



*The Internal Revenue Service Needs to
Improve Procedures to Identify
Noncompliance With the Reporting
Requirements for Noncash Charitable
Contributions*

March 5, 2007

Reference Number: 2007-30-049

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

Phone Number | 202-927-7037

Email Address | Bonnie.Heald@tigta.treas.gov

Web Site | <http://www.tigta.gov>



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 5, 2007

**MEMORANDUM FOR DEPUTY COMMISSIONER FOR SERVICES AND
ENFORCEMENT**

FROM: *Michael R. Phillips*
Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Internal Revenue Service Needs to Improve
Procedures to Identify Noncompliance With the Reporting
Requirements for Noncash Charitable Contributions
(Audit # 200630012)

This report presents the results of our review of Provision 883 (Increased Reporting for Noncash Charitable Contributions) of the American Jobs Creation Act of 2004.¹ The overall objective of this review was to evaluate the implementation of Provision 883 and the processing of individual income tax returns reporting deductions for noncash contributions.

Impact on the Taxpayer

Gifts of donated property, clothing, and other noncash items have long been a popular deduction for taxpayers. In recent years, the legitimacy of the values placed on some of these noncash donations has been questioned by the Internal Revenue Service (IRS) and Congress. As a result, Congress passed legislation adding additional reporting requirements to substantiate the value of some of these donations. Currently, taxpayers who may not be entitled to deductions for noncash contributions are reducing their tax liabilities and may receive refunds regardless of whether they provide the required substantiation. This could result in a loss of revenue to the Federal Government and inequitable treatment of taxpayers.

¹ Pub. L. No. 108-357, 118 Stat. 1418 (2004).



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Synopsis

Individual taxpayers are required to file Noncash Charitable Contributions (Form 8283) if their charitable deductions claimed for noncash contributions exceed \$500. If the value of donated property exceeds \$5,000, taxpayers are required to obtain signatures on their Forms 8283 acknowledging receipt of the donated property. In addition, taxpayers are required to attest on their Forms 8283 that the value placed on the donated property was determined by a qualified appraisal;² however, until passage of the American Jobs Creation Act of 2004, taxpayers were not required to attach the appraisals to their tax returns regardless of the value placed on the donated property.

The IRS revised tax forms and publications and provided training and information to employees to facilitate implementation of the new requirements for claiming noncash charitable contributions. However, taxpayers and tax practitioners still need to be better educated concerning requirements for claiming charitable contributions. Also, additional procedures need to be established to identify noncompliance with charitable contribution requirements during returns processing. Better education of taxpayers and preparers and additional returns processing procedures will enable the IRS to address potential noncompliance, as Congress intended in its legislation. We estimate 101,236 taxpayers could have claimed unsubstantiated noncash contributions totaling approximately \$1.8 billion for the period January 15 through September 21, 2006.

Recommendations

We recommended the Commissioner, Large and Mid-Size Business Division, coordinate with the other affected operating divisions to develop a comprehensive outreach plan on the reporting requirements for noncash charitable contributions for affected taxpayers and tax practitioners. We also recommended the Commissioner, Small Business/Self-Employed Division, and the Commissioner, Wage and Investment Division, develop procedures to correspond with taxpayers to obtain missing Forms 8283 and supporting documentation. Taxpayers failing to provide missing Forms and substantiation should have a specific audit code input on their tax returns to alert the Examination function of returns without required substantiation for noncash charitable contributions.

² In general, the appraiser must sign the Form 8283 attesting to his or her qualifications, impartiality, and independence.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Response

IRS management agreed with the first recommendation and plans to supplement their outreach plan by 1) partnering with several professional stakeholders to promote awareness of the increased reporting requirements, 2) coordinating the IRS' efforts to promote awareness of the increased reporting requirements to donee organizations, and 3) partnering with professional appraisal stakeholders to promote awareness of the increased reporting requirements and appraiser responsibilities.

IRS management partially agreed with the second recommendation. The IRS will continue to correspond with taxpayers claiming noncash contributions over a specific dollar threshold but with no Forms 8283 attached to their returns. In addition, the IRS agreed to use a specific indicator to identify for the Examination function returns claiming noncash contributions over the same threshold dollar amount but with no Forms 8283 attached. Management's complete response to the draft report is included in Appendix IV.

Office of Audit Comment

Although the IRS plans to continue corresponding with taxpayers and will add a specific indicator for instances in which Forms 8283 are missing, we believe few instances of unsubstantiated deductions will be addressed by these actions. The dollar threshold, which remains unchanged, has been set too high and needs to be lowered to ensure most of the returns claiming unsubstantiated deductions are addressed in concert with Congressional concerns. Also, the IRS does not plan any additional actions concerning incomplete documentation, such as missing signatures and appraisals. Based on our sampling, we estimate fewer than 1 percent of the returns with noncash charitable contribution deductions are above the IRS' dollar threshold. We applaud the IRS' efforts to increase its outreach program to better educate taxpayers and tax practitioners, but we urge the IRS to lower the dollar threshold and address returns with incomplete documentation to better deal with these unsubstantiated deductions.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit, (Small Business and Corporate Programs), at (202) 622-5894.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Table of Contents

Background	Page 1
Results of Review	Page 2
Tax Forms and Publications Were Revised, and Training and Information Were Provided to Employees to Facilitate Implementation of the New Requirements for Claiming Noncash Charitable Contributions	Page 2
Taxpayers and Tax Practitioners Need to Be Better Educated Concerning Requirements for Claiming Charitable Contributions	Page 2
<u>Recommendation 1:</u>	Page 4
Additional Procedures Need to Be Established to Identify Noncompliance With Charitable Contribution Requirements During Returns Processing	Page 4
<u>Recommendation 2:</u>	Page 5
Appendices	
Appendix I – Detailed Objective, Scope, and Methodology	Page 7
Appendix II – Major Contributors to This Report	Page 9
Appendix III – Report Distribution List	Page 10
Appendix IV – Management’s Response to the Draft Report	Page 11



*The Internal Revenue Service Needs to Improve Procedures to
Identify Noncompliance With the Reporting Requirements for
Noncash Charitable Contributions*

Abbreviations

AJCA	American Jobs Creation Act of 2004
IRS	Internal Revenue Service
LMSB	Large and Mid-Size Business
TIGTA	Treasury Inspector General for Tax Administration



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Background

The Tax Code allows individuals and businesses to make noncash contributions (e.g., vehicles, paintings, used clothing, and household goods) to qualifying charities and to claim deductions for these contributions on their tax returns. Gifts of donated property, clothing, and other noncash items have long been an important source of revenue for many charitable organizations and a popular deduction for taxpayers. In recent years, the legitimacy of the values placed on some of these noncash donations has been questioned by the Internal Revenue Service (IRS) and Congress. In Tax Year 2003,¹ individuals reported 14.3 million noncash donations valued at \$36.9 billion.²

On October 22, 2004, President Bush signed the American Jobs Creation Act of 2004 (AJCA).³ AJCA Provision 883 (Increased Reporting for Noncash Charitable Contributions) created additional reporting requirements for individual taxpayers making noncash charitable contributions valued at more than \$500,000. The IRS Large and Mid-Size Business (LMSB) Division was assigned primary responsibility for implementation of Provision 883. The implementation of this Provision involved multiple actions, including training and providing guidance to IRS employees, creating and revising tax forms and publications, and coordinating extensively with various IRS functions.

This review focused on noncash donations other than vehicles and works of art. The review was performed at the IRS office in Holtsville, New York, during the period March through September 2006. It included a review of tax returns filed nationwide and discussions with personnel in the Submission Processing function of the Wage and Investment Division and the Field Specialists function of the LMSB Division. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

¹ Tax Year 2003 was the most current year for which complete data were available.

² IR-2006-113, July 18, 2006.

³ Pub. L. No. 108-357, 118 Stat. 1418 (2004).



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Results of Review

Tax Forms and Publications Were Revised, and Training and Information Were Provided to Employees to Facilitate Implementation of the New Requirements for Claiming Noncash Charitable Contributions

To facilitate implementation of the new requirements for claiming noncash charitable contributions, the LMSB Division created on its web site an AJCA webpage that contained links to notices, news releases, fact sheets, and other existing technical guidance relating to the Act. Tax forms and publications related to noncash charitable contributions were properly updated in accordance with the new law. In addition, training covering the new law was provided to IRS employees.

The LMSB Division used the Legislative Implementation Tracking System, which is an IRS Intranet-based planning and monitoring system, to monitor implementation of the legislation. This System lists the required actions with estimated due dates and the functions responsible for taking the necessary actions.

Taxpayers and Tax Practitioners Need to Be Better Educated Concerning Requirements for Claiming Charitable Contributions

Individual taxpayers are required to file a Noncash Charitable Contributions (Form 8283) if their charitable deductions claimed for noncash contributions exceed \$500. If the value of donated property exceeds \$5,000, taxpayers are required to obtain signatures on their Forms 8283 acknowledging receipt of the donated property. In addition, taxpayers are required to attest on their Forms 8283 that the value placed on the donated property was determined by a qualified appraisal;⁴ however, until passage of the AJCA, taxpayers were not required to attach the appraisals to their tax returns regardless of the value placed on the donated property.

AJCA Provision 883 requires all donors who contribute property (other than cash, inventory, or publicly traded securities) for which a deduction of more than \$500,000 is claimed to attach a qualified appraisal to their tax returns. Provision 883 is effective for donations made after June 3, 2004.

⁴ In general, the appraiser must sign the Form 8283 attesting to his or her qualifications, impartiality, and independence.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

We reviewed statistically valid samples of Tax Year 2005 individual income tax returns on which the deductions claimed for noncash charitable contributions were greater than \$5,000. In 46 (22 percent) of 211 cases, taxpayers failed to provide the required substantiation for deductions of approximately \$23 million.⁵ Paid preparers prepared 161 (76 percent) of the returns in our samples and prepared 33 (72 percent) of the 46 error cases.⁶

Figure 1: Tax Returns Filed Without Substantiation for Noncash Contributions

	Returns Sampled	Signature Missing	Appraisal Missing	Form 8283 Missing	Totals	Percentage With Missing Documentation
Noncash Contributions \$5,001-\$500,000	121	27	Not Applicable	2	29	24%
Noncash Contributions Greater Than \$500,000	90	1	16	0	17	19%
Totals	211	28	16	2	46	22%

Source: Our analysis of cases in which the deductions for noncash contributions were greater than \$5,000.

Normally, the onus is on taxpayers and their preparers to stay abreast of existing and new tax law provisions. However, the IRS also has a responsibility to help taxpayers understand and meet their tax responsibilities. The fact that over 20 percent of taxpayers and/or preparers were not complying with the specific requirements (both old and new) for claiming noncash charitable contributions indicates the need for further action by the IRS.

Unlike other provisions of the AJCA, for which the IRS provided information to practitioners and other stakeholders through news releases and other communications, guidance on Provision 883 has generally been limited to the revision of tax forms and publications. More than 2 years after enactment of the legislation, an IRS notice under Internal Revenue Code Section 170⁷ providing guidance and transitional rules for increased reporting for noncash charitable contributions was approved for release. Also, a draft of new regulations under Internal

⁵ The actual tax losses cannot be determined because the IRS did not identify these returns and therefore took no actions to determine whether the taxpayers could provide the required documentation.

⁶ We also reviewed a judgmental sample of 54 tax returns on which the noncash charitable contributions claimed were more than \$500 but less than or equal to \$5,000. We found that the Forms 8283 were attached to the returns and were prepared correctly.

⁷ 26 U.S.C. Section 170 (2005).



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Revenue Code Section 170 with more formal guidance on increased reporting for noncash charitable contributions is not scheduled for release until 2007. Our samples were identified from returns processed from January 15 through March 18, 2006. Based on the results of our samples, we estimate 51,502 taxpayers claimed unsubstantiated noncash charitable deductions of approximately \$676 million on Tax Year 2005 returns processed during this time. If the error rate for the returns processed from March 19 through September 21, 2006, remained the same as the rate in our samples,⁸ we estimate 101,236 taxpayers could have claimed unsubstantiated noncash contributions totaling approximately \$1.8 billion for the period January 15 through September 21, 2006.⁹ Without proper documentation, these taxpayers, by law, are not entitled to these deductions.

Recommendation

Recommendation 1: The Commissioner, LMSB Division, should coordinate with the other affected operating divisions to develop a comprehensive outreach plan on the reporting requirements for noncash charitable contributions for affected taxpayers and tax practitioners.

Management's Response: IRS management agreed with the recommendation and plans to supplement their outreach plan by 1) partnering with several professional stakeholders to promote awareness of the increased reporting requirements, 2) coordinating the IRS' efforts to promote awareness of the increased reporting requirements to donee organizations, and 3) partnering with professional appraisal stakeholders to promote awareness of the increased reporting requirements and appraiser responsibilities.

Additional Procedures Need to Be Established to Identify Noncompliance With Charitable Contribution Requirements During Returns Processing

The procedures used by the IRS Submission Processing function were not adequate to ensure taxpayers met requirements for deducting noncash charitable deductions. Tax laws related to noncash charitable contributions state that no deduction shall be allowed for various noncash charitable contributions unless taxpayers provide specific substantiating information with their

⁸ For contributions of \$5,001 to \$500,000, the error rate was 24 percent and the average contribution amount was \$10,809. For contributions over \$500,000, the error rate was 19 percent and the average contribution amount was \$1,338,967.

⁹ These estimates were determined using the two samples described in Figure 1. For the sample of noncash contributions of \$5,001 to \$500,000, we estimate 100,677 taxpayers could have claimed unsubstantiated noncash contributions totaling approximately \$1.1 billion. For the sample of noncash contributions greater than \$500,000, we estimate 559 taxpayers could have claimed unsubstantiated noncash contributions totaling approximately \$700 million.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

tax returns. In general, individuals who claim noncash charitable contributions must provide the following with their returns:

- Noncash contributions of \$501 to \$5,000 – Form 8283 containing a description of the donated property.
- Noncash contributions of \$5,001 to \$500,000 – Form 8283 containing a description of the donated property, a signature from the charitable organization acknowledging receipt of the donated property, and the signature of a qualified appraiser.
- Noncash contributions of more than \$500,000 – Form 8283 containing a description of the donated property, a signature from the charitable organization acknowledging receipt of the donated property, the signature of a qualified appraiser, and a copy of the appraisal.

Instructions for Form 8283 inform the taxpayer that his or her deduction generally will be disallowed if he or she fails to attach Form 8283, get a required appraisal, or attach an appraisal when required. However, the IRS Submission Processing function did not adjust or stop these returns during processing or implement any type of review of these returns. Submission Processing function guidelines allow returns with such deductions to be processed except in the most egregious cases where the deductions are of a very significant amount and Form 8283 is missing. All other income tax returns filed without substantiation for the claimed noncash contribution deductions are processed as filed by the taxpayers.

Further, the IRS indicated the Examination function would be responsible for any review of information related to these returns; however, the returns were not coded or processed in any way to alert the Examination function of the unsubstantiated deductions. Instead, the returns go through the same Examination function selection criteria as any other tax returns. The Examination function generally audits fewer than 1 percent of the individual income tax returns filed each year.

By not identifying returns filed without the required substantiation for charitable contributions, the IRS is not addressing the Congressional intent of this legislation. Taxpayers who are not entitled to deductions for noncash contributions are reducing their tax liabilities and may receive refunds regardless of whether they provide the required substantiation. This could result in a loss of revenue to the Federal Government and inequitable treatment of taxpayers.

Recommendation

Recommendation 2: The Commissioner, Small Business/Self-Employed Division, and the Commissioner, Wage and Investment Division, should develop the following procedures to address returns without required substantiation for noncash charitable contributions:

- a) Correspond with taxpayers to obtain missing Forms 8283 and supporting documentation.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

- b) Input a specific audit code on tax returns that fail to provide missing Forms and substantiation, to alert the Examination function of returns without required substantiation for noncash charitable contributions.

Management's Response: IRS management partially agreed with this recommendation. The IRS will continue to correspond with taxpayers claiming noncash contributions over a specific dollar threshold but with no Forms 8283 attached to their returns. It also plans to use and provide guidance for a specific indicator to identify for the Examination function returns claiming noncash charitable contributions over a specific threshold dollar amount but with no Forms 8283.

Office of Audit Comment: Although the IRS plans to continue corresponding with taxpayers and will add a specific indicator for instances in which Forms 8283 are missing, we believe few instances of unsubstantiated deductions will be addressed by these actions. The dollar threshold, which remains unchanged, has been set too high and needs to be lowered to ensure most of the returns claiming unsubstantiated deductions are addressed in concert with Congressional concerns. Also, the IRS does not plan any additional actions concerning incomplete documentation, such as missing signatures and appraisals. Based on our sampling, we estimate fewer than 1 percent of the returns with noncash charitable contribution deductions are above the IRS' dollar threshold.

We applaud the IRS' efforts to increase its outreach program to better educate taxpayers and tax practitioners, but we urge the IRS to lower the dollar threshold and address returns with incomplete documentation to better deal with these unsubstantiated deductions.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to evaluate the implementation of Provision 883 (Increased Reporting for Noncash Charitable Contributions) of the AJCA¹ and the processing of individual income tax returns reporting deductions for noncash contributions. To accomplish our objective, we:

- I. Evaluated the IRS' implementation of Provision 883.
 - A. Reviewed the requirements for deductions of noncash charitable contributions and identified the new requirements under Provision 883.
 - B. Determined what actions have been taken by the IRS to implement Provision 883.
 1. Reviewed and monitored the Legislative Implementation Tracking System² to identify planned actions to implement Provision 883.
 2. Determined whether the IRS timely developed and revised tax forms, schedules, instructions, and/or publications when necessary. We also determined whether training of IRS employees was sufficient and whether taxpayers and tax practitioners were informed adequately concerning the requirements of the law.
- II. Evaluated controls over the processing of deductions for noncash charitable contributions reported on individual income tax returns by reviewing samples of tax returns.
 - A. Extracted data from the Individual Master File³ Return Transaction File,⁴ which is stored at the Treasury Inspector General for Tax Administration (TIGTA) Data Center Warehouse.⁵ We used the criterion of noncash charitable contributions in excess of \$500 for the Tax Year ending Dec. 31, 2005.⁶ We stratified the population

¹ Pub. L. No. 108-357, 118 Stat. 1418 (2004).

² This is an IRS Intranet-based planning and monitoring system to monitor implementation of legislation. This System lists the required actions with estimated due dates and the functions responsible for taking the necessary actions.

³ This is the IRS database that maintains transactions or records of individual tax accounts.

⁴ The Return Transaction File contains line items transcribed during return processing and other fields such as math calculations.

⁵ The TIGTA Data Center Warehouse provides data and data access services; centralizes storage, security, and administration of files; and develops uniform and user-friendly interfaces for users to access data.

⁶ We selected this tax period so any deductions for noncash charitable contributions would be subject to AJCA Provision 883. The TIGTA Data Center Warehouse file included Tax Year 2005 returns processed from January 15 through March 18, 2006.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

of 3,732,911 returns by the amount of the deduction for noncash charitable contributions into the following ranges:

- 1) More than \$500 but less than or equal to \$5,000 (3,517,950 returns).
- 2) More than \$5,000 but less than or equal to \$500,000 (214,486 returns).
- 3) Greater than \$500,000 (475 returns).

We selected three random and statistically valid samples (see audit steps B, C, and D below) from the stratified populations based on a 95 percent confidence level and a precision rate of ± 10 percent. A statistical sampling method was used to make a projection about the population from which the samples were selected. We validated the tax return data against the data on the Individual Master File Return Transaction File. No discrepancies were found.

- B. Used a random statistically valid sample of 140 tax returns on which the noncash charitable contributions claimed were more than \$500 but less than or equal to \$5,000 to determine whether a Form 8283 was attached to the return and prepared correctly. Because our review of the first 54 cases showed no errors, we decided that further review of this sample was unnecessary.
- C. Reviewed a random statistically valid sample of 121 tax returns on which the noncash charitable contributions claimed were more than \$5,000 but less than or equal to \$500,000 to determine whether a Form 8283 was attached to the return and the required information/signatures were obtained from a qualified appraiser and the donee.
- D. Reviewed a random statistically valid sample of 90 tax returns on which the noncash charitable contributions claimed were more than \$500,000 to determine whether a Form 8283 and an appraisal were attached to the return.
- E. Determined whether deductions are disallowed on tax returns without the required documentation.
- F. Extracted data from the Individual Master File Return Transaction File at the TIGTA Data Center Warehouse using the criteria from strata 2) and 3) in Step II.A. to determine the number of additional error cases processed for the period March 19 through September 21, 2006.⁷

⁷ We used the error rates from the original samples to arrive at this figure.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs)
Kyle R. Andersen, Director
Robert K. Irish, Audit Manager
Dolores M. Castoro, Acting Audit Manager
Bernard F. Kelly, Acting Audit Manager
Philip W. Peyser, Lead Auditor
Margaret F. Filippelli, Senior Auditor
Stephen A. Wybaillie, Senior Auditor
Layne Powell, Information Technology Specialist



*The Internal Revenue Service Needs to Improve Procedures to
Identify Noncompliance With the Reporting Requirements for
Noncash Charitable Contributions*

Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Commissioner, Large and Mid-Size Business Division SE:LM
Commissioner, Small Business/Self-Employed Division SE:S
Commissioner, Wage and Investment Division SE:W
Assistant Deputy Commissioner for Services and Enforcement SE
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:
 Commissioner, Large and Mid-Size Business Division SE:LM
 Commissioner, Small Business/Self-Employed Division SE:S
 Commissioner, Wage and Investment Division SE:W



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Appendix IV

Management's Response to the Draft Report



DEPUTY COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

RECEIVED
FEB 15 2007

February 15, 2007

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Kevin M. Brown *Kevin M. Brown*
Deputy Commissioner Services and Enforcement

SUBJECT: Draft Audit Report – The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With The Reporting Requirements for Noncash Charitable Contributions (Audit #200630012)

We have reviewed your draft report, "The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance with the Reporting Requirements for Noncash Charitable Contributions." We agree with your recommendation that more education of taxpayers and tax practitioners will increase awareness of the reporting requirements for noncash charitable contributions. We have made significant outreach efforts to ensure taxpayers are aware of the reporting requirements for noncash charitable contributions. To further these efforts, we agree to supplement our outreach plan.

We also support the premise that obtaining missing documentation may increase reporting compliance for noncash contributions. Therefore, we agree to correspond with taxpayers to obtain missing Forms 8283, "Noncash Charitable Contribution," and supporting documentation in situations involving significant noncash charitable contributions. We also agree to your recommendation to assign specific audit codes on returns with significant noncash charitable contributions missing Forms 8283. The procedures in place will be closely monitored and adjusted as necessary.

Attached is a detailed response outlining our corrective actions.

If you have any questions, please contact me or call Kathy Petronchak, Commissioner, Small Business/Self-Employed Division, at (202) 622-0600.

Attachment



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

Attachment

RECOMMENDATION 1:

The Commissioner, Large and Mid-Sized Business (LMSB) Division, should coordinate with the other impacted Operating Divisions to develop a comprehensive outreach plan on the reporting requirements for noncash charitable contributions for the affected taxpayers and tax practitioners.

CORRECTIVE ACTIONS:

The LMSB Division will fully discuss and coordinate the following corrective actions with impacted Operating Divisions before they are implemented:

- a) Partner with the Tax Executive Institute (TEI), American Institute of Certified Public Accountants (AICPA), American Bar Association (ABA), and other professional stakeholders to promote awareness of the increased reporting requirements.
- b) Work with the Small Business/Self Employed (SB/SE) and the Wage and Investment (W&I) Divisions and, to the extent necessary, the Tax Exempt and Government Entities (TE/GE) Division to promote awareness of the increased reporting requirements to donee organizations, including the requirements for appraisals and appraiser signatures on Form 8283.
- c) Partner with the American Society of Appraisers (ASA), Appraisal Institute (AI), and other professional appraisal stakeholders to promote awareness of the increased reporting requirements and appraiser responsibilities.

IMPLEMENTATION DATE:

The Field Specialists Office in the LMSB Division will coordinate with SB/SE, W&I and, to the extent necessary, TE/GE to develop an action plan by March 31, 2007. We anticipate that any corrective actions agreed upon may be implemented by September 30, 2007.

RESPONSIBLE OFFICIAL:

Director, Field Specialists Office, Large and Mid-Sized Business Division

CORRECTIVE ACTION(S) MONITORING PLAN:

The Director, Field Specialists Office, LMSB Division, will advise the LMSB Commissioner of any delays in implementing this corrective action.

RECOMMENDATION 2:

The Commissioner, Small Business/Self-Employed, and the Commissioner, Wage and Investment Division, should develop the following procedures to address returns without required substantiation for noncash charitable contributions:

- a) Correspond with taxpayers to obtain the missing Forms 8283 and supporting documentation.



The Internal Revenue Service Needs to Improve Procedures to Identify Noncompliance With the Reporting Requirements for Noncash Charitable Contributions

2

- b) Taxpayers failing to provide missing forms and substantiation should have a specific audit code input on their tax returns to alert the Examination function of returns without required substantiation for noncash charitable contributions.

CORRECTIVE ACTIONS:

- a) We partially agree with this recommendation, and the W&I Submission Processing function will continue to correspond with taxpayers claiming a noncash contribution over a specific threshold dollar amount and missing Forms 8283.
- b) (i) We partially agree with this recommendation. SB/SE Examination will provide guidance to W&I Submission Processing for applying a specific indicator to returns claiming noncash charitable contributions over a specific threshold dollar amount and missing Forms 8283.
- b) (ii) W&I Submission Processing will request programming changes to apply a specific indicator for returns claiming noncash charitable contributions over a specific threshold dollar amount and missing Forms 8283.

IMPLEMENTATION DATE:

- a) Completed.
- b) (i) June 15, 2007
- b) (ii) January 15, 2009

RESPONSIBLE OFFICIAL:

- a) N/A
- b) (i) Director, Examination, SB/SE Division
- b) (ii) Director, Submission Processing, Customer Accounts Services, W&I Division

CORRECTIVE ACTION(S) MONITORING PLAN:

- a) N/A
- b) (i) The Director, Examination function, SB/SE Division, will advise the SB/SE Commissioner of any delays in implementing these corrective actions.
- b) (ii) The Director, Submission Processing, Customer Accounts Services, W&I Division, will advise the W&I Commissioner of any delays in implementing these corrective actions.