

## E-ALERT | Election and Political Law

May 13, 2011

### THE MORE THINGS CHANGE, THE MORE THEY STAY THE SAME

There is much hand-wringing and teeth-gnashing in this week's news about whether the IRS has changed its views on the possible application of the federal gift tax to large transfers to 501(c)(4) social welfare organizations. See, e.g., [The New York Times](#), [Politico](#), and [Roll Call](#). As a consequence, many individuals who have given, or who are planning to give, to social welfare organizations are asking whether the past twenty years, in which there have been no publicly documented instances of the IRS assessing the gift tax in such situations, were an anomaly and may be coming to an end. This is also a matter of not insignificant concern to social welfare organizations of all political stripes. Based on what we know today, that concern is premature.

#### WHAT WE KNOW

We know that there has been no publicly documented application of the federal gift tax with respect to large transfers to social welfare organizations in over two decades.

We know that the IRS has given no indication that it is abandoning its long silence on assessing the gift tax in such situations.

We know that the gift tax does not necessarily apply to transfers to social welfare organizations and that there are ways to structure transfers to reduce or even eliminate the risk of incurring gift tax.

All that said, something of a firestorm has erupted following the release of a redacted copy of a single gift tax audit letter which is circulating widely among tax lawyers this week. In that letter, an IRS agent has asked a taxpayer to identify his or her contributions to social welfare organizations and to explain why no gift tax was paid on the transfers.

We know that the IRS has confirmed that only 5 such audits have been opened and that they are not part of a broader effort looking at donations to 501(c)(4) organizations. Rather, they are part of a general effort to combat non-filing of gift tax returns. Thus, there is no coordinated IRS plan to target particular exempt organizations (such as targeting politically active social welfare organizations – a specific concern shared by many).

#### WHAT WE DON'T KNOW

We don't know how the audits will turn out.

We don't know if any gift tax will ultimately be assessed by the IRS and paid.

We don't know yet if the IRS intends to open more such audits. The IRS statement confirming that only 5 gift tax audits have been opened in the 501(c)(4) context leaves open the possibility of further gift tax audits.

As with many types of transactions, those contemplating making significant transfers of personal wealth to any entity, including a social welfare organization operating under Section 501(c)(4) of the Internal Revenue Code, should consider the potential tax treatment of the transfers. The specific facts and circumstances of any transfer may change the way in which it is treated under the tax laws.

Covington provides sophisticated advice to individuals, multinational corporations and not-for-profit entities in the application of the tax laws to various types of transactions. These matters include the successful resolution of domestic and international tax controversies, IRS attempts to revoke exempt organizations' tax exemptions, very large case audits, administrative appeals, and litigation involving a broad spectrum of subject matter areas.

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If you have any questions concerning the material discussed in this client alert, please visit our [website](#) or contact the following members of our Election and Political Law or Tax practice groups:

<b>Kevin Shortill</b>	202.662.5113	<a href="mailto:kshortill@cov.com">kshortill@cov.com</a>
<b>Robert Kelner</b>	202.662.5503	<a href="mailto:rkelner@cov.com">rkelner@cov.com</a>
<b>Bob Lenhard</b>	202.662.5940	<a href="mailto:rlnhard@cov.com">rlnhard@cov.com</a>

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