PERSPECTIVE

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Senators Ask IRS to Weigh in on College Admissions Scandal

By Robert W. Wood

People accused in the college admissions scandal are facing serious legal problems, as well as various other repercussions. Prosecutors charged 50 people in an alleged scheme to secure spots at top universities by illicit means. The specifics ranged from fixing test scores, to faking athletic prowess, to rigging donations that perhaps were not really donations at all. The charges have yet to be proven, but the 33 parents who are charged will have to contend with cooperating witnesses, including the alleged mastermind of the scheme.

The supposed mastermind, William Rick Singer has already pleaded guilty to counts of racketeering conspiracy, money laundering conspiracy, conspiracy to defraud the United States, and obstruction of justice. And as what has been released already shows, the feds have collected some evidence that seems to be fairly persuasive in at least some of the cases. A number of parents were charged with conspiracy to commit mail fraud and honest services mail fraud. Prison time is certainly possible.

The public and workplace backlash has also been swift. Some of the accused have faced employment, economic and social consequences that are themselves pretty significant. In some cases, their children have too. And then there are the taxes. So how do taxes figure in?

The tax elements of the case are now getting some press. The U.S. Senate Finance Committee Chairman Chuck Grassley (R-IA) and Ranking Member Ron Wyden (D-OR) have called on the IRS Commissioner Chuck Rettig, asking him to fully enforce the tax laws against those involved. In this sense, perhaps the Republicans and Democrats can agree on something after all.

The senators outline several types of transactions for the IRS chief. These deals were between parents and the Key Worldwide Foundation to facilitate the illicit payments. The arrangements included payments made from private foundations and from businesses for what appear to be personal, illicit benefit, as well as donations of stock arranged to appear as charitable donations.

If all of this sound like a no-fly zone when you're doing your taxes, you're right. The tax angles are huge, and the potential taxes, penalties and interest are serious. It may be fraudulent too, and there is a separate 75 percent civil fraud penalty the IRS can impose. And that is just if the IRS stays civil with this mess. Criminal tax charges are possible too, and they could be very serious in themselves.

The tax law is clear that you cannot write off a charitable contribution if it wasn't really a charitable contribution. One way it might not be is if you were paying for services. Another way would be if the charitable entity wasn't really charitable. Still another might be linked to where the money you contributed came from originally.

The Senate Finance Committee chair's letter to the IRS commissioner points out that several of the parents involved in the scandal may have misappropriated funds from private foundations over which they have financial control in order to make illicit payments to the Key Worldwide Foundation. That means there could be a raft of other tax problems, not just individual ones. There are tight tax law controls over how private foundations spend money, with special restrictions on so-called self-dealing transactions.

But the tax issues don't stop there. Then there is the business expense angle. An affidavit in the case alleges that some of the parents paid bribes and other payments from accounts associated with their *businesses*. It is obviously a no-no for a personal expense to masquerade as a business expense by having a business pay for it.

Did this happen too? The affidavit in the case describes one defendant father asking the scandal's ringleader, "What are the options for the payment? Can we make it for consulting or whatever from the [K]ey so that I can pay it from the corporate account? [Ringleader] replied that he could make the invoice for business consulting fees, so that [father] could 'write off as an expense.' [Father] replied, 'Awesome!'"

Shortly thereafter, the defendant father's company allegedly wired $100,000 to Key Worldwide Foundation. The senators say this strongly suggests the payments were not legitimate business expense deductions. The tax system is so complex, that taxpayers commonly can say with some justification that they just made a mistake, and didn't understand the tax law.

But that kind of excuse might be difficult to use in a case of this sort. In a criminal tax case, the government wants to show willfulness, not a mere mistake. Willfulness or knowledge of wrongdoing can be hard for the government to prove in a criminal tax case. However, based on what we've seen so far, in at least some of these cases, it may be hard to show that these tax mistakes were unintentional.

There are more tax angles too. For example, there is the alleged end-run around capital gain taxes. The two Senators point the IRS commissioner to the affidavit again. It suggests that some parents made stock donations to allegedly charitable entities. Why would they donate stock?

That way, you get a write-off for the market value of the stock, and are not required to pay the capital gain tax on the appreciation in the shares. Wealthy people like Warren Buffett generally make all their significant charitable donations this way. It is the ultimate tax efficiency, a true double tax benefit!

There are many aspects to these cases, for it is not one case. Not every case is likely to come out the same. However, in a number of them, taxes could play a large part. Some of the people involved are likely to be doing some damage control, considering amended tax returns and disclosures to the IRS and state tax authorities. And that is on top of everything else.

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