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IRS Audits Donors on Gift Tax

The IRS recently sent audit letters to 5 donors who had not filed gift tax forms for donations they had made in 2008 to certain social advocacy groups. These groups come under Section 501(c)4 of the tax code, the section that permits groups the right to withhold the identities of their donors who contribute towards political campaign advertisements. Since 2008, many political groups were formed under Section 501(c)4 such as American Crossroads, which discloses donors, and Crossroads GPS, which doesn't, both of which are large Republican organizations.

Not to be outdone, the Democrats also plan to start 2 groups of their own – Priorities USA and Priorities USA Action – to raise \$100 million for the 2012 re-election of President Barack Obama.

Donations to such groups are subject to a 35% gift tax, but this requirement has not been strictly enforced by the IRS. Until now.

The latest move by the IRS has raised concerns that it could curtail funding ahead of the 2012 presidential elections. But the IRS denied that their action was politically motivated. In a recent statement, it said, “All of the decisions involving these cases were made by career civil servants without

any influence from anyone outside the IRS,” and that the letters were “not part of a broader effort looking at donations to 501(c)4s.” The IRS clarified that the letters were sent by their Estate and Gift Tax unit workers as “part of their increased efforts in the area of non-filing of gift and estate tax returns”.

According to the nonpartisan Center for Responsive Politics, last year nonprofit groups including many 501(c)4’s spent almost \$300 million in mid-term elections to campaign for elected representatives, most of whom were Republicans.

Generally the lawyers of those who were audited feel that the IRS had been unfair to their clients because they were not informed beforehand about this action of enforcing the gift tax. The concern is that the action eventually could include donations to the new political organizations that cropped up in the 2010 midterm elections.

This might prompt legal action on 2 grounds. Firstly, that the gift tax was not designed to apply to such donations and secondly, that the IRS did not give any notice of enforcement of the tax after decades of inaction.

The IRS’ enforcement of 501(c)4 could also involve a wide range of established issue-advocacy groups, ranging from environmental to anti-tax organizations.