

The IRS Will Not Apply the Gift Tax to Section 501(c)(4) Donations . . . for Now

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Ending months of speculation and uncertainty, the Internal Revenue Service (IRS) announced in July that it would no longer devote its resources to considering whether to levy a gift tax on donations by individuals to Section 501(c)(4) social welfare organizations. For the time being, individuals may donate to Section 501(c)(4) organizations without the fear of incurring gift tax liability.

Earlier this year, the IRS sent audit letters to five individual taxpayers requesting additional information and documents concerning donations made in 2008 to Section 501(c)(4) organizations. The IRS contemplated invoking a 30-year-old ruling that stated that because the tax code did not contain a specific exemption from the gift tax for donations to Section 501(c)(4) organizations, such donations could be subject to the gift tax. Tax code amendments had created specific exemptions from the gift tax for donations to other entities, including Section 501(c)(3) charitable organizations and Section 527 political organizations; however, donations to Section 501(c)(4) organizations were left off that list. Notwithstanding its earlier ruling, the IRS had not historically imposed a gift tax on individual donations to Section 501(c)(4) organizations.

The five audit letters sent shockwaves throughout the legal and political communities, largely because Section 501(c)(4) organizations have become major political players and important advocacy tools in recent years. The IRS faced significant backlash from the media and members of Congress over its actions, culminating in a letter from six U.S. Senators to the IRS Commissioner expressing concern that imposing the gift tax on Section 501(c)(4) organizations was politically motivated and that such application would possibly violate the First Amendment.

It is important to note that the IRS has not closed the door to applying the gift tax on donations to Section 501(c)(4) organizations at some point in the future, but the IRS did indicate it will only do so for donations made after the IRS has given prior notice to the public.