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IRS Is Starting Inquiry Into Foundations Set Up by Individuals to Pare Federal Tax

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WASHINGTON — The Internal Revenue Service is starting an intensive investigation of a plan promoted by a Barrington, Ill., group for individuals to minimize Federal income taxes by setting up foundations to manage their business affairs, a high IRS official said.

As detailed in yesterday's Wall Street Journal, the Illinois group, called Americans Building Constitutionally, or ABC, advises individuals on how to channel most of their income through such foundations.

Particularly in light of the new attention focused on the operation, the IRS official said, "we will attack . . . we sure as hell aren't going to let these things go unchallenged."

For one thing, the official said, IRS agents will seek the membership list of ABC, which claims more than 800 members in nearly all 50 states. The agents then will study the situations of the individual members to see if tax-exempt low rulings they've received should be kept in force or revoked in a civil proceeding. If any false statements are found in exemption applications, criminal action could result, officials said.

Robert D. Hayes, ABC trustee, noted in

Barrington that the organization had expected the IRS investigation to come "sooner or later." He said IRS officials had contacted ABC "about three days ago." The IRS has indicated it will submit a list of questions it would like to have answered about ABC's activities, the trustee said.

"We haven't done anything illegal," Mr. Hayes declared. "And we're going right ahead with what we're doing," he said.

Mr. Hayes said ABC officials had told the IRS that its membership list was regarded as "confidential" and that ABC "wouldn't divulge" any names.

Some of the individuals, according to the account, haven't ever sought IRS rulings conferring tax-free status on their foundations. "Without a ruling, they're completely vulnerable," the official maintained.

The organization's comments indicate, though, that it disputes the idea that such rulings are necessary, and officials suspect ABC or its members might well fight any IRS challenges in court.

The IRS, however, maintains that Federal law authorizes the service's ruling on tax exemptions. "I suspect we're going to have a good fight on our hands, but we won't lose it for lack of trying," an official said.

When advance rulings are requested, the IRS usually issues them on the strength of the organizers' own statements on the purposes of the foundation without taking time to thoroughly check them out. Such requests, numbering more than 14,000 annually, usually appear to be very "innocent," an official said, but he noted that whether a group is permitted to retain its exemption depends on its "actual operation" rather than just its stated purposes.

The matter of determining when tax-free status is justified by an organization's activities isn't a simple one, analysts conceded, and they aren't ruling out the possibility that they may have to seek a tougher law from Congress.

As an example of the foundations' workings, the Wall Street Journal story described one set up by a Midwest doctor who said his foundation collects all his fees and in return provides him, tax-free, with a house, a car, a retirement plan and insurance, and is providing grants with which his four children are attending college.

Revenue men believe the providing of tax-free housing leaves a foundation open to question. Generally, the only situation in which housing can be provided without giving rise to a tax liability, they say, is when the nature of the job requires the person to live on his duty post. A doctor ordered to live in a hospital wouldn't be taxed on the value of his quarters, for example, one says, "but if he starts living down the street, he's open to challenge."

Another red flag to revenue men is when a foundation gives some of its money to members of the family that created it. They also are particularly skeptical when a foundation "pays" benefits that recipients in the family consider to be tax-free.