

Under Political Pressure, IRS Halts Investigation of Anonymous Political Contributions

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In early 2011, the Internal Revenue Service began investigating the contributions of five individuals to tax-exempt 501(c)(4) organizations. These investigations were generally seen as threatening anonymous political contribution. After initiating the investigations, however, the IRS came under political pressure — and on July 7, it announced the termination of its investigations.

Individuals and organizations have, in recent years, been contributing to 501(c)(4) organizations that, in turn, support political candidates and causes. Although the law generally requires public identification of individuals and organizations providing financial support for candidates and political causes, donors routing their political contributions through 501(c)(4) organizations were in many cases able to avoid public identification.

Earlier this year, the IRS began investigating five individuals who apparently had made large contributions to 501(c)(4) organizations. The IRS was specifically investigating such individuals' failure to file gift tax returns and pay any resulting gift tax following their contributions. Although there are several circumstances in which an individual need not pay a gift tax on large gifts, the initiation of the IRS investigations was expected to increase in many cases the cost of anonymous contributions by individuals to 501(c)(4) organizations participating in political activity. This result arguably followed from an IRS determination in 1982 that an individual's contributions to organizations that are neither charitable nor political are subject to the gift tax.

(The gift tax does not apply to corporations or labor unions, so the IRS investigations were not expected to affect anonymous contributions by these entities.)

After the IRS investigations were reported in the press, several members of the U.S. Senate and House of Representatives publicly questioned the motives for the new investigations. Many political observers believe that elimination of anonymous contributions would more significantly impair Republican political interests compared to Democratic ones — although, to be sure, many Republicans disfavor anonymity for political contributors and, according to news reports on unfolding strategies for the 2012 election cycle, Democratic organizations are significantly increasing their reliance on anonymous funding.

On July 7, the IRS announced that it “will [no longer] use resources to pursue examinations” of contributions to 501(c)(4) organizations for gift tax purposes until additional guidance or legislation may be made available. Furthermore, while the IRS had initially attempted to enforce the gift tax with respect to 501(c)(4) contributions made during the 2008 and 2010 election cycles, the IRS has now declared that “[a]ny future action...will be prospective and after notice to the public.” This announcement, therefore, suspends indefinitely the IRS investigations, and appears to signal that a contribution to a 501(c)(4) organization will not be subject to the gift tax unless, before the contribution is made, the IRS publicly announces its intention to apply the gift tax to this type of contribution.

Although the IRS's decision may have been a reaction to political pressure from Congress, the IRS publicly attributed its announcement to the fact that it had not in recent years issued clear guidance on the application of the gift tax to 501(c)(4) contributions.

Until further notice, it appears that the price of an individual's anonymous political contributions through 501(c)(4) organizations will not be increased due to the application of the gift tax.

Visit www.dailyjournal.com to read a previous article by these authors, which describes the factual and legal background in greater detail.

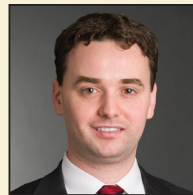
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