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# Congress of the United States

## U.S. House of Representatives

COMMITTEE ON WAYS AND MEANS

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February 27, 2014

The Honorable Jack Lew  
Secretary  
Department of the Treasury  
1500 Pennsylvania Avenue, N.W.  
Washington, DC 20520

The Honorable John Koskinen  
Commissioner  
Internal Revenue Service  
CC:PA:LPA:PR (REG-134417-13), Room  
5205  
1111 Constitution Avenue N.W.  
Washington, D.C. 20224

Dear Secretary Lew and Commissioner Koskinen:

As members of the Committee on Ways and Means, we are writing to express our strong opposition to the November 29, 2013, Notice of Proposed Rulemaking, "Guidance for Tax-Exempt Social Welfare Organizations on Candidate-Related Political Activities."<sup>1</sup> This rulemaking should be abandoned because: 1) it has been put forward based on a demonstrably false premise, 2) its construction will restrict the free speech of citizens and the groups with which they associate, and 3) it is premature in light of the ongoing investigations.

### **The proposed rule is based on a demonstrably false premise.**

The proposed new rule cites "confusion for both the public and the IRS in making appropriate section 501(c)(4) determinations," as the reason for changing a rule that has been in force since 1959.<sup>2</sup> This rationale is quoted from a hastily written IRS report, "Charting a Path Forward at the IRS: Initial Assessment and Plan of Action," (hereafter the "Werfel Report"), that was prepared before the IRS was able to question those employees involved.<sup>3</sup> At Treasury Secretary Lew's direction, then-Acting IRS Commissioner Danny Werfel undertook a thirty-day review of the agency in

<sup>1</sup>78 FR 71535 (proposed November 29, 2013).

<sup>2</sup>78 FR 71536.

<sup>3</sup> Daniel Werfel, "Charting a Path Forward at the IRS: Initial Assessment and Plan of Action," (June 24, 2013).

response to Treasury Inspector General for Tax Administration's (TIGTA) findings that the IRS had targeted organizations based on name and policy position.<sup>4</sup> The Werfel Report's conclusion that confusion led to the targeting thereby necessitating this rule change is refuted by evidence the Committee has uncovered in its ongoing investigation.

In late 2009 through early 2010, Tea Party applications were being received by the Cincinnati-based IRS field office, processed and approved without delay or intrusive questionnaires.<sup>5</sup> However, in late February 2010, a screener in Cincinnati began to flag Tea Party applications for his superiors' attention because of "possible media interest."<sup>6</sup> In the initial messages of the email chain, the revenue agent and his immediate boss correctly cited the applicable law and regulations.<sup>7</sup> Within twenty-four hours, news of these cases was transmitted to Holly Paz, then-Director of Rulings and Agreements of the IRS' Exempt Organizations (EO) unit located in Washington, D.C. Paz responded:

Thanks for the heads up.... I think we should take a few more cases...and would ask that you [Cincinnati] hold the rest until we get a sense of what the issues may be.<sup>8</sup>

The then head of the Exempt Organization Unit, Lois Lerner, would later affirm this decision, not because of confusion, but because the Tea Party was "dangerous." Lerner told subordinates:

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<sup>4</sup> TIGTA Audit Report, "Inappropriate Criteria Were Used to Identify Tax-Exempt Applications for Review" (May 14, 2013). The TIGTA report actually did recommend for Treasury and the IRS to publish guidance on how to measure political activity. The new proposed rule does not address this other than to invite comment. A colloquy between Ways and Means Member Kevin Brady and Thomas Barthold, Chief of Staff to the Joint Committee on Taxation, on February 11, 2014 during a mark-up of H.R. 3865 illustrates the difference:

Mr. Brady: Mr. Barthold, a question. The Inspector General did recommend some rules related to this area, but his focus was on the measurement of the social welfare activities. Does the proposed new – and that's a big distinction from what this rule does, a major distinction from it. So, does this proposed new rule provide any specific rules on how to measure social welfare activity?

Mr. Barthold: The proposed regulations do not address the issue of determining what's primary.

Mr. Brady: So the recommendations from the Inspector General, who revealed the targeting in the first place, isn't even present in this rule, is that correct?

Mr. Barthold: Again, you're correct. It doesn't address the measurement issue.

<sup>5</sup> See, e.g., Amarillo Tea Party Patriots (received by the IRS office in Cincinnati, OH December 22, 2009; approved February 20, 2010) and Champaign Tea Party (received November 9, 2009; approved February 20, 2010).

<sup>6</sup> IRSR00000181003-7. According to the Internal Revenue Manual (IRM), revenue agents are to flag cases that are "likely to attract media...attention [or] presents unique or novel issues," among other things. IRM 7.29.3.2(2)(C)(07-14-2008), "Processing of Cases by Tax Law Specialists (TLS)."

<sup>7</sup> IRSR00000181003-7.

<sup>8</sup> *Id.*

Tea Party Matter very dangerous. This could be the vehicle to go to court on the issue of whether Citizen's United overturning the ban on corporate spending applies to tax exempt rules. Counsel and Judy Kindell [Lerner advisor] need to be in on this...Cincy should probably NOT have these cases --Holly please see what exactly they have please.<sup>9</sup>

The initial cases flagged in late February 2010, and nearly two hundred more received thereafter, were screened out and set aside at the direction of Washington, D.C. for two years or more. Confusion was never asserted as a factor in the use of the inappropriate selection criteria.

The Werfel Report, on which the draft rule is premised, is deficient because it was not based on any meaningful fact-finding by the agency. At a June 27, 2013, Ways and Means Committee hearing concerning the report, Mr. Werfel conceded that the agency was not conducting employee interviews and was relying on documents requested by Congress for its internal review:

Chairman Camp. Is the IRS interviewing employees who were directly involved with the Tea Party discrimination at this point?

Mr. Werfel. Right now, the IRS is relying on the Justice Department and the Inspector General to conduct those interviews. We are working closely with them. But it is critical that, because there is an ongoing criminal investigation, that we do not step in front of the Justice Department and the IG at this time.<sup>10</sup>

The failure to question employees directly involved in the targeting renders any conclusion in the Werfel Report deficient. Therefore, this report should not be used as the basis for the proposed rule.

Although the Committee's investigation of IRS targeting is not complete, the differences between it and the Werfel Report are stark. The Committee's investigation has spanned over nine months. The Committee has interviewed almost three-dozen IRS employees, from line screeners in Cincinnati to former Commissioner Shulman. The Committee has reviewed nearly 400,000 internal IRS documents. The Committee has held five public hearings and has heard testimony from IRS officials, like former Acting Commissioners Miller and Werfel, current Commissioner Koskinen, as well as victims of the targeting.

Evidence the Committee's investigation has uncovered not only refutes the claim of confusion as justification for the rule, it also establishes that Treasury and the IRS were secretly working on the rule as early as 2011, long before a finding of confusion was put forward.<sup>11</sup> In a June 2012 email, a lawyer in Treasury's Office of Tax Policy forwarded

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<sup>9</sup>IRSR00000156550.

<sup>10</sup>Committee on Ways and Means Hearing on the Status of Internal Revenue Service's Review of Taxpayer Targeting Practices, June 27, 2013.

<sup>11</sup> Transcribed interview of Janine Cook, at 36, Internal Revenue Serv., in Wash., D.C. (Sept. 9, 2013)(stating that "In spring 2011, we started informal conversations about looking at the issue of political activity in (c)(4), (5)s, (6)s, (3)s, the gamut".)

an article to Lois Lerner and others at the IRS with the message:

Don't know who in your organizations is keeping tabs on c4s, but since we mentioned potentially addressing them (off -plan) in 2013, I've got my radar up and this seemed interesting...<sup>12</sup>

“Off-plan” means excluded from the Treasury’s Priority Guidance Plan. According to the IRS, “[t]he Guidance Priority List focuses resources on guidance items that are most important to taxpayers and tax administration.”<sup>13</sup> Presumably, the first change to a 54 year-old regulation would be considered to be among the “most important to taxpayers and tax administration,” but Treasury and the IRS chose to cloak their work. Nowhere in this document is confusion cited for this “off-plan” rulemaking.

The purpose of the rulemaking process is to give the public fair notice and the reason for a rule or rule change. This proposed rule is based on a demonstrably false premise, which raises questions about the integrity of the proposed rule. Basing a rule on a false premise is an abuse of rulemaking discretion given to Treasury and the IRS by Congress.

**The construction of the proposed new rule will restrict the free speech of citizens and the groups with which they may freely associate.**

The construction of the proposed new rule will restrict the free speech of citizens and the groups with which they may freely associate under the Constitution. The stated governmental interest in the rulemaking is clarity. This purported governmental interest in clarity must be weighed against the fundamental First Amendment freedoms of speech and association.<sup>14</sup> Given that the government’s stated interest has been shown to be unsubstantiated, it is unclear upon what basis Treasury is infringing upon these fundamental rights. The proposed rule does not, for example, implicate any government interest in lost revenue.<sup>15</sup>

Under current law, 501(c)(3) charitable organizations receive tax deductible donations, and in exchange for this valuable benefit, must agree to forego any political activity. The

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<sup>12</sup> IRS0000305906.

<sup>13</sup> <http://www.irs.gov/uac/Priority-Guidance-Plan> visited February 22, 2014.

<sup>14</sup> Pursuant to Executive Order 13563, issued by President Obama on January 18, 2011: [E]ach agency must, among other things: (1) propose or adopt a regulation only upon a reasoned determination that its benefits justify its costs...[and]; (2) tailor its regulations to impose the least burden on society, consistent with obtaining regulatory objectives...”

<sup>15</sup> At the mark-up of H.R. 3865 on February 11, 2014, the Committee on Ways and Means Chairman Dave Camp and Thomas Barthold, Chief of Staff to the Joint Committee on Taxation engaged in the following colloquy:

Chairman Camp: Do these proposed regulations respond to some kind of revenue loss or some tax avoidance scheme?

Mr. Barthold: Not that I'm aware of, sir. These organizations are generally exempt and a revenue loss has not been identified as the basis for the proposed regulations.

IRS has provided extensive guidance on what is/is not political activity for a 501(c)(3). Consider the following example from an IRS revenue ruling:

A section 501(c)(3) organization that promotes community involvement, sets up a booth at the state fair where citizens can register to vote. The signs and banners in and around the booth give only the name of the organization, the date of the next upcoming statewide election, and notice of the opportunity to register. No reference to any candidate or political party is made by the volunteers staffing the booth or in the materials available at the booth, other than the official voter registration forms which allow registrants to select a party affiliation. [The organization] is not engaged in political campaign intervention when it operates this voter registration booth.<sup>16</sup>

Under current law, voter registration activities as described above are not political activity for 501(c)(3) organizations and likewise are not political activity for 501(c)(4) social welfare organizations, 501(c)(5) unions and 501(c)(6) chambers of commerce. However, under the proposed rules, voter registration activities would *per se* be political activity only for 501(c)(4) social welfare organizations. There is no explanation why get out the vote efforts and candidate forums in advance of an election should now be considered as political activity for only 501(c)(4) organizations.

The Committee has heard from victims of the IRS targeting, received reports by organizations affected by the proposed rule, and reviewed hundreds of applications for exempt status. Based on this background, it is clear that the regulation disproportionately impacts the same kind of conservative 501(c)(4) groups that were inappropriately targeted by the IRS. Indeed, under the proposed regulation, many of these groups would no longer be able to operate under this section of the Code because they are primarily engaged in activities now excluded from the definition of social welfare. While the proposed rule is being put forward to address the cause behind the Tea Party targeting, it has the effect of restricting the free speech of the very same kinds of groups.

### **The proposed rule is premature.**

While the proposed rule purports to address the cause of the targeting, investigations into the targeting by TIGTA and Congress have yet to be completed. And more, there is no compelling need to expedite the rulemaking because neither current law nor the proposed new rule affects revenue.<sup>17</sup> The Committee has yet to receive all relevant documents from the IRS, and several interviews are outstanding. Unfortunately, the IRS is prolonging the investigation by refusing to produce to the Committee all Lois Lerner emails from the period of January 1, 2009 forward. Only after the Committee has access to all pertinent documents can it conclude its investigation.

At present, our review into the targeting has not uncovered facts establishing the need to change current law. Treasury's race to publish the proposed regulations based on a

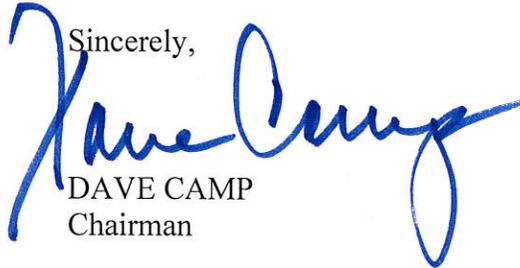
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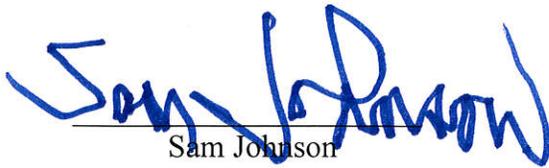
<sup>16</sup> Internal Revenue Bulletin: 2007-25 (June 18, 2007) Rev. Rul. 2007-41.

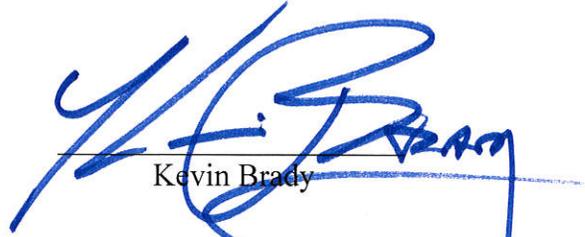
<sup>17</sup> See n15.

flawed premise, focused only on one class of exempt organizations, and before the investigations have been completed, has the appearance of trying to affect the upcoming 2014 elections. We ask that you abandon the rulemaking entirely, but at a minimum, do not finalize the proposed rule for at least a year to allow the investigations to be completed and for the public to fully weigh in on the proposal.

The foregoing are our reasons for opposing the new proposed rule.

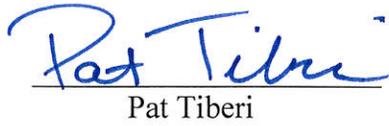
Sincerely,  
  
DAVE CAMP  
Chairman

  
Sam Johnson

  
Kevin Brady

  
Paul Ryan

  
Devin Nunes

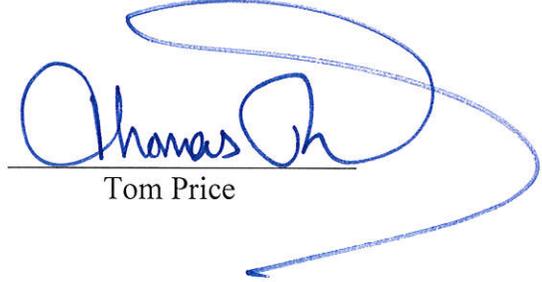
  
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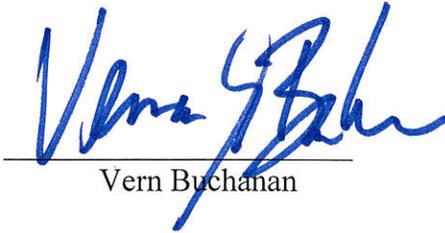
  
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Diane Black



Tom Reed

*Todd Young*

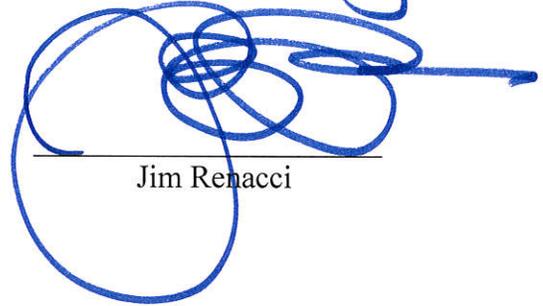
Todd Young

*Mike Kelly*

Mike Kelly

*Tim Griffin*

Tim Griffin



Jim Renacci