transfer money to the nonprofit Democratic National Campaign Committee (DNCC), and from there to President Bill Clinton's reelection campaign.<sup>12</sup> The DNCC gave back \$2.8 million it had received from individuals and for-profit entities,<sup>13</sup> and a 501(c)(3) religious organization, the International Buddhist Progress Society, also agreed to pay a civil penalty related to allegations of corporate facilitation of illegal contributions.<sup>14</sup> More recently, a Mexican businessman was convicted of violating federal election laws for improperly using funds to influence the 2012 San Diego mayoral election,<sup>15</sup> and a U.S. citizen pleaded guilty to facilitating illegal donations to an Obama campaign committee.<sup>16</sup>

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probed/62d55b8d-490f-49b2-9243-91f35ee4076b/?utm\_term=.100d91cc886d [https://perma.cc/7EFH-ZJLC]; John Fund, *Not All Foreign-Influence Scandals Are Created Equal*, NAT'L REV. (July 16, 2017, 10:35 PM), <https://www.nationalreview.com/2017/07/chinese-illegally-donated-bill-clinton-reelection-campaign-media-downplayed> [https://perma.cc/5R4V-RG5M].

<sup>12</sup> James Bennet, *Clinton Says Chinese Money Did Not Influence U.S. Policy*, N.Y. TIMES (May 18, 1998), <https://www.nytimes.com/1998/05/18/us/clinton-says-chinese-money-did-not-influence-us-policy.html> [https://perma.cc/Z6VC-K3KF]; see also Woodward & Duffy, *supra* note 11.

<sup>13</sup> Dan Balz, *Democrats Return \$1.4 Million in Questionable Donations*, WASH. POST (June 28, 1997), 1997 WLNR 7203134 (Westlaw) (detailing total amount returned as \$2.8 million, including some amounts where the DNC lacked sufficient information about donors).

<sup>14</sup> Conciliation Agreement at 1–2, 8, *In re International Buddhist Progress Society, Inc.*, (Nov. 27, 2000), <https://www.fec.gov/files/legal/murs/4530/00000306.pdf> [https://perma.cc/HY42-B54A]; Robert Lenhard, *FEC Issues Zero Tolerance Decision on Foreign National Contributions*, COVINGTON & BURLING LLP: INSIDE POL. L. (Nov. 21, 2014), <https://www.insidepoliticallaw.com/2014/11/21/fec-issues-zero-tolerance-decision-on-foreign-national-contributions/> [https://perma.cc/8FBS-BZRH]; *Al Gore and the Temple of Cash*, N.Y. TIMES (Feb. 22, 1998), <https://www.nytimes.com/1998/02/22/opinion/al-gore-and-the-temple-of-cash.html?mtrref=www.google.com&gwh=51B1F5DCF9A12C80B3C334DAA71EE91C&gwt=pay> [https://perma.cc/UEE5-DJRD] (describing Justice Department allegations of foreign gifts from American Buddhist monks to Al Gore during the 1996 election).

<sup>15</sup> Indictment (2nd Superseding), *United States v. Matsura*, No. 14CR0388-MMA (S.D. Cal. Mar. 4, 2016), 2016 WL 9080188; Greg Moran, *Judge Sentences Azano to Three Years in Federal Prison*, SAN DIEGO UNION TRIB. (Oct. 27, 2017, 5:45 PM), <https://www.sandiegouniontribune.com/news/courts/sd-me-azano-sentencing-20171027-story.html> [https://perma.cc/3RRY-A3Q3]. According to the Government's case, Azano used individual "straw donors" to make donations for candidates on his behalf, in addition to "in-kind" services to campaigns that were funded by foreign money. Indictment (2nd Superseding), *Matsura*, 2016 WL 9080188; Indictment (Superseding) at 6–7, *United States v. Matsura*, No. 14CR00388-MMA (S.D. Cal. Aug. 12, 2014), 2014 WL 10384719.

<sup>16</sup> Press Release, Dep't of Justice, Fla. Man Pleads Guilty to Helping Disguise Foreign Contribution During 2012 Presidential Election and Making False Declaration before Grand Jury (July 25, 2016), <https://www.justice.gov/opa/pr/florida-man-pleads-guilty-helping-disguise-foreign-contribution-during-2012-presidential> [https://perma.cc/L6YM-5XPU]; Nate Raymond, *Florida Man Admits Helping Funnel 2012 Foreign Political Contribution*, REUTERS (July 25, 2016, 2:53 PM), <https://www.reuters.com/article/us-florida-crime-election-idUSKCN10527V> [https://perma.cc/FBE3-4BZZ]. The campaign committee cooperated with investigators and was not accused of wrongdoing. Raymond, *supra*.

The scope of the problem caused by a lack of public information about dark money sources, and whether any of these sources could be foreign, is demonstrated by recent speculation over campaign support from the National Rifle Association (NRA) during the 2016 election cycle. The NRA operates as a 501(c)(4) social welfare organization, which is chartered in New York.<sup>17</sup> The NRA reported spending millions more during the 2016 campaign cycle on political campaign intervention than it had spent in previous cycles.<sup>18</sup> During this time, NRA officials and members also allegedly had contact with Russian nationals. According to a Statement of Offense by the United States Attorney for the District of Columbia, senior staff and board members of a “gun rights organization” communicated with Russians in the United States, and also visited Russia.<sup>19</sup> These allegations have led to speculation that

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<sup>17</sup> The National Rifle Association (NRA) consists of several affiliated entities, including the National Rifle Association of America, a 501(c)(4) organization incorporated in New York; the NRA Foundation, a 501(c)(3) organization incorporated in the District of Columbia; and the National Rifle Association of America Political Victory Fund, a political action committee that engaged in the support of pro-gun candidates during the 2016 election cycle. See *National Rifle Association of America Political Victory Fund: Spending 2015–2016*, FED. ELECTION COMM’N, <https://www.fec.gov/data/committee/C00053553/?cycle=2016&tab=spending> [https://perma.cc/CG2Q-SWKX].

<sup>18</sup> Reports of NRA support during the 2016 election cycle vary. During the two-year period from January 1, 2015 until December 31, 2016, the NRA Political Victory Fund reported \$21,260,409.45 in political contributions to the FEC. See *National Rifle Association of America Political Victory Fund: Financial Summary 2015–2016*, FED. ELECTION COMM’N, <https://www.fec.gov/data/committee/C00053553/?cycle=2016> [https://perma.cc/747Y-6V2S]. This amount is nearly a fifty percent increase over the 2011 to 2012 period. See *National Rifle Association of America Political Victory Fund: Financial Summary 2011–2012*, FED. ELECTION COMM’N, <https://www.fec.gov/data/committee/C00053553/?cycle=2012> [https://perma.cc/D295-3MPR]. A larger amount was reported to the FEC by the NRA’s lobbying arm, the Institute for Legislative Action. See *National Rifle Association Institute for Legislative Action: Spending 2015–2016*, *supra* note 17. According to an analysis by the Center for Responsive Politics, “the PAC and nonprofit arms of the NRA spent a combined \$54.4 million in the 2016 elections . . . \$35.2 million, was channeled through the NRA Institute for Legislative Action (NRA-ILA).” Robert Maguire, *Audit Shows NRA Spending Surged \$100 Million Amidst Pro-Trump Push in 2016*, OPENSECRETS.ORG (Nov. 15, 2017), <https://www.opensecrets.org/news/2017/11/audit-shows-nra-spending-surged-100-million-amidst-pro-trump-push-in-2016/> [https://perma.cc/ZLW6-N22H]; see also Peter Stone & Greg Gordon, *Web of Elite Russians Met with NRA Execs During 2016 Campaign*, MCCLATCHY DC BUREAU (June 11, 2018, 5:00 AM), <https://www.mcclatchydc.com/latest-news/article212756749.html> [https://perma.cc/7SYP-5RGQ] (“The NRA, Trump’s biggest financial backer, spent more than \$30 million to boost his upstart candidacy; that’s more than double what it laid out for 2012 GOP nominee Mitt Romney, and the NRA money started flowing much earlier in the cycle for Trump.”).

<sup>19</sup> Mariia Butina, also known as Maria Butina, a Russian national living in the United States, pled guilty to acting as a Russian agent and conspiring with the Russian Ministry of Foreign Affairs to involve the NRA (“Gun Rights Organization”) in furthering a “back channel of communication” to the NRA and the Republican Party (“Political Party 1”). Indictment, United States v. Butina, No. 18-cr-00218-TSC (D.D.C. July 17, 2018), 2018 WL 3455963 [hereinafter Butina Indictment]; Plea Agreement, United States v. Butina, No. 18-cr-00218-TSC (D.D.C. Dec. 13, 2018), 2018 WL 6583981 [hereinafter Butina Plea]; Statement of Offense, United States v. Butina, No. 18-cr-00218-TSC (D.D.C. May 1, 2019) [hereinafter Butina Statement]. She cooperated with investigators and was sentenced to eighteen months

foreign contributions might have been made from Russia or another country, using the NRA, an affiliate, or some 501(c)(4) organization as a conduit, during the period of the 2016 election campaign.<sup>20</sup> The NRA has denied using foreign funds for political activities,<sup>21</sup> but reports indicate that federal authorities have investigated whether the NRA used foreign donations to support political campaigns.<sup>22</sup> To date, all investigations have resulted in no

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in prison. Sara Murray & David Shortell, *Alleged Russian Agent Maria Butina Sentenced to 18 Months in Prison on Conspiracy Charge*, CNN (Apr. 27 2019, 6:59 AM), <https://www.cnn.com/2019/04/26/politics/maria-butina-sentencing/index.html> [https://perma.cc/98G3-BBRT]. In pleading guilty, Butina admitted to working with a Republican operative and boyfriend, Paul Erickson (identified in court papers as “U.S. Person 1”) at the behest of a Russian official in order “to establish unofficial lines of communication with Americans having power and influence over U.S. politics . . . for the benefit of the Russian Federation . . .” Butina Statement, *supra*, at 2; see Criminal Complaint, United States v. Butina, No. 18-cr-00218-TSC (D.D.C. July 14, 2018), 2018 WL 3455966. The indictment of Butina does not allege that Butina sought to or did funnel funds from Russia to the NRA. Butina Indictment, *supra*.

<sup>20</sup> See, e.g., Chris Smith, “Coincidence Number 395”: *The N.R.A. Spent \$30 Million to Elect Trump. Was It Russian Money?*, VANITY FAIR (June 21, 2018), <https://www.vanityfair.com/news/2018/06/the-nra-spent-dollar30-million-to-elect-trump-was-it-russian-money> [https://perma.cc/S9GM-A3YV].

<sup>21</sup> Tim Mak, *NRA Says It Receives Foreign Funds, But None Goes to Election Work*, NPR (Mar. 27, 2018, 11:11 AM), <https://www.npr.org/2018/03/27/597279176/nra-says-it-receives-foreign-funds-but-none-goes-to-election-work> [https://perma.cc/2N4U-DMS9]. However, the NRA has acknowledged receiving small donations from foreign sources. *Id.*; Trish Turner & Matthew Mosk, *NRA Says It Received One Contribution of Less Than \$1000 from a Russian*, ABC NEWS (Mar. 28, 2018, 5:19 PM), [https://abcnews.go.com/amp/Politics/nra-received-contribution-1000-russian/story?id=54080082&\\_twitter\\_impression=true](https://abcnews.go.com/amp/Politics/nra-received-contribution-1000-russian/story?id=54080082&_twitter_impression=true) [https://perma.cc/CV8N-LG25]. The NRA acknowledged a small donation representing life membership dues from Alexander Torshin, the Russian official understood to be referenced to in the Maria Butina case, but “NRA General Counsel John C. Frazer, in a letter to Sen. Ron Wyden of Oregon . . . said the gun-rights group accepted foreign donations, though not for electioneering purposes.” Turner & Mosk, *supra*.

<sup>22</sup> Peter Stone & Greg Gordon, *FBI Investigating Whether Russian Money Went to NRA to Help Trump*, McCLATCHY DC BUREAU (Jan. 18, 2018, 5:00 AM), <https://amp.mcclatchydc.com/news/nation-world/national/article195231139.html> [https://perma.cc/WUM5-HVG5]. But see Mark Follman, *The NRA Has Deep Ties to Accused Russian Spy Maria Butina*, MOTHER JONES (July 19, 2018), <https://www.motherjones.com/politics/2018/07/nra-maria-butina-spying-charges-trump-campaign> [https://perma.cc/2AME-KM5X] (stating FBI would “neither confirm nor deny” the existence of an investigation). The Attorney General of New York opened an investigation of the tax-exempt status of the NRA and its affiliated entities in April 2019, without specifying its particular concerns. See Danny Hakim, *N.R.A. President to Step Down as New York Attorney General Investigates*, N.Y. TIMES (Apr. 27, 2019), <https://www.nytimes.com/2019/04/27/us/oliver-north-nra.html> [https://perma.cc/9TGN-3E9U]; see also Press Release, N.Y. State Att’y Gen., AG James Stops NRA from Attending Interviews of Witnesses (Aug. 19, 2019), <https://ag.ny.gov/press-release/ag-james-stops-nra-attending-interviews-witnesses> [https://perma.cc/F4HV-VK9Z]. Investigations into the NRA and its charitable foundation also arose in the District of Columbia. See Katie Zezima, Carol D. Leonnig & Keith L. Alexander, *D.C. Attorney General Issues Subpoenas to NRA, Its Charitable Foundation*, WASH. POST (July 12, 2019), [https://www.washingtonpost.com/national/dc-attorney-general-issues-subpoenas-to-nra-its-charitable-foundation/2019/07/12/835bb30e-a4bb-11e9-bd56-eac6bb02d01d\\_story.html](https://www.washingtonpost.com/national/dc-attorney-general-issues-subpoenas-to-nra-its-charitable-foundation/2019/07/12/835bb30e-a4bb-11e9-bd56-eac6bb02d01d_story.html) [https://perma.cc/P2G2-LFTR] (reporting that the Office of the Attorney General for the District of Columbia issued subpoenas to the NRA and the NRA Foundation as part of an investigation into a possible violation of the District’s Nonprofit Act, and noting that “[t]wo Democratic House members have written to NRA



charges or official accusations that the NRA used foreign funds to support domestic political campaigns.<sup>23</sup> However, because nonprofits are not required to disclose their donors' identities,<sup>24</sup> observers (including media and members of Congress) have continued to ask questions about the increase in NRA campaign support for U.S. elections.<sup>25</sup>

The use of 501(c)(4) organizations to engage in political activity and fund political campaigns has expanded significantly over the past decade.<sup>26</sup> Nonetheless, public records do not reveal that either the Federal Election Commission (FEC) or the Internal Revenue Service (IRS) have imposed a

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Executive Vice President Wayne LaPierre, stating they were concerned about a 'complex web of relationships' between the organization and Russia.”).

<sup>23</sup> See James Bamford, *The Spy Who Wasn't*, NEW REPUBLIC (Feb. 11, 2019), <https://newrepublic.com/article/153036/maria-butina-profile-wasnt-russian-spy> [<https://perma.cc/98ZC-YQHJ>] (stating the FBI investigation “produced no evidence of illicit cash transfers” and arguing that Butina was a scapegoat for the 2016 election); see also Butina Plea, *supra* note 19; Butina Statement, *supra* note 19; Butina Indictment, *supra* note 19 (including no admissions in Butina's plea agreement or statement of offense that she sought to or did transfer or assist in the transfer of Russian funds to the NRA to support U.S. political campaigns).

<sup>24</sup> Sugin, *supra* note 2, at 899–900 (“[T]he identity of donors to (c)(4) organizations remains secret . . . .”); see Rev. Proc. 2018-38, 2018-31 I.R.B. 280 (“These [Section 501(c)(3)] organizations are no longer required to report the names and addresses of their contributors on the Schedule B of their Forms 990 or 990-EZ.”); see also Cory G. Kalanick, Note, *Blowing Up the Pipes: The Use of (c)(4) to Dismantle Campaign Finance Reform*, 95 MINN. L. REV. 2254, 2258 (2011).

<sup>25</sup> See, e.g., Igor Derysh, *Maria Butina's Boyfriend Claimed He Set Up Trump-Russia NRA "Conduit" as Campaign Funds Flowed*, SALON (Dec. 12, 2018, 12:00 PM), <https://www.salon.com/2018/12/12/maria-butinas-boyfriend-claimed-he-set-up-trump-russia-nra-conduit-as-campaign-funds-flowed> [<https://perma.cc/A4QJ-UEQB>]; Danny Hakim, *N.R.A. Seeks Distance From Russia as Investigations Heat Up*, N.Y. TIMES (Jan. 28, 2019), <https://www.nytimes.com/2019/01/28/us/nra-russia-maria-butina-investigations.html> [<https://perma.cc/KT62-D2TZ>]; Pete Madden & Matthew Mosk, *Lawmakers Launch New Probe into 'Complex Web' of Alleged Ties Between NRA, Russians*, ABC NEWS (Feb. 18, 2019, 9:02 AM), <https://abcnews.go.com/Politics/lawmakers-launch-probe-complex-web-alleged-ties-nra/story?id=61137356> [<https://perma.cc/9ZQX-X7J6>] (reporting inquiry by Reps. Kathleen Rice and Ted Lieu into Moscow trip by NRA members). There is no readily available information on the NRA website pertaining to foreign donors. NAT'L RIFLE ASS'N, <https://home.nra.org> [<https://perma.cc/B3N5-8UNF>].

<sup>26</sup> Michael Beckel, *Nonprofits Outspent Super PACs in 2010*, OPENSECRETS.ORG (June 18, 2012), <https://www.opensecrets.org/news/2012/06/nonprofits-outspent-super-pacs-in-2> [<https://perma.cc/QKN7-ZPY3>] (“While super PACs were cast as the big, bad wolves during the last election, the groups were outspent by “social welfare” organizations by a 3-2 margin, a trend that may continue amid reports that major donors are giving tens of millions of dollars to the secretive nonprofit groups.”); Sean Sullivan, *What Is a 501(c)(4), Anyway?*, WASH. POST (May 13, 2013), <https://www.washingtonpost.com/news/the-fix/wp/2013/05/13/what-is-a-501c4-anyway> [<https://perma.cc/V5XJ-4EZK>] (explaining the “key difference” is that “[s]uper PACs must disclose their donors while 501(c)(4)s do not. If you are a donor looking to influence [an] election but do not want to reveal your identity, the 501(c)(4) is an attractive option through which to send your cash.”); see also Sugin, *supra* note 2, at 897–98 (arguing for states to intervene in the regulation of 501(c)(4) organizations to protect the charitable sector).

penalty upon a social welfare organization for serving as a foreign conduit.<sup>27</sup> Because nonprofit organizations are shielded from revealing sources of campaign donations and the use of dark money donations has grown substantially,<sup>28</sup> this Essay examines the possibility that illegal donations from foreign sources have previously—or could in the future—illegally fund domestic campaigns without reporting or public knowledge. It examines potential legal responses that might ensure accountability and deter misconduct if a hypothetical 501(c)(4) organization intentionally or unintentionally allowed itself to be used as a conduit for foreign funds to support U.S. political campaigns. These could be pursued either by federal authorities—utilizing election laws, money-laundering statutes, or tax law—or state authorities—using state nonprofit laws standing alone or in conjunction with other proscriptions.

## II. EXPLORATIONS OF LIABILITY

Can federal and state authorities hold nonprofits culpable as entities and hold their management and board responsible for illegal donations? What are the fiduciary duties of officers, directors, and staff of nonprofit organizations with respect to monitoring the funds they receive and the campaign activities in which they engage? Is there civil or criminal liability for a board member who fails to diligently monitor—or is willfully ignorant of—donations to their nonprofit that come directly or indirectly from a foreign terrorist, criminal, or state-supported foreign entity and are contributed to political campaigns? These questions are important in order to understand whether existing rules are adequate to promote fair elections and police nonprofit welfare organizations.

Suppose investigations by the FBI, FEC, or a state attorney general acting independently, reveal that senior staff and board members of a 501(c)(4) nonprofit organization assisted a foreign terrorist or a criminal organization by recklessly or intentionally permitting the organization to be a conduit for unlawful contributions. Or suppose the organization has itself engaged in campaign activities using foreign funds. What potential legal perils would confront the organization and its officers, directors, donors, and staff? This Part addresses three potential sources of law to confront illegal

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<sup>27</sup> Investigations of 501(c)(4) welfare organizations that did not result in assessments would not be disclosed by the IRS or FEC over email with the author or in telephone conversations with a Northwestern Law Review Associate Editor. *See* Email from Cecilia Barreda, IRS Media Relations, to Norman Silber (Sept. 5, 2019, 01:21 EST) (email on file with author).

<sup>28</sup> Anna Massoglia, *State of Money in Politics: Billion-Dollar 'Dark Money' Spending Is Just the Tip of the Iceberg*, OPENSECRETS.ORG (Feb. 21, 2019), <https://www.opensecrets.org/news/2019/02/somp3-billion-dollar-dark-money-tip-of-the-iceberg> [https://perma.cc/CYH8-R3QT] (charting growth in partially disclosed and undisclosed funding).

donations and their shortcomings: (1) election law; (2) criminal money laundering statutes; and (3) IRS authority.

### A. Federal Election Law

Federal election laws fail adequately to discourage social welfare organizations from accepting unlawful foreign contributions. Consider first the nature of the civil and criminal violations of the election laws. Contributions *by* foreign nationals to U.S. political campaigns are prohibited by federal election law and are subject to civil and criminal penalties.<sup>29</sup> Contributions *to* political campaigns by prohibited foreign parties in the name of another person are treated identically and are subject to the same penalties.<sup>30</sup> Knowingly accepting foreign contributions is also prohibited and subject to criminal and civil penalties.<sup>31</sup> Furthermore, laundering campaign contributions through conduits and straw donors is “persuasive evidence of the Act’s willful intent element.”<sup>32</sup>

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<sup>29</sup> Prohibition on Contributions, Donations, Expenditures, Independent Expenditures, and Disbursements by Foreign Nationals, 11 C.F.R. § 110.20(b) (2016) provides: “A foreign national shall not, directly or indirectly, make a contribution or a donation of money or other thing of value, or expressly or impliedly promise to make a contribution or a donation, in connection with any Federal, State, or local election.” Paragraph (c) prohibits contributions or donations to “a political committee of a political party, including a national party committee, a national congressional campaign committee, or a State, district or local party committee . . . .” Paragraph (e) prohibits disbursements by foreign nationals for electioneering communications. Paragraph (f) prohibits knowing solicitation, acceptance, or receipt from a foreign national of any prohibited contribution or donation. Paragraph (g) is titled “Solicitation, acceptance, or receipt of contributions and donations from foreign nationals,” and provides: “No person shall knowingly solicit, accept, or receive from a foreign national any contribution or donation prohibited by paragraphs (b) through (d) of this section.” Paragraph (j) prohibits direct or indirect donations to an inaugural committee and knowing acceptance of a donation to an inaugural committee. 11 C.F.R. § 111.24(a)(2) (2016) establishes relatively modest monetary civil penalties for knowing and willful violations. The Department of Justice has concurrent criminal jurisdiction and has criminally prosecuted individuals for violating this prohibition on foreign political contributions. See Ciara Torres-Spelliscy, *Yes. Violating Certain Campaign Finance Laws Is a Criminal Offense*, MOYERS (July 13, 2017), <https://billmoyers.com/story/violating-certain-campaign-finance-laws-criminal-offenses/> [<https://perma.cc/63FP-9K9F>]. The section applies to both federal and non-federal elections.

<sup>30</sup> 52 U.S.C. § 30122 (2012) (“No person shall make a contribution in the name of another person or knowingly permit his name to be used to effect such a contribution, and no person shall knowingly accept a contribution made by one person in the name of another person.”).

<sup>31</sup> *Id.* As this Essay indicates, state law director fiduciary standards for determining misconduct would be less demanding. See *infra* notes 70–73.

<sup>32</sup> FEDERAL PROSECUTION OF ELECTION OFFENSES 141 (Richard C. Pilger ed., 8th ed. 2017). In the context of domestic contributions of campaign funds, federal election regulations prohibit state political campaign committees from serving as laundering conduits to “circumvent” limits on “soft money.” See *FEC v. Beaumont*, 539 U.S. 146, 160 (2003) (“Nonprofit advocacy corporations are . . . no less susceptible than traditional business companies to misuse as conduits for circumventing the contribution limits imposed on individuals.”); see also *McConnell v. FEC*, 540 U.S. 93, 162 (2003), *partially overruled by* *Citizens United v. FEC*, 558 U.S. 310 (2010) (“The core of § 323(b) [now 52 U.S.C.

The statute enabling the FEC to enforce the prohibition on foreign contributions, however, includes a remarkably stringent test for establishing that a nonprofit actor knowingly accepted an illegal contribution.<sup>33</sup> In contrast to a test that would permit reasonable inferences to be drawn, the liability of a recipient will be triggered only if there is “[a]ctual knowledge that the funds have come from a foreign national; [a]wareness of certain facts that would lead a reasonable person to believe that there is a substantial probability that the money is from a foreign national; or [a]wareness of facts that should have prompted a reasonable inquiry into whether the source of funds is a foreign national.”<sup>34</sup>

There is, additionally, a safe harbor: If the nonprofit obtains copies of a donor’s current and valid U.S. passport, then, unless the defendant is proved to have “actual knowledge that the source of the funds solicited, accepted, or received is a foreign national,” there will be insufficient proof of intent to satisfy the culpability standard.<sup>35</sup> There is furthermore no requirement for a 501(c)(4) publicly to divulge the names of its donors, which might help in an effort to establish a nexus between a foreign contributor and an entity.<sup>36</sup>

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§ 30125] is a straightforward contribution regulation: It prevents donors from contributing nonfederal funds to state and local party committees to help finance ‘Federal election activity.’”).

<sup>33</sup> 11 C.F.R. § 110.20 (prohibiting contributions, donations, expenditures, independent expenditures, and disbursements by foreign nationals); *Who Can and Can’t Contribute*, FED. ELECTION COMM’N, <https://www.fec.gov/help-candidates-and-committees/candidate-taking-receipts/who-can-and-cant-contribute> [https://perma.cc/Y2S3-QYVN]; see text *infra* at note 34.

<sup>34</sup> *Who Can and Can’t Contribute*, FED. ELECTION COMM’N, *supra* note 33. 11 C.F.R. § 110.20 further provides that a recipient should decline a gift in circumstances such as where the contributor uses a foreign passport for identification purposes or provides a foreign address; or if the contribution is made from a foreign bank; or the contributor or donor resides abroad, and the written justification for the regulation states that the third prong of the standard establishes, “in effect willful blindness.” 67 Fed. Reg. 69,928, 69,941 (Nov. 19, 2002) (codified at 11 C.F.R. § 110.20) is applicable to situations in which a known fact should have prompted a reasonable inquiry, but did not. But the safe harbor in 11 C.F.R. § 110.20(a)(7) provides that a person has conducted a reasonable inquiry if he or she seeks and obtains copies of current and valid U.S. passport papers unless he or she has “actual knowledge that the source of the funds solicited, accepted, or received is a foreign national.” 11 C.F.R. § 110.20(a)(7).

<sup>35</sup> *Id.*

<sup>36</sup> A 501(c)(4) organization is not required by federal tax or election law publicly to divulge campaign fund donors or recipients. See Gene Takagi, *Treasury Eliminates Donor Information Disclosures by 501(c)(4) and 501(c)(6) Organizations*, NEO L. GROUP (July 16, 2018), <http://www.nonprofitlawblog.com/treasury-eliminates-donor-information-disclosures-by-501c4-and-501c6-organizations> [https://perma.cc/X3AK-6SDK]. At the time of the 2016 presidential campaign, however, the names of donors were required to be reported to the IRS confidentially. The confidentiality of records of the board meetings of nonprofit organizations, which according to the organization’s governing documents are definable as confidential, as well as lists of members and donors, unless subject to open meetings laws, will be enforced. Such material, however, is subject to subpoena by appropriate law enforcement and regulatory officers in appropriate circumstances. State laws requiring the submission of donor lists by nonprofits has been upheld. See, e.g., *Ams. for Prosperity Found. v. Becerra*, 903 F.3d 1000, 1004 (9th Cir. 2018) (“[T]he California Attorney General’s Schedule B requirement, which obligates charities to submit the very information they already file each year with the IRS, survives

As a further observation, it should be noted that the likelihood of detection and prosecution is further inhibited by the fact that nothing in the federal election law specifically prohibits a foreign person or entity from making a general gift to a nonprofit.<sup>37</sup> Subsequent to receipt of a gift by a foreign source to general funds, a nonprofit—money being fungible—might reallocate other general funds toward campaign activities without being noticed or readily traced.

If, however, a nonprofit were so reckless, unreasonable, and devoid of sound legal advice as to use foreign-sourced funds to make donations to political campaigns, steer around the safe harbor, and knowingly and directly place foreign contributions into an account dedicated to the support of a political campaign, then the FEC or the Justice Department, or both, *might* find a violation and pursue relatively limited civil fines, or potentially bring more serious criminal charges under the statute.<sup>38</sup> In short, federal election law regulations are evadable and do not effectively deter misconduct by a nonprofit determined to facilitate illegality.

#### B. Federal and State Criminal Money-Laundering Statutes

Criminal money-laundering statutes are ill-equipped to address this problem as well. If it were determined that a nonprofit organization or its senior officers or directors intentionally converted the proceeds of “some form of unlawful activity” so that the donated funds appeared to be coming from lawful sources, then federal and state money-laundering statutes might be invoked.<sup>39</sup> A federal conviction for money laundering can result in fines of up to \$500,000, or double the amount of money that was laundered, whichever is greater.<sup>40</sup> New York has also established money-laundering offenses denominated from the fourth degree to the first degree.<sup>41</sup> Other

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exactng scrutiny as applied to the plaintiffs because it is substantially related to an important state interest in policing charitable fraud.”); *Citizens United v. Schneiderman*, 882 F.3d 374, 378 (2d Cir. 2018) (rejecting the claim that requiring nonprofit organizations to disclose their donors on a yearly basis violates the First Amendment). *But see* *Nat’l Ass’n for Advancement of Colored People v. Alabama*, 357 U.S. 449, 458–59 (1958) (denying the state a subpoena to obtain NAACP records, including membership lists).

<sup>37</sup> 11 C.F.R. § 110.20 (b)–(j) prohibit enumerated electioneering and political contributions by foreign nationals. The regulation does not limit foreign persons or entities from making general gifts to a nonprofit.

<sup>38</sup> FEDERAL PROSECUTION OF ELECTION OFFENSES, *supra* note 32, at 138.

<sup>39</sup> 18 U.S.C. § 1956 (2016) (imposing civil penalties and/or imprisonment on those who knowingly conduct or attempt to conduct a financial transaction, or transfer, involving unlawful proceeds); 18 U.S.C. § 1957 (2016) (mandating punishment for those who knowingly engage or attempt to engage in a monetary transaction involving criminally derived property in excess of \$10,000, and the offense either occurs within the jurisdiction of the United States, or the defendant is a person of the United States).

<sup>40</sup> § 1956(a)(1)–(2).

<sup>41</sup> A person is guilty of money laundering in the fourth degree when,

major nonprofit jurisdictions, including California, Massachusetts, and Florida, have also established statutes to punish money-laundering offenses.<sup>42</sup>

Under both federal and New York state statutes, it would be futile to argue that a monetary gift transformed sums of money into illegal proceeds.<sup>43</sup> The elements of the offense require that the laundering recipient knows that the funds are the proceeds of felonious activity, and in many jurisdictions specified types of felonious criminal conduct.<sup>44</sup> In short, perhaps the donated foreign-source sums themselves derived from illegal sources, but unless it

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Knowing that the property involved in one or more financial transactions represents the proceeds of criminal conduct he or she conducts one or more such financial transactions which in fact involve the proceeds of specified criminal conduct with intent to: promote the carrying on of criminal conduct or engage in conduct constituting a felony . . . [under tax law]; or knowing that the transaction or transactions in whole or in part are designed to conceal or disguise the nature, the location, the source, the ownership or the control of the proceeds of criminal conduct; or avoid any transaction reporting requirement imposed by law . . . .

N.Y. PENAL LAW §§ 470.05–20 (2019) (internal sectioning omitted). Failing to report income derived from criminal activity in a material manner can be a felony under federal tax law. *See* 26 U.S.C. § 7206 (2012); 26 U.S.C. § 7201 (2012).

<sup>42</sup> In California, for example, an individual may be found guilty of money laundering when: (1) the individual completed a transaction or series of transactions through at least one financial institution; (2) the total amount of the transaction(s) is more than \$5,000 or a total value exceeding \$25,000 within a 30-day period; and (3) the transaction(s) was made with the intent to promote criminal activity or the individual knew that the funds involved were the proceeds of criminal activity. CAL. PENAL CODE § 186.10 (West 2019). Massachusetts imposes penalties for money laundering on those who,

knowingly transport[] or possess[] a monetary instrument or other property that was derived from criminal activity with the intent to promote, carry on or facilitate criminal activity [or knowingly] engage[] in a transaction involving a monetary instrument or other property known to be derived from criminal activity with the intent to promote, carry on or facilitate criminal activity . . . .

MASS. GEN. LAWS ch. 267A, § 2 (2019) (internal sectioning omitted). The Florida Money Laundering Act states in pertinent part:

It is unlawful for a person [k]nowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, to conduct or attempt to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity: [w]ith the intent to promote the carrying on of specified unlawful activity; or [k]nowing that the transaction is designed in whole or in part [t]o conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity . . . .

FLA. STAT. § 896.101 (2011) (internal sectioning omitted).

<sup>43</sup> *See, e.g.*, CHARLES DOYLE, CONG. RESEARCH SERV., MONEY LAUNDERING: AN OVERVIEW OF 18 U.S.C. 1956 AND RELATED FEDERAL CRIMINAL LAW 3 (2012); 2101. *Money Laundering Overview*, U.S. DEP'T OF JUSTICE, <https://www.justice.gov/jm/criminal-resource-manual-2101-money-laundering-overview> [https://perma.cc/AMD8-VCEN].

<sup>44</sup> *See supra* note 43. Similar to other leading jurisdictions, New York Penal Law requires that the individual possess knowledge of the proceeds' illegal source. *See* N.Y. PENAL LAW §§ 470.05–20. Additionally, to impose money-laundering penalties pursuant to the United States Code, the individual must be aware, or know, that the funds are derived from an illegal source. *See* 18 U.S.C. §§ 1956–57 (2012).

can be established that the donated funds were the product of criminal activity, and that the nonprofit organization or its officers or directors could be charged with intentional criminal conduct, the nonprofit and its officers and directors would not be subject to money-laundering penalties.<sup>45</sup>

### C. Internal Revenue Service Authority

Penalties potentially imposed by the FEC and the Justice Department would be the beginning of the story of federal enforcement. But what about the IRS? If a penalty is assessed against a nonprofit by the FEC, or an audit by the IRS reveals unlawful expenditures, how might the IRS hold accountable such a nonprofit and discourage future misconduct?

Crucial for understanding of the IRS's accountability problem is an appreciation of the distinctions between the treatment of 501(c)(3) charitable organizations and a 501(c)(4) social welfare organizations. Section 501(c)(3) of the Internal Revenue Code allows "insubstantial" political activity and absolutely forbids political campaigning; Internal Revenue Code Section 4955 further imposes a series of graduated taxes on an offending 501(c)(3) nonprofit organization and on managers who make "political expenditures."<sup>46</sup>

In the case of 501(c)(4) organizations, the regime is different. Unlike 501(c)(3) groups who cannot engage in campaigning, 501(c)(4) social welfare organizations are *entitled*—by regulatory and judicial interpretation—to engage in as much non-campaign related political activity as they choose, provided it is not the "primary" activity of the organization; furthermore, like 501(c)(3) groups, social welfare organizations can accept foreign donations and deploy them for nonpolitical and advocacy purposes.<sup>47</sup>

<sup>45</sup> See N.Y. PENAL LAW §§ 470.05–20; 18 U.S.C. § 1956.

<sup>46</sup> The tax in Section 4955 is on "any amount paid or incurred by a section 501(c)(3) organization in any participation in, or intervention in (including the publication or distribution of statements), any political campaign on behalf of (or in opposition to) any candidate for public office." 26 U.S.C. § 4955(d)(1) (2012). The amount of the tax is initially a percentage of the amount spent, and it is supplemented dramatically by additional taxes if there is no recovery of the amount spent and no safeguards against future misbehavior established. § 4955(a)–(c).

<sup>47</sup> Social Welfare organizations classified as 501(c)(4)s must operate "primarily" to serve social welfare, and contributions to these groups are not tax-deductible. The maximum amount of political activity social welfare organizations may engage in before political campaigning becomes their "primary" activity is unspecified. See Rev. Rul. 81-95, 1981-1 C.B. 332, 1981 WL 166125; see also Aprill, *supra* note 2, at 43 n.2; Johnny Rex Buckles, *Curbing (or Not) Foreign Influence on United States Politics and Policies Through the Federal Taxation of Charities*, 79 MD. L. REV. \_\_ (forthcoming 2020) (exploring the lawful yet questionable means by which foreign actors are permitted to influence domestic political campaigns with contributions to nonprofit organizations). In contrast, Internal Revenue Code Section 527 organizations specifically engage in political campaigning, and their campaign expenditures are also shielded from taxation, but their donor lists are public and their non-campaign activities are restricted. See 26 U.S.C. § 527 (2012).

In addition, while it is true that 501(c)(4) social welfare organizations—as well as 501(c)(5) labor and agricultural organizations and 501(c)(6) business league organizations—face a tax similar to the tax faced by 501(c)(3) organizations on expenditures that “influenc[e] or attempt[] to influence the selection, nomination, election, or appointment of any individual to any State or local public office or office in a . . . political organization,” the disciplinary impact of this tax breaks down. This breakdown is due to the authorization for 501(c)(4) organizations to establish “segregated funds,” closely resembling FEC “Political Action Committees,” which may collect and spend funds on political campaign-intervention free of the tax on exempt expenditures.<sup>48</sup> The wisdom of permitting this escape hatch has been contested, but it stands as the law.<sup>49</sup> Thus, supposing that foreign illegal activity is engaged in by means of a 501(c)(4)’s segregated fund, there appears to be no directly applicable intermediate sanction—the Internal Revenue Code does not provide for excise taxes on social welfare organizations that knowingly or recklessly engage in impermissible political activity.<sup>50</sup>

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Because donations to 501(c)(3) organizations are tax deductible but donations to 501(c)(4) organizations are not, an incentive exists to donate to 501(c)(3) organizations, which will transfer amounts of money that are not “substantial” to 501(c)(4) organizations in to attempt to influence legislation. Charities funding affiliated social welfare organizations must therefore strictly condition gifts above the “insubstantial” on use for charitable purposes only. There is no precise definition of “substantial.” As one court has explained, “[a]lthough there is no statutory or regulatory definition of what constitutes a ‘substantial part’ of an organization’s activities, courts have found that less than 5% of an organization’s activity is not substantial, while over 16.6% is substantial.” *United Food & Commer. Workers Local 99 v. Brewer*, 817 F. Supp. 2d 1118 (D. Ariz. 2011) (comparing *Seasongood v. Comm’r*, 227 F.2d 907 (6th Cir. 1955) with *Haswell v. United States*, 500 F.2d 1133, 1146 (Ct. Cl. 1974)). Only if an organization makes a 501(h) election is there a formula to determine the precise permissible amount of a funds transfer to a 501(c)(4). See *The Powerful, Free, and Easy 501(h) Election: Benefits Galore!*, NAT’L COUNCIL NONPROFITS, <https://alliancefornevadanonprofits.com/wp-content/uploads/2013/02/501h.pdf> [https://perma.cc/6X2W-5FGT]. Continuing with the hypothetical example of the 501(c)(3) NRA Foundation, it did not make a 501(h) election in the 2016 fiscal tax year and so its permissible lobbying expenses are those allowed under the ambiguous “substantial” amount test. The NRA Foundation transferred at least \$206 million to the NRA since 2010. See Danny Hakim, *At the N.R.A., a Cash Machine, Sputtering*, N.Y. TIMES (May 14, 2019), <https://www.nytimes.com/2019/05/14/us/nra-finances-executives-board-members.html> [https://perma.cc/5KR7-NQNV] (analyzing NRA tax records).

<sup>48</sup> § 527(e)(5)(A). Compare § 527(f)(3) with § 4955 (allowing for graduated taxes on offending 501(c)(3) nonprofit organizations who engage in political campaigning or make political expenditures). See also Johnny Rex Buckles, *Not Even a Peep? The Regulation of Political Campaign Activity by Charities Through Federal Tax Law*, 75 U. CIN. L. REV. 1071, 1077–78, 1078 n.40 (2007).

<sup>49</sup> See *supra* notes 46–48 and accompanying text. See generally Roger Colinvax, *Social Welfare and Political Organizations: Ending the Plague of Inconsistency*, 21 N.Y.U. J. LEGIS. & PUB. POL’Y 481 (2018).

<sup>50</sup> See § 527 (failing to mandate, or specify, excise taxes for social welfare organizations engaging in illegal political activities).



The principal reason for the passage of intermediate sanctions that affect penalties for misconduct by private foundations and 501(c)(3) public charities was to empower the IRS to impose an effective and calibrated disincentive against misbehavior rather than having to destroy an entity entirely by revoking its exempt status. Yet absent from the tax code is an analogous provision that would impose a tax on social welfare organizations that violate federal election campaign expenditure laws, as well as on their culpable managers and board members, including for violations of 52 U.S. Code Section 30121, which covers “contributions and donations by foreign nationals.”<sup>51</sup> Such a rule would do more to deter minor violations than can be done under present tax law.<sup>52</sup>

Without authority to sanction the board or its individual members, the IRS could consider other approaches. Illegal foreign contributions—whether classified as unrelated business income, gifts, or otherwise—would constitute income that a nonprofit would need to report accurately.<sup>53</sup> It would be unlawful not to report the income or pay any tax that is due on it. If hidden donations went unreported and were characterizable as unrelated business income, for example, that intentional mischaracterization or under-reporting could jeopardize an organization’s tax exemption.<sup>54</sup> That being said, a sophisticated nonprofit organization that is determined to operate as a conduit for foreign funds or to acquiesce in their receipt would probably

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<sup>51</sup> See 52 U.S.C. § 30121 (2012).

<sup>52</sup> Lloyd Hitoshi Mayer, “*The Better Part of Valour Is Discretion*”: Should the IRS Change or Surrender Its Oversight of Tax-Exempt Organizations?, 7 COLUM. J. TAX L. 80, 100 (2016) (noting that increased penalties would enhance compliance if the organization or its members are aware of the costs and risks of noncompliance).

<sup>53</sup> James v. United States, 366 U.S. 213, 218 (1961) (embezzled funds must be included in the gross income of the embezzler); 26 C.F.R. § 1.61–14 (2019) (“Illegal gains constitute gross income.”). Money acquired through illegal means must be reported and taxed. Income from illegal activities must be included as income on Form 1040, line 21. Form 990 attaches great importance to reporting unrelated business income. In its guidance about gaming operations, for example, the Service states that:

IRC Section 501(c)(4) organizations promote social welfare. Gaming is considered both a business and a recreational activity; it does not ordinarily promote social welfare. If it is the primary activity of a social welfare organization, it may jeopardize the organization’s exempt status. If not a primary activity, the gaming income will be UBTI unless an exclusion or exception applies.

*Exempt Organization Gaming and Unrelated Business Taxable Income*, INTERNAL REVENUE SERV. (Mar. 26, 2019), <https://www.irs.gov/charities-non-profits/exempt-organization-gaming-and-unrelated-business-taxable-income> [https://perma.cc/EH8W-U74Z].

<sup>54</sup> Organizations classified as 501(c)(4)s must complete IRS Form 990 and complete Schedule C, parts I and III if they engage in lobbying and campaign activities. Schedule C requires that the organization provide a description of direct and indirect campaign activities and political campaign political expenditures. See INTERNAL REVENUE SERV., U.S. DEP’T OF TREAS., INSTRUCTIONS FOR SCHEDULE C (FORM 990 OR 990-EZ) (2019), <https://www.irs.gov/pub/irs-pdf/i990sc.pdf> [https://perma.cc/K2T2-EM5L].

report a foreign-sourced contribution as a gift for purposes unrelated to the support of any political campaign.<sup>55</sup>

The IRS could try to revoke the tax-exempt status of the nonprofit for failing to meet its “operational mandate.”<sup>56</sup> When an organization does not operate in ways that serve its mission, its status must be revoked.<sup>57</sup> This failure occurs in mundane situations, such as by the neglect to complete informational returns, or, more unusually, by a deviation from a stated tax-exempt purpose. This happened, for instance, to an association of war veterans which failed to have sufficient war veterans as members.<sup>58</sup> Notably, in June 2018, the IRS revoked the tax-exempt status of Americans for Job Security, a tax-exempt 501(c)(6) business league which spent millions of dollars influencing elections but failed to file its tax returns for three years. However, it was the failure to file, rather than the political activity itself, which formed the basis for the revocation.<sup>59</sup>

While the general proposition that revocation is a viable option in appropriate circumstances is a sound one, the possibility that the IRS would revoke the tax-exempt status of a large, powerful, national nonprofit social welfare organization with thousands of members that was not found guilty of an FEC violation seems remote. If an incumbent political administration had received considerable support from and had strong links to the nonprofit advocacy organization, the imposition of a drastic penalty would be theoretical at best—even if members of the board confessed to engaging in

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<sup>55</sup> See e.g., *United States v. Kanchanalak*, 192 F.3d 1037, 1039 (D.C. Cir. 1999) (holding that FEC reporting regulations require the true source of conduit contributions be reported following accusations that the defendants were funneling illegally disguised foreign campaign funds into national and state political committees and filing false reports with the FEC).

<sup>56</sup> See *Revoked? Reinstated? Learn More*, INTERNAL REVENUE SERV. (June 24, 2019), <https://www.irs.gov/charities-non-profits/automatic-revocation-of-exemption> [<https://perma.cc/PP4H-7WA2>] (explaining that the IRS automatically revokes an organization’s tax-exempt status when it fails to file Form 990, 990-EZ, 990-PF or Form 990-N for three consecutive years).

<sup>57</sup> Failing an “organizational” test, which focuses on governing documents out of compliance with nonprofit taxation and governance requirements, would jeopardize tax-exempt status. So, too, would failing to provide sufficient community benefits. However, the IRS has provided minimal guidance about how low the level of benefit would need to be. See Daniel Halperin, *The Tax Exemption Under Section 501(c)(4)* 9–11 (May 2014) (Urb. Inst. Tax Pol’y & Charities Project, unpublished working paper), <https://www.urban.org/sites/default/files/publication/22661/413152-The-Tax-Exemption-Under-Section--c-.PDF> [<https://perma.cc/Y3E4-E57X>].

<sup>58</sup> See I.R.S. Priv. Ltr. Rul. 9315002 (Nov. 5, 1992); see also *Tax Exempt Organization Search (Formerly Select Check)*, INTERNAL REVENUE SERV. (July 2, 2019), <https://www.irs.gov/charities-non-profits/tax-exempt-organization-search> [<https://perma.cc/97Q8-2K6Y>].

<sup>59</sup> See William Gray, *IRS Revokes Dark Money Group Americans for Job Security’s Tax Exempt Status*, ISSUEONE (June 12, 2018), <https://www.issueone.org/irs-revokes-dark-money-group-americans-for-job-securitys-tax-exempt-status> [<https://perma.cc/7NJ5-5FWP>].

illegal conduct.<sup>60</sup> The possibility that the IRS might revoke the exemption of an affiliate would be somewhat greater.<sup>61</sup>

### III. EXPLORATIONS OF LIABILITY UNDER STATE LAW

Imagine that an investigation reveals illegal conduit activity, or that foreign individuals have been convicted of interfering with an election with the willing or careless assistance of a nonprofit—what might a state attorney general do? Using New York as an example, this Part first addresses the power state attorneys general have over nonprofit organizations. It then examines viable theories for establishing accountability, including claims based on duties of obedience and duties of care. Finally, it examines the available remedies for FEC violations, and the imposed limitations.

#### A. *The Powers of State Attorneys General*

In the major jurisdiction of New York, as in other states, the Attorney General is responsible for supervising charitable organizations and has broad independent authority to monitor and investigate nonprofit activities.<sup>62</sup> She

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<sup>60</sup> A confession of guilt for engaging in illegal campaign activity would, of course, substantially overcome difficulties in establishing culpability noted in Part II.C above; conduct of illegal activity is a substantial bar to exemption under IRC 501(c)(4). Engaging in illegal activity may result in a revocation of an organization's tax-exempt status, since such activity is contrary to the organization's operational mandate or mission of social welfare. See INTERNAL REVENUE SERV., *J. Activities That Are Illegal Or Contrary To Public Policy*, in EXEMPT ORGANIZATIONS CONTINUING PROFESSIONAL EDUCATION (CPE) TECHNICAL INSTRUCTION PROGRAM FOR FISCAL YEAR 1985 (1985), <https://www.irs.gov/pub/irs-tege/eotopicj85.pdf> [<https://perma.cc/L6FZ-AVT4>] ("Illegal activities, which violate the minimum standards of acceptable conduct necessary to the preservation of an orderly society, are contrary to the common good and the general welfare of the people of the community and thus are not permissible means of promoting social welfare for purposes of IRC 501(c)(4)."); see also *Publication 557 (01/2019), Tax-Exempt Status for Your Organization*, INTERNAL REVENUE SERV. (Mar. 6, 2019), <https://www.irs.gov/publications/p557> [<https://perma.cc/9H9N-D3B5>] ("If, to carry out its program, an organization violates applicable canons of ethics, disrupts the judicial system, or engages in an illegal action, the organization will jeopardize its exemption."); Eric C. Surette, *Construction and Application of Federal Regulations Governing Retroactive Revocation of Tax-Exempt Status*, 22 A.L.R. Fed. 3d Art. 5 (2017) (discussing cases in which courts applied or construed federal regulations governing retroactive revocation of tax-exempt status). See generally *Partners in Charity, Inc. v. Comm'r*, 141 T.C. 151, 161–63 (2013) (describing revocation of 501(c)(3)).

<sup>61</sup> In our hypothetical case, a foreign donor under existing law could state that it donated to the social welfare organization for general political purposes but not campaign intervention purposes—but whether it in fact did so would be a question of fact. Any claim that it was for general purposes and that receipt of funds was not intended to offset larger campaign contributions would not need to be taken at face value by the IRS or an attorney general.

<sup>62</sup> See, e.g., Press Release, N.Y. State Att'y Gen., Att'y Gen. Underwood Announces Lawsuit Against Donald J. Trump Found. and its Bd. of Dirs. for Extensive and Persistent Violations of State and Fed. Law (June 14, 2018), <https://ag.ny.gov/press-release/attorney-general-underwood-announces-lawsuit-against-donald-j-trump-foundation-and-its> [<https://perma.cc/7M4C-NC9E>]; *Building Better Charities*, ILL. ATT'Y GEN., <http://www.illinoisattorneygeneral.gov/charities> [<https://perma.cc/XS8L-B2AG>] ("Under Illinois law, fundraisers and charitable organizations are required to register each year

is the state's chief legal officer, and as such, "the guardian of the legal rights of [its] citizens . . . its organizations and its natural resources" with subpoena powers.<sup>63</sup> The Attorney General also enforces the election law statutes of the state.<sup>64</sup>

With respect to an attorney general's supervisory authority, her concerns are primarily about overseeing the mission accomplishments of nonprofits and monitoring the governance responsibility of directors and officers. In the hypothetical scenario above, assume that the social welfare organization itself has violated its mission by serving as a conduit; that some of its fiduciaries intentionally made or knew of false statements or omissions on federal and/or state tax returns; and that some senior managers and board members either knew or willfully were ignorant of foreign donations that were intended to enlarge the amount of the nonprofit's political campaign contributions. Under these circumstances, an attorney general could pursue—well within the scope of her authority—a multiplicity of causes of action.

### B. *Contrasting Objectives for Enforcement*

The New York Not-for-Profit Corporation Law is directed, as stated, at ensuring the integrity and effectiveness of nonprofit governance.<sup>65</sup> The FEC rules are, quite naturally, directed at a distinctly different objective: they are principally about promoting the integrity and functionality of the election

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with the Attorney General's office."); *Charities*, STATE OF CAL. DEP'T OF JUST., <https://oag.ca.gov/charities> [<https://perma.cc/JL76-QWL2>] ("The purpose of this oversight is to protect charitable assets for their intended use and ensure that the charitable donations contributed by Californians are not misapplied and squandered through fraud or other means."); *The Attorney General's Non-Profit Organizations/Public Charities Division*, MASS.GOV, <https://www.mass.gov/orgs/the-attorney-generals-non-profit-organizationspublic-charities-division> [<https://perma.cc/NU65-ZCJA>] ("The Non-Profit Organizations/Public Charities Division is responsible for overseeing more than 23,000 public charities in Massachusetts.").

<sup>63</sup> *Divisions and Bureaus*, N.Y. ST. OFF. OF THE ATT'Y GEN., <https://ag.ny.gov/bureaus> [<https://perma.cc/M8QS-M36F>].

<sup>64</sup> N.Y. ELEC. LAW § 3–104 (McKinney 2018); *see also* Press Release, N.Y. State Att'y Gen., A.G. Underwood Announces Election Day Hotline to Protect Voter Access During Tuesday's Gen. Election (Nov. 5, 2018), <https://ag.ny.gov/press-release/ag-underwood-announces-election-day-hotline-protect-voter-access-during-tuesdays> [<https://perma.cc/XY9K-54XA>]. The hypothetical does not suppose that the nonprofit organization corrupted state elections.

<sup>65</sup> N.Y. NOT-FOR-PROFIT CORP. LAW § 204 (McKinney 2014) ("[A] corporation of any kind to which this chapter applies shall conduct no activities for pecuniary profit or financial gain, whether or not in furtherance of its corporate purposes, except to the extent that such activity supports its other lawful activities then being conducted."). This law places great emphasis on good faith dealings. *See* N.Y. NOT-FOR-PROFIT CORP. LAW § 552(b) (McKinney 2014) ("In addition to complying with the duty of loyalty . . . each person responsible for managing and investing an institutional fund shall manage and invest the fund in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.").

process, or, according to some FEC commissioners, about encouraging free and abundant political speech.<sup>66</sup> The FEC test, which must be met to establish culpability for “knowing receipt” of foreign campaign funds,<sup>67</sup> including its safe harbor, aligns more consistently with FEC objectives in promoting the ease and efficiency with which candidates for federal office can raise funds, than it does with evaluating the mission orientation and integrity of a nonprofit. In short, an inquiry by a state attorney general into a nonprofit’s behavior in concealing and misusing foreign-source income would spring from a different predicate, consider different statutory provisions, and use a different calculus for measuring wrongdoing than would be triggered by an FEC investigation.<sup>68</sup>

### C. New York as an Illustration

New York is home to a large array of charitable organizations, and New York state law illustrates the latitude available to attorneys general to pursue officers and directors. Section 112(a) of the New York Not-for-Profit Corporation Law authorizes the Attorney General to take actions and bring special proceedings, including derivative actions, against nonprofit organizations that violate their mission.<sup>69</sup>

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<sup>66</sup> *Mission and History*, FED. ELECTION COMM’N, <https://www.fec.gov/about/mission-and-history> [<https://perma.cc/RT87-F3H3>] (stating FEC mission is “[t]o protect the integrity of the federal campaign finance process by providing transparency and fairly enforcing and administering federal campaign finance laws”); see also Trevor Potter, *Money, Politics, and the Crippling of the FEC: A Symposium on the Federal Election Commission’s Arguable Inability to Effectively Regulate Money in American Elections*, 69 ADMIN. L. REV. 447, 450 (2017) (ideological differences over the interpretation of the law, capture by the major political parties, and deadlock prevent adequate enforcement); Dave Levinthal, *Another Massive Problem with U.S. Democracy: The FEC is Broken*, ATLANTIC (Dec. 17, 2013), <https://www.theatlantic.com/politics/archive/2013/12/another-massive-problem-with-us-democracy-the-fec-is-broken/282404> [<https://perma.cc/5BSQ-VBEX>] (“The Republicans, led by McGahn, insisted the agency should above all ensure the free speech rights of political actors—rights they believe should include the raising and spending of big money to either promote or lambaste political candidates.”); see also *infra* Part IV.

<sup>67</sup> See *supra* notes 33–36 and accompanying text.

<sup>68</sup> See Evelyn Brody, *Whose Public? Parochialism and Paternalism in State Charity Law Enforcement*, 79 IND. L.J. 937, 992 (2004) (“[T]he broad interests of the Attorney General necessarily entail protecting the public against any social and economic *disadvantages* which may be occasioned by the activities and functioning of public charities . . . .”) (internal footnote and quotation omitted).

<sup>69</sup> N.Y. NOT-FOR-PROFIT CORP. LAW § 112(a) (McKinney 2014). The specified actions include: “(1) To annul the corporate existence or dissolve a corporation that has acted beyond its capacity or power or to restrain it from carrying on unauthorized activities; (2) To annul the corporate existence or dissolve any corporation that has not been duly formed; . . . (4) To procure a judgment removing a director of a corporation for cause under section 706 (Removal of directors); (5) To dissolve a corporation under article 11 (Judicial dissolution); . . . (7) To enforce any right given under this chapter to members, a director or an officer of a charitable corporation. The attorney-general shall have the same status as such members, director or officer.” *Id.*

A state attorney general's investigation would focus on whether officers and board members of a nonprofit violated duties of obedience—duties recognized under common law as separate causes of action in New York—and duties of care.<sup>70</sup> Such an exploration would include—but would not necessarily be limited to—the identical conduct evaluated by the FEC, yet would not necessarily be confined by the standards applied by FEC regulations.

The duty of obedience requires that the board work to ensure that the organization complies with applicable laws and regulations, acts in accordance with its own policies, carries out its mission appropriately, and does not engage in unauthorized activities.<sup>71</sup> A board member or officer who condoned or acquiesced to the use of accounting misrepresentations made to conceal the real source of funds; or who concealed or willfully ignored the true purpose of a foreign gift ostensibly donated for general mission purposes; or who reallocated expenses from a mission-related activity to a political campaign contribution after becoming aware of a sudden infusion of foreign-source funds without inquiring into its purpose, would simultaneously undermine respect for law, aid in the corruption of the democratic process, and jeopardize the mission of an organization.

The duty of care requires directors to act “in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.”<sup>72</sup> Assume that a substantial gift of foreign funds was

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<sup>70</sup> Brody, *supra* note 68, at 948 (“In carrying out its supervisory role, the attorney general (or other designated state official), can investigate charges of improper charitable activities, view books and records, and subpoena witnesses.”). Following an investigation, the attorney general has the authority to impose reform mechanisms rather than call for punishment. *Id.* (“Reform rather than punishment is generally the goal of the charity regulator, and board members as well prefer a chance to improve their behavior while avoiding embarrassment and personal liability.”).

<sup>71</sup> See *Manhattan Eye, Ear & Throat Hosp. v. Spitzer*, 186 Misc. 2d 126, 152 (N.Y. Sup. Ct. 1999).

<sup>72</sup> N.Y. NOT-FOR-PROFIT CORP. LAW § 717 (2019); see *Consumers Union of U.S., Inc. v. State*, 806 N.Y.S.2d 99, 118 (N.Y. 2005) (holding business judgment rule does not apply where nonprofit directors breached duty of care); *Kavanaugh v. Gould*, 223 N.Y. 103, 106 (1918) (holding duty of care breached by failure to monitor excessive lending because “[n]o custom or practice can make a directorship a mere position of honor void of responsibility, or cause a name to become a substitute for care and attention”); *S.H. and Helen R. Scheuer Family Found., Inc. v. 61 Assocs.*, 179 A.D.2d 65, 70 (N.Y. App. Div. 1992) (holding business judgment rule would be inapplicable to protect directors if a sizeable majority of the board “failed to possess the independence and disinterested status which is a prerequisite to insulation from [the rule]”); *Epiphany Cmty. Nursery Sch. v. Levey*, No. 654655/2016, 2017 N.Y. Slip Op. 31668(U) at 11, 15 (N.Y. Sup. Ct. Aug. 7, 2017), *aff’d*, 94 N.Y.S.3d 1 (N.Y. App. Div. 2019) (explaining that a director breaches the duty of care by a “‘sustained or systematic failure . . . to exercise oversight’ over the corporation’s activities” and holding duty of care was violated by manager who failed to spot “‘indicia’ of fraudulent financial dealings which ‘were so glaring and flagrant that ‘even the most novice of accountants’ would have recognized and ‘objected to’ them,’ and “[n]o reasonably prudent director could miss the fact that her husband was siphoning millions of dollars . . .”); *Schneiderman v.*

donated to a nonprofit social welfare organization for general activity purposes, and that a segregated campaign fund account simultaneously increased by some corresponding or commensurate amount. In this case, a reasonably prudent director who is aware of these facts may be obligated to take further steps: to use due diligence to become knowledgeable of the affairs of the organization, to inquire further, and to be competently assured that donated foreign funds were not intended to offset increased campaign expenditures by the organization.<sup>73</sup> A board failing to exercise due diligence to identify the true purpose of a massive foreign gift, or worse, deciding to increase its campaign contributions because of a windfall foreign gift, has violated its duty of care.

#### *D. Factors at Play in the Application of Remedies*

A 501(c)(4) organization which attempted to defend itself by asserting that foreign contributions were purely made as general activity gifts would face considerable difficulty if facts demonstrated that it retained the contributed funds for its own general activity and operating purposes and then spent money previously allocated for general purposes on campaign donations, thereby violating FEC rules. The IRS might, conceivably, characterize the transfers themselves as part of a conspiracy to violate election laws or as bribes.<sup>74</sup> The manager or executive director of a campaign fund in this hypothetical also would have negligently violated fiduciary duties of care and obedience by failing to operate the fund in good faith and as a reasonably prudent person would.

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Lower Esopus River Watch, Inc., 975 N.Y.S.2d 369 (N.Y. Sup. Ct. 2013) (adherence is required “to basic fiduciary duties . . . includ[ing] the duty of care”).

<sup>73</sup> See *supra* note 72. If board members—or those upon whom they are entitled to rely—are revealed to know or be willfully ignorant of a large contribution made directly or indirectly by a foreign contributor intended to result in larger contributions being made to political campaigns, the primary element of culpability for a breach of the duty of care will be established. Directors have a duty to be appropriately informed. See *People v. Grasso*, No. 401620/04, 2017 N.Y. Slip Op. 52019(U) at 28 (N.Y. Sup. Ct. Oct. 8, 2006), *aff’d as modified*, 54 A.D.3d 180 (N.Y. App. Div. 2008) (“[T]he Court is acknowledging the fundamental duty of each member of a board to understand the business of the company upon whose board they sit.”); *People v. Cent. Fish Co.*, 101 N.Y.S. 1108 (N.Y. App. Div. 1907). Nonprofit directors, especially those who serve on audit committees, are responsible for ensuring that major gifts are appropriately accounted for and properly spent on mission activities. See, e.g., *Gift Acceptance, Counting and Reporting*, CARNEGIE MELLON U., <https://www.cmu.edu/policies/forms-and-documents/Gift%20Acceptance%20Counting%20and%20Reporting%20Policy.pdf> [https://perma.cc/AD3E-PT2L] (representative policy for gift acceptance, counting, and reporting).

<sup>74</sup> Misreporting bribes as gifts can lead to criminal prosecution for tax fraud conspiracy. See, e.g., Press Release, Dep’t of Justice, U.S. Att’y’s Office, Arrests Made in Nationwide College Admissions Scam: Alleged Exam Cheating & Athletic Recruitment Scheme (Mar. 12, 2019), <https://www.justice.gov/usao-ma/pr/arrests-made-nationwide-college-admissions-scam-alleged-exam-cheating-athletic> [https://perma.cc/9ZNW-TVQ7].

Per Section 112 of the New York Not-for-Profit Corporation Law, the standard for annulling the corporate existence of a nonprofit is not specified by the statute or established by caselaw.<sup>75</sup> If it could be proven that the nonprofit became involved in concealing foreign contributions; engaged in fraudulent accounting; significantly corrupted an election and undermined public faith in the election process; and diminished the chances for success of candidates whose views conflicted with the interests of the nonprofit, then surely these would be sufficient causes to justify annulment.<sup>76</sup>

Beyond annulment, proceedings could be initiated by the Attorney General to remove complicit board members and hold them personally liable for acting in bad faith. Mandating a new election would be beyond the authority of the Attorney General but she could, on tort principles, pursue monetary judgments against responsible officers and directors and against the entity itself, which might be calculated, in theory, according to the provable actual damages to the citizens of the state, enhanced by a punitive amount with a deterrent additur.<sup>77</sup>

Establishing the personal liability of managers and board members would require showing that they personally breached their duty of care or obedience, or “aided and abetted” a breach of a fiduciary duty.<sup>78</sup> Individual corporate directors and officers would not incur personal liability for the torts of their corporation, however, “unless they participate[d] in the wrong or authorize[d] or direct[ed] that it be done.”<sup>79</sup> In the context of a commercial dispute, for example, in *Wantickets RDM, LLC v. Eventbrite, Inc.*,<sup>80</sup> the New

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<sup>75</sup> N.Y. NOT-FOR-PROFIT CORP. LAW § 112 (McKinney 2014).

<sup>76</sup> § 112(a)(1) (“The attorney-general may maintain an action or special proceeding: To annul the corporate existence or dissolve a corporation that has acted beyond its capacity or power or to restrain it from carrying on unauthorized activities . . .”).

<sup>77</sup> See generally Stephen D. Sencer, Note, *Read My Lips: Examining the Legal Implications of Knowingly False Campaign Promises*, 90 MICH. L. REV. 428, 457–63 (1991) (exploring tort damages for false campaign promises).

<sup>78</sup> Derivative actions to address misdeeds of a board could, in New York, be maintained by five percent or more of a membership corporation’s members. N.Y. NOT-FOR-PROFIT CORP. LAW § 623 (2019); see *Segal v. Powers*, 687 N.Y.S.2d 589, 591 (N.Y. Sup. Ct. 1999) (reading § 623 to require that an action be brought by a minimum proportion of members and that the matter first be presented to the board). N.Y. NOT-FOR-PROFIT CORP. LAW § 720-a (2019), which provides broad immunity to directors against third parties in circumstances other than gross negligence or intentional misconduct, does not immunize directors from the reach of federal statutes to the extent the claims are based upon federal law. This section also does not apply to actions taken by the Attorney General or actions commenced under § 719 (director liability in certain defined transactions) or § 720 (actions brought on behalf of the organization).

<sup>79</sup> *Meeker v. McLaughlin*, 2018 U.S. Dist. LEXIS 117211 at \*22 (S.D.N.Y. July 13, 2018); see also *Marine Midland Bank v. John E. Russo Produce Co.*, 405 N.E.2d 205, 212 (N.Y. 1980) (“[C]orporate officers and directors are not liable for fraud unless they personally participate in the misrepresentation or have actual knowledge of it.”).

<sup>80</sup> No. 654277/2016, 2017 N.Y. Misc. LEXIS 2780 (Sup. Ct. July 21, 2017).



York Commercial Division recently denied a motion to dismiss the plaintiffs' claims for aiding and abetting a breach of fiduciary duty, stating that there were sufficient allegations that a manager "provide[d] 'substantial assistance' to the primary violator" in order to plead knowing participation in a breach of fiduciary duty.<sup>81</sup>

A state attorney general does not ordinarily bring criminal charges against board members or organizations, but there have been exceptions. Although uncommon, a state attorney general has the capability to prosecute individual board members when their conduct is evidently criminal. Professor Evelyn Brody writes, "[i]n rare cases, conduct by the organization or individuals rises to the level of criminal activity — for example, the deliberate and flagrant use of an exempt school to convert personal expenditures into deductible charitable contributions."<sup>82</sup> Brody also highlights the possibility of criminal prosecutions for supporting terrorism where fraudulent misreporting to State or Federal agencies plays a role.<sup>83</sup> *United States v. Mubayyid*,<sup>84</sup> for example, upheld an individual's convictions for filing false Form 990s and informational returns, which concealed a jihadist website, newsletter, and orphan sponsorship program for families of martyred mujahideen.<sup>85</sup>

Foundational principles of nonprofit law provide a separate basis for considering whether the organization faces liability for involvement in the corruption of the political process. In the situations discussed above, if an individual or individuals worked inside a nonprofit, in bad faith, to corrupt an election, the state attorney general, responsible for protecting the integrity of nonprofit organizations and the integrity of the election system, would be within the bounds of her role to refer the matter for prosecution to the State's Attorney.

#### IV. INTERJURISDICTIONALITY

The final problem concerns the overlap between federal and state authority, and the argument that the attorney general might be intruding on other jurisdictional authority—that it is traditional for state attorneys general

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<sup>81</sup> *Id.* at \*12–\*13; *see also* *Fitzgerald v. Nat'l Rifle Ass'n*, 383 F. Supp. 162, 167 (D.N.J. 1974) ("No one is entitled to use the *First Amendment* protections as a shield behind which illegal activities are conducted, or legal obligations are shirked.").

<sup>82</sup> Evelyn Brody, *Reforming Tax Policy with Respect to Nonprofit Organizations*, in *RESEARCH HANDBOOK ON NOT-FOR-PROFIT LAW* 484, 493 (Matthew Harding ed., 2018).

<sup>83</sup> *Id.*

<sup>84</sup> 658 F.3d 35 (1st Cir. 2011).

<sup>85</sup> *Id.* at 64–65.

to defer to the IRS or the FEC in matters trenching on federal jurisdiction.<sup>86</sup> In other work, I have argued for the value of more precisely delineating jurisdictional boundaries to encourage enforcement.<sup>87</sup>

There are working relationships which operate to establish priorities for enforcement. State and federal authorities devote their resources in a consistent manner to some enforcement activities rather than others, depending on current events and political philosophies. Such consistency reduces concerns about double jeopardy, over-prosecution, and the like. Regardless of the pressure state authorities may feel to go after a nonprofit for its failure to pay state taxes on unrelated business income, such cases will virtually always be an IRS priority.<sup>88</sup> Conversely, no matter how forcefully the IRS is urged to take up a conflict over the interpretation of a bylaw (unless, perhaps, the bylaw involved discrimination subject to federal civil rights laws or depended on the language of a federal tax provision for its interpretation), or a dispute over governance succession, or a violation of the duty of care or the duty of obedience, state action would probably occur first.<sup>89</sup>

In the situations contemplated, however, federal authorities are not incentivized or adequately empowered to protect important state interests, and the breaches of duty are fiduciary ones, traditionally monitored by state officials.<sup>90</sup> Although the corruption of a national election would normally invoke national regulatory authorities, the implementation of a corrupt and illegal scheme through the misgovernance of a state-chartered nonprofit would present a distinctive, hybrid type of problem.<sup>91</sup>

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<sup>86</sup> See Norman I. Silber, *Nonprofit Interjurisdictionality*, 80 CHI.-KENT L. REV. 613, 618 (2005) (“Today there is, in substance, considerable overlapping enforcement responsibility of the principal state and federal actors, namely the Attorneys General and the Internal Revenue Service.”).

<sup>87</sup> *Id.* at 617–19.

<sup>88</sup> *Id.* at 627 (quoting MARION R. FREMONT-SMITH, GOVERNING NONPROFIT ORGANIZATIONS: FEDERAL AND STATE LAW AND REGULATION xiii (2004)) (“[e]xempt organizations are no longer the stepchildren of the Service . . . who view their role as assuring that exempt charitable organizations continue to make [the] contributions to our society that are the rationale for the special status they are afforded in the tax system.”).

<sup>89</sup> *Id.* at 621 (“Except for federal tax law violations, few types of nonprofit wrongdoing have escaped the purview of an Attorney General’s authority to investigate, and, if warranted, to prosecute miscreants.”).

<sup>90</sup> See Margaret H. Lemos, *State Enforcement of Federal Law*, 86 N.Y.U. L. REV. 698, 726 (2011) (arguing that different incentives and regulatory powers drove then-New York Attorney General Eliot Spitzer to employ state securities law more aggressively than federal authorities who subsequently took action under federal law).

<sup>91</sup> If the attorney general attempted to prosecute election law violations or to challenge federal election procedures, rather than to prosecute breaches of nonprofit fiduciary duty, this analysis would be complicated by constitutional Supremacy Clause and Elections Clause considerations. See FED. ELECTION COMM’N, FEDERAL AND STATE CAMPAIGN FINANCE LAWS 1 (1995), [https://transition.fec.gov/pages/brochures/fed\\_state\\_law\\_brochure.pdf](https://transition.fec.gov/pages/brochures/fed_state_law_brochure.pdf) [<https://perma.cc/M5UK-T5RG>]

## CONCLUSION

Safeguarding the election process from foreign interference in elections has been documented as a pressing matter.<sup>92</sup> Federal resources have been marshalled and legal authorizations strengthened to address some of the emerging threats.<sup>93</sup> Further statutory and regulatory reform has not yet been directed to the vulnerability to abuse as conduits of nonprofit organizations.<sup>94</sup>

In the absence of such reforms, it appears that federal election rules, money laundering statutes, tax laws, and election rules are inadequately suited to safeguarding the integrity of the nonprofit sector. Perhaps counter-intuitively, this Essay therefore argues that federal efforts to hold nonprofit social welfare organizations accountable are likely to be less effective in protecting broad public interests than the existing rules that authorize state attorneys general to act. State authorities can hold accountable officers and directors who let nonprofits become vehicles for foreign interference in national elections—as well as the organizations themselves.

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(explaining brochure was designed to help “determine whether federal or state laws govern a particular election activity”); *see also* *Gonzalez v. Arizona*, 677 F.3d 383, 394 (9th Cir. 2012) (citing *Foster v. Love*, 522 U.S. 67, 74 (1997)) (providing an approach for reviewing state election voter registration procedures, specifically when state legislation affecting federal voter registration procedures are reviewed pursuant to the Elections Clause rather than preemption analysis under the Supremacy Clause, and where “Congress addressed the same subject as the state law, we consider whether the federal act has superseded the state act, based on a natural reading of the two laws and viewing the federal act as if it were a subsequent enactment by the same legislature”). Under a preemption analysis, “Congress does not cavalierly pre-empt state-law causes of action.” *Id.* at 392 (quoting *Wyeth v. Levine*, 555 U.S. 555, 566 n.3 (2009)).

<sup>92</sup> *See, e.g.*, 1 ROBERT S. MUELLER, III, U.S. DEP’T OF JUSTICE, REPORT ON THE INVESTIGATION INTO RUSSIAN INTERFERENCE IN THE 2016 PRESIDENTIAL ELECTION 50 (2019), [https://www.justice.gov/storage/report\\_volume1.pdf](https://www.justice.gov/storage/report_volume1.pdf) [<https://perma.cc/HW6U-H43S>] (documenting intrusions targeting the administration of U.S. elections); U.S. S. COMM. ON FIN. MINORITY STAFF REP., THE NRA AND RUSSIA: HOW A TAX-EXEMPT ORGANIZATION BECAME A FOREIGN ASSET 75 (Sept. 2019), <https://www.documentcloud.org/documents/6430090-The-NRA-Russia-How-a-Tax-Exempt-Organization.html> [<https://perma.cc/2ZFN-3X9N>] (“This report illustrates potential weaknesses related to potential misuse of tax-exempt resources by section 501(c)(4) organizations and how such misuse can expose an organization to improper influence.”).

<sup>93</sup> Regarding authorizations, *see, e.g.*, John S. McCain National Defense Authorization Act for Fiscal Year 2019, Pub. L. No. 115-232, § 1642(a), 132 Stat. 1636, 2132 (2018) (authorizing active cyber defense measures against Russia, China, Iran, and North Korea); Philip Bump, *What’s Russia Still Doing to Interfere With U.S. Politics—And What’s the U.S. Doing About It?*, WASH. POST (May 3, 2019), [https://www.washingtonpost.com/politics/2019/05/03/whats-russia-still-doing-interfere-with-us-politics-whats-us-doing-about-it/?utm\\_term=.6ca81a1e41e5](https://www.washingtonpost.com/politics/2019/05/03/whats-russia-still-doing-interfere-with-us-politics-whats-us-doing-about-it/?utm_term=.6ca81a1e41e5) [<https://perma.cc/9W25-49ML>] (assessing potential for interference in 2020 election cycle).

<sup>94</sup> U.S. S. COMM. ON FIN. MINORITY STAFF REP., *supra* note 92, at 75 (recognizing the “potential weaknesses to foreign intelligence threats by American tax-exempt organizations” and suggesting that Congress further reform the current tax-exempt laws by promoting increased disclosure requirements and information reporting, and strengthening campaign finance rules to protect against foreign intrusions).