

Dark Money in Arizona: The Right to Know, Free Speech and Playing Whack-a-Mole

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Dark money.

The name itself carries ominous undertones, undertones that critics of this relatively new campaign-finance phenomenon claim reflect a genuine threat to democracy. Its defenders, on the other hand, argue that the dark money approach to funding political campaigns is merely an extension of Americans' basic right to free speech.

In other words, the issues at hand could hardly be more profound.

Dark money refers to the infusion of large amounts of money into political campaigns by corporations, business associations, unions and wealthy individuals who refuse to be publically identified. Political operatives launder these undisclosed funds through complex networks of organizations, including many nonprofit corporations.

Dark money has shown up in federal, state and local elections in Arizona and elsewhere, serving up what some see as an "equal-opportunity election influencer."¹ Nor is the practice limited to elections. Groups have used it to try to shape views on policy issues and to support lobbying. Meanwhile, efforts to get a handle on it have been controversial and thus far unsuccessful.

A Historic Supreme Court Decision

The flow of dark money increased dramatically following the U.S. Supreme Court's 2010 decision in *Citizens United v. Federal Election Commission*. This decision erased limits on how much corporations, unions and other organizations can directly spend for or against candidates for office through campaign advertising. More broadly, the court ruled in favor of a system of unlimited spending by outside groups acting independently of the candidates they support.

Encouraged by the decision, many corporations and wealthy individuals raised their contributions to outside political campaigns. Some chose to work through Super PACs, a type of political-action committee that came into being as the result of the *Citizens United* ruling. Others chose to go through non-profit tax-exempt entities formed under the U.S. Internal Revenue tax code.

Social welfare organizations, organized under Section 501 (c) (4) of the tax code, have been of particular use to those who would hide the identity of donors. These non-profit entities may engage in political activities without donor disclosure as long as their primary purpose remains social welfare. Tax experts have commonly taken this to mean that at least 51 percent of their activities must fall into the social-welfare category.

Social welfare nonprofits frequently pass along funds to other organizations, funds that may wind up in the coffers of Super PACs or committees working for or against particular candidates or ballot measures. These organizations must report where they get their money. However, when the money comes from a nonprofit, they must only disclose the name of the nonprofit, leaving the original source of the money "dark."

"I firmly believe that anonymous political speech is not a danger to our nation – it has played an important role throughout our history. Anonymity in political speech protects the speaker from retribution, but it also serves a greater good: it allows the public to listen to ideas without any bias toward the messenger."

– **Sean Noble**, president of the Center to Protect Patient Rights, "Left seeks to intimidate and silence conservative non-profits," *Arizona Republic*, Feb. 23, 2014

"Arizona elections are becoming thoroughly consumed by such anonymous spending, known as 'dark money.' It overwhelmed spending on the race for U. S. Senate here as well as nearly all the contested congressional races and many legislative races."

– **Doug MacEachern**, columnist, *Arizona Republic*
Jan. 12, 2013

In the 2011-2012 cycle, \$1.3 billion of the \$7 billion spent on federal elections came from groups operating independently of any candidate's committee. Close to half of the outside spending came from Super PACs, while much of the rest – some 46 percent of the total – came from dark money groups, principally non-profit social-welfare groups. The growth in dark money use has been impressive: Dark money nonprofits spent \$336 million on presidential and congressional campaigns during the 2012 election cycle. In 2006, such groups reported less than \$6 million on federal campaign spending.²

Though dollar totals are lacking, many of the organizations spending on federal elections also spend lavishly on state and even local elections. Large corporations and wealthy individuals have poured millions into politically active nonprofits through shell corporations formed in states where disclosure laws are minimal or non-existent. In these states, the only donor on record is the shell company.

The complex systems built to launder funds through a variety of organizations to avoid donor disclosure resemble sets of Russian nesting dolls, where a series of hollow wooden figures fit inside larger ones. The process means that voters seeking the identities of campaign donors encounter organization after organization listing other organizations as the source of the funds.

Political operatives and fund-raisers have found that a “no-disclosure-of-donors promise” helps greatly in bringing in money for candidates or political causes. It also allows political operatives to portray their organizations as enjoying widespread “grassroots” support, when in fact they depend on the support of one or two wealthy contributors.

Initially, most of the dark money came from the conservative side. Gathering much media attention, for example, has been the chain of non-profits linked to billionaire industrialists David and Charles Koch. Liberal organizations, however, appear to be rapidly catching up.³ Dark money now flows into national, state, and local elections from the both the left and the right. Liberals worry about right-wing organizations, including Americans for Prosperity in the Koch network. Conservatives, on the other hand, worry about union contributors, organizations like the League of Conservation Voters and progressive big-money donors such as billionaire George Soros.

California Revelations: The Arizona Connection

The issue of dark money captured national headlines in 2013, when California’s political campaign watchdog agency, the Fair Political Practices Commission (FPPC), exposed a network through which nonprofit organizations funneled \$11 million to influence voters on ballot propositions in California’s 2012 election.

The FPPC suspected something was amiss in October 2012 when Americans for Responsible Leadership (ARL), an obscure Arizona-based 501 (c) (4) nonprofit headed by former Arizona House Speaker Kirk Adams and with no history of political activity in California, contributed funds to two political action committees there. One committee supported an anti-union initiative and the other opposed a tax increase, both on the California ballot in 2012.

The money, ultimately spent on political advertising, came to ARL through a convoluted network of dark money nonprofit groups in Virginia and Iowa

“With its aggressive elections commission asserting serious-minded disclosure requirements, California proved that states do not have to meekly allow anonymous ‘independent expenditure’ groups with limitless funds to control their elections.”

– **Editorial**, *Arizona Republic*,
Oct. 25, 2013

associated with the Koch brothers. Another Arizona nonprofit in the Koch network, the Center to Protect Patient Rights, headed by Sean Noble, an aide to former Arizona Congressman John Shadegg, was also involved in the distribution of funds into the California campaigns in what the FFPC said amounted to a money-laundering scheme.⁴

The California venture did not turn out well for the Kochs. The dark money organizations lost both proposition fights, and a court forced organizers to reveal the names of some of the donors. More important, the revelations prompted a nationwide inquiry into the dark money issue and brought pressure in Washington, D.C. and state capitols to do something to require timely disclosure of donors.

Developments in Arizona

Millions of dark money dollars have been sloshing around Arizona, much of it from out-of-state donors. In 2012, it showed up in congressional contests and state legislative races; in 2013, it surfaced in Phoenix's municipal elections. Ballot measures have also been involved. For example, Americans for Responsible Leadership was active in Arizona as well as California in 2012, spending around \$1.6 million to defeat propositions that would have created a "top-two" primary system and extended Arizona's temporary 1-cent sales-tax increase.

In 2011, Noble's organization in the Koch network helped fund an organization known as Fair Trust in Arizona. Lawyers for this group attempted to influence the Arizona Independent Redistricting Commission's creation of new maps for state legislative and congressional districts. At the time, the group refused to reveal its donors, despite repeated requests from some commission members.⁵

In 2013, Arizona Public Service Company admitted having given two nonprofits close to \$4 million to run ads concerning net-energy metering – an issue in dispute between APS and the solar-power industry. The two nonprofits, 60+ and Prosper, were also associated with Noble.

That year, dark money was also behind television ads and mailers by the Arizona Public Integrity Alliance that were critical of Attorney General Tom Horne for alleged campaign-finance misconduct. Secretary of State Ken Bennett dismissed a complaint against the group, finding that the Arizona Public Integrity Alliance was a nonprofit organization that does not have to report

"People have the right to play in the political arena . . . They don't have the right to hide who they are."

– **Sen. Steve Farley**, D-Tucson, a sponsor of a measure aimed at dark money. Quoted by Sean Peick, Cronkite News Service, "Measure would shed light on 'dark money,'" *Mohave Valley Daily News*, Feb. 4, 2013

where its money comes from. Moreover, Bennett concluded, the group did not even have to report how much it was spending on the ads because they fell into the category of issue advocacy, rather than electioneering.

Until recently, little attention has been paid to the nonprofit dark-money groups that register with the Arizona Corporation Commission. Many of them appear quickly, register with the Commission, and just as quickly disappear after Election Day because their work is over.⁶ As evidenced in the California revelations,

some of these have been active not only locally but in other states.

A Range of Responses

In the 2013 legislative session, state Democrats proposed forcing disclosure of dark money donors to nonprofits; their bills, however, found little traction in the Republican-controlled Legislature. By 2014, though, members of both parties expressed support for greater disclosure. State Sen. Michele Reagan, R-Scottsdale, chair of the Senate Elections Committee, sponsored a measure (SB1403) that would require independent expenditure committees in state and local elections to reveal the “identifiable contributors” to their campaigns, even though these funds came to them through a chain of organizations.

The “identifiable contributor” noted in the bill is the specific person(s), corporation(s), or union(s) from within or outside of Arizona that makes the initial donation, not some vaguely named entity that passed the funds along. The independent committee would also be required to reveal the name of the leading three financiers in its campaign advertisements, literature and similar materials.

A central focus of SB1403 is on Arizona’s many shell corporations or “convenience corporations” that seek to influence elections without revealing the identity of their funders. The bill outlaws attempts to hide the identity of donors by the creation of such entities and by funneling funds from one organization to another. To enforce the law, the Secretary of State, acting upon a complaint, would have wide authority to determine if a group or organization is primarily engaged in electioneering. If so, it would be regulated as a political committee and be subject to disclosure.

Critics of SB1403 argued that the bill gives too much power to election officials and would accomplish little more than produce a chilling effect on free speech. By the middle of February 2014, the bill had stalled in the Senate, failing to get out of committee. Reagan lashed out at lobbyists for the Arizona Chamber of Commerce, the Arizona Federation of Labor and other groups opposing the bill.

“They don’t want this discussion,” Reagan said. “They don’t want to change. They want status quo. . . Their clients do not want us to see what they’re doing.”⁷

National and State Remedies

Ultimately, the search for effective solutions to the dark money problem will depend heavily on what happens in the nation’s capitol. Thus far, Congress has sputtered in its effort to bring greater disclosure. A proposed DISCLOSE (*Democracy Is Strengthened by Casting Light On Spending in Elections*) bill, which would require disclosure of the names of those giving more than \$10,000 (in its latest version) to independent expenditure groups, including non-profits, has yet to secure the necessary support.

Those seeking reform have also called upon various federal agencies to take actions that would enhance disclosure. Critics have faulted the Federal Election Commission, U.S Internal Revenue Service, Federal Communications Commission, and Securities and Exchange

Commission for creating or contributing to the dark money problem, and have asked them to take corrective steps.⁸ Late in 2013, the IRS began moving toward containing somewhat the political activities of the nonprofits, but these efforts have encountered considerable opposition.

Because of U. S. Supreme Court decisions, states cannot do anything to prevent corporations, business associations, unions or other groups or individuals from spending all they want on political campaigns. Nor can states alter federal tax or campaign laws. The California episode demonstrates, however, that states are not powerless in this arena. They can act to enforce disclosure rules on nonprofit and other entities that are attempting to influence state and local elections

Thus far, state legislators have been less concerned with disclosure than with the fact that spending by independent dark money groups has been rapidly increasing. Seeking to counter the influence of independent groups, many state lawmakers have increased the amount of money individuals can contribute to legislative and other campaigns. Sponsors of increasing limits have argued that candidates for state office need more money to compete with outside dark money organizations. On this matter, there seems widespread agreement among Republicans and Democrats. In 2013 alone, legislatures in eight states including Arizona approved higher limits. Several more are poised to do so.⁹

In some states, legislators have coupled higher contribution limits with donor disclosure. Watchdog groups contend, however, that allowing more disclosure should not come at the cost of allowing more money to flow directly to candidates from wealthy donors. To them, both disclosure and strict campaign contribution limits are necessary.¹⁰

The need for donor disclosure has caught the attention of state attorneys general, election officials and legislators throughout the country. Some have called for laws along the lines of the proposed DISCLOSE Act. In California, a bill of this nature is currently awaiting the governor's signature. It strengthens an already strong set of laws by giving the FPPC more authority to require tax-exempt political nonprofits to reveal their donor lists.

In 2012, Rhode Island passed a law requiring certain tax-exempt organizations to reveal the names of the top five top donors to issue ads aired in state candidate or ballot elections, and to publically disclose the names of those contributing \$1,000 or more to the organization. Utah, responding to a scandal involving dark money, passed a law that requires corporations, including nonprofits, to disclose their donors if their spending on election campaigns exceeds \$750.

"The reality is that disclosure [of donors] is probably one of the most harmful forms of regulation to political discourse in the United States and it achieves almost nothing that its proponents claim."

– **Bill Maurer**, director of the Institute for Justice's Washington state office, a non-profit, public-interest, libertarian, law firm. Quoted in Robert Gehrke, "Does Utah law trample free speech in campaigns?" *Salt Lake Tribune*, Jan. 22, 2014

Early in 2014, there was considerable interest expressed in a proposal in the Washington State legislature that would have required nonprofits that spend \$100,000 or more in statewide races, or more than \$20,000 in local races, to disclose donors of \$2,000 or more. Legislative leaders, however, refused to bring the bill to the floor for a vote. It appeared that many legislators did not want to go on record against disclosure, preferring instead to let the issue become lost in the process without a formal vote.¹¹ Similar maneuvers appear to have been used in other states, including Arizona.

Pros, Cons and Prospects

Requiring donor disclosure has long been a cornerstone of state governments' efforts to regulate campaign spending. Indeed, Arizona's first governor, George W.P. Hunt, led the charge. He argued that Arizonans suffered because of behind-the-scenes manipulations by wealthy business leaders out to further their own interests. Hunt's campaign against this "invisible government" led to reform proposals calling for more public disclosure of those behind campaign and lobbying activities.

Modern-day proponents of disclosure argue that they are not seeking to prevent speech, but only to let the public know who is speaking. A related argument is that people – corporations included – should be willing to stand up for what they believe. Although their views may be unpopular, this argument continues, laws exist to prevent retaliation for what they say.¹² Opponents of mandatory disclosure, on the other hand, contend that disclosure requirements have a chilling effect on the right of free speech guaranteed by the First Amendment of the U.S. Constitution. Disclosure requirements, they say, may make some citizens less willing to speak out for fear of harassment for airing their views. This, they argue, discourages political participation and the full airing of views that should be heard in the public policy marketplace.

Many corporate leaders value anonymity because of concerns about what their shareholders, employees and customers might think about their taking a stand on a candidate or issue.

Backlashes such as boycotts are a possibility. Business leaders too may be wary of possible retaliation from unions or public officials. In fact, leaders of the U.S. Chamber of Commerce and many large corporations have viewed the demand for more disclosure as essentially an effort from the Left to diminish the influence of the business community in the policymaking arena.¹³

"I think it's really important that we allow our citizens and voters to see (who's) paying for different campaigns. I have to, as a candidate, disclose who's contributing to me. It seems like a no-brainer that if a group is spending money that the citizens have a right to be able to see where that money's coming from . . ."

– **Sen. Michele Reagan**, R-Scottsdale, quoted by Jeremy Duda, "Dark Money, Specter of anonymous campaign spending looms over 2014," *Arizona Capitol Times*, Nov. 22, 2013

However, some companies see value in disclosure. A recent study by the Center for Public Integrity, a nonprofit, nonpartisan watchdog organization, found that about a third of the Fortune 300 companies voluntarily disclose their contributions to politically engaged nonprofits. They see transparency as a good business practice for building the reputation and image of the corporation and for

promoting public trust.¹⁴

Disclosure of dark money donors is a relatively new area for the states. It is also one marked by considerable uncertainty over what can and should be done, and by considerable political resistance. The laws that do exist are largely works in progress. The legislative road ahead is likely to be one of trial and error, as lawmakers move toward effective remedies that can withstand political and legal challenges. Meanwhile, dark money is likely to play an increasingly important role in elections, as is already apparent concerning the 2014 campaigns.¹⁵

Opponents of disclosure commonly cite the difficulty of passing truly effective legislation against it. They argue that trying to do so is like playing the popular “Whack-a-mole” game: As one avenue of autonomous spending is forced down, another pops up. Faced with new obstacles, opponents say, wealthy donors may well find a way to game the system or circumvent the law through other means. In the end, for example, they might disclose more but also increase their influence on policy by raising their direct contributions to candidates.

What should Arizona do? Questions surrounding donor disclosure, free speech rights and contribution limits remain much in dispute. But few on either side of the debate would deny that the issues involved are vital to a healthy political system.

NOTES

¹ E-mail from Paul Ryan, longtime Arizona political activist, Jan. 30, 2014

² “FEC Summarizes Campaign Activity of the 2011-2012 Election Cycle,” Federal Election Commission News Release, April 19, 2013, found at http://www.fec.gov/press/press2013/20130419_2012-24m-Summary.shtml); and “Outside Spending, Political Non-Profits” Open secrets.org found at http://www.opensecrets.org/outsidespending/fes_summ.php?cycle=2012

³ Robert Maguire, “Liberal Dark Money Dominating 2014 Elections,” OpenSecrets.org, Nov. 7, 2013. : <http://www.opensecrets.org/news/2013/11/liberal-dark-money-dominating-2014-elections.html>)

⁴ Local coverage of California case is found in Yvonne Wingett Sanchez and Ryan Randazzo, “Calif. Fines Ariz. Non-profits,” *The Arizona Republic*, Oct. 25, 2013. Later a report by ProPublica, a nonprofit investigative journalism organization, highlighted Noble’s central role in distributing \$137 million in anonymous campaign spending in 2012 in California and elsewhere. See Kim Baker and Theodor Meyer, ProPublica, “How a former Arizona congressional aide ...” *The Arizona Republic*, Feb. 19, 2014

⁵ Baker and Meyer, “How a former congressional aide.” See also: Jeremy Duda, “Koch ‘dark money’ network helped fund GOP redistricting group FAIR Trust,” *Arizona Capitol Times*, Feb. 21, 2004

⁶ See: Jeremy Duda, “IRS rules unlikely to curb anonymous campaign spending,” *Arizona Capitol Times*, Dec. 9, 2013

⁷ Jeremy Duda, “Dark money bill halted, but Sen. Reagan isn’t giving up,” *Arizona Capitol Times* Feb. 21, 2014. See also Howard Fischer, Capitol Media Services, “Lawmakers seek to shine light on hidden campaign donations,” *Arizona Daily Star*, Feb. 19, 2014

⁸ See, for example, Trevor Potter and Bryson B. Morgan, “The History of Undisclosed Spending in U.S. Elections & How 2012 Became the ‘Dark Money’ Election, *Notre Dame Journal of Law, Ethics & Public Policy* (2013, Volume 27): 383; and the Federal Communications Commission; Lili Levi, “Plan B For Campaign-Financed Reform: Can the

FCC Help Save American Politics After Citizens United?" *Catholic University Law Review* (Winter 2011, Volume 61): 97

⁹ Janet Loehrke, "Politicians Move to Rake in More Campaign Cash," *USA Today*, December 15, 2013

¹⁰ Lisa Rosenberg, "To Combat Dark Money, States Must Focus on Disclosure," July 22, 2013, Sunlight Foundation website, <http://sunlightfoundation.com/>

¹¹ Shawn Vestal, "Shedding Light on Dark Money Struggle," *The Spokesman-Review* (Spokane, WA) , Feb. 21, 2014

¹² Trevor Potter and Bryson B. Morgan, "The History of Undisclosed Spending in U.S. Elections & How 2012 Became the 'Dark Money' Election," *Notre Dame Journal of Law, Ethics & Public Policy* (2013, Volume 27): 383

¹³ Michael Beckel, "Top U.S. Corporations funneled \$185 million to political nonprofits –Company filings shine light on dark money," Center for Public Integrity, Thursday, Jan. 16, 2014

¹⁴ Ibid

¹⁵ Maguire, "Liberal Dark-Money." See also: Jeremy Duda, "Dark Money: Specter of anonymous campaign spending in Arizona looms over 2014," *Arizona Capitol Times*, Nov. 25, 2013

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