Nonprofit Tax Update:  
*More Than Just the 990*

MACPA Government & Not for Profit  
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Agenda

- New Select Check Tool From IRS
- Significant Changes to Form 990 for 2011
- Automatic Revocation for Non-Filing
- New Form 8940 for Miscellaneous Determinations
- 2-Month Suspension for E-Filing
- IRS Exempt Organization Annual Report and Workplan
- Fast-Track Settlement Program
- Employment Tax Initiative, Offshore Voluntary Disclosure Initiative, and Voluntary Classification Settlement Program
- Congressional Focus
- State Initiatives

Exempt Organizations Select Check

- Exempt Organizations Select Check ([http://apps.irs.gov/app/eos/](http://apps.irs.gov/app/eos/)) is an on-line search tool that allows users to select an exempt organization and check certain information about its federal tax status and filings. It consolidates three former search sites into one, providing expanded search capability and a more efficient way to search for organizations that:

  - Are eligible to receive tax-deductible contributions (Pub 78),
  - Have had their tax-exempt status automatically revoked because they have not filed Form 990 series returns or notices annually as required for three consecutive years (Auto-Revocation List), or
  - Have filed a Form 990-N annual electronic notice (e-Postcard).
Significant Form 990 Changes for 2011

Joint Ventures and Investment Partnerships

- Per recent IRS announcement an FAQ, below is optional for 2011
- 990 now requires organizations to report revenues, expenses and assets related to joint ventures and investment partnerships using amounts reported on Schedule K-1:
  - Part X, Balance Sheet - requires reporting distributive share of assets in any joint ventures and other entities treated as partnerships for federal tax purposes according to the ending capital account the partnership reported on Schedule K-1.
  - Parts VIII and IX, Revenue and Expenses - requires reporting distributive share of investment income, royalties and rental income, and expenses from joint ventures as reported on Schedule K-1.

Significant Form 990 Changes (continued)

Compensation

- Schedule J Part I, an organization that is part of a related group of organizations will be required to provide a narrative description of any reliance by such organization on a related organization to establish the compensation of any of the reporting organization’s ODTKE.
- Also requires additional narrative of compensatory benefits and any severance or change-of-control payments.

Contributions/Easements

- Contributions of conservation easements and other qualified conservation contributions must be reported consistently with how the organization reports revenue from such contributions in its books, records and financial statements.
Significant Form 990 Changes (continued)

• Organization is not considered to have provided a complete copy of its Form 990 to all members of its governing body prior to filing the form merely by making the form available upon request. *(Part V, Line 11)*

• If a governing body delegates broad authority to an executive committee or similar committee, this must be explained in Schedule O. *(Part V, Line 1a)*

• Examples illustrating when Board chair compensation is considered to compensate the Board chair as an officer or an employee of the organization. *(Part V, Line 1(b))*

Significant Form 990 Changes (continued)

• Instructions no longer provide that a director loses independence because the director or a family member of the director was a key employee of an entity that engaged in a business transaction with the filing organization reportable in Schedule L

• Instructions exempt from reporting certain business relationships in which an officer, director, trustee, or key employee of the filing organization was a key employee of another organization
Significant Form 990 Changes (continued)

• Only one position box should be checked for each person listed in the compensation table, unless the individual is both an officer and a director/trustee of the organization. (Part VII, Section A, Column C)

• Although an organization may report revenue on line 1 of Part VIII under SFAS 116, the value of donated services or the use of donated materials, equipment or facilities may not be reported.

• “Term endowment” is renamed “Temporarily restricted endowment” and includes not only endowment funds established by donor-restricted gifts for a specified period, but all other temporarily restricted net assets held in a donor-restricted endowment, including certain income from permanent endowments. (Glossary)

Significant Form 990 Changes (continued)

• Organizations that provided more than $5,000 of grants and other assistance to organizations or individuals outside the United States or inside the United States for foreign activity must complete certain sections of Schedule F. (Part IV, Lines 15 and 16)

• Organizations must complete Form 990, Part I of Schedule F, Statement of Activities Outside the United States, if it had foreign investments during the tax year valued at $100,000 or more. Previously, Part I of Schedule F needed to be completed only if the organization had aggregate revenues or expenses of more than $10,000 attributable to various foreign activities.
Significant Form 990 Changes (continued)

- Instructions clarify an organization should make reasonable efforts to obtain information from third parties needed to complete Form 990.
- The name and address of the principal officer and the web site address should be current as of the date of filing.
- Paid Preparers
  - A paid preparer may sign original or amended returns by rubber stamp, mechanical device, or computer software program.
  - All paid preparers must enter their preparer’s taxpayer identification number (PTIN) in Part II.
- 990 VII, Section B, line 1, Independent Contractor Payments - clarifies that independent contractor compensation should be reported for the calendar year ending with or within the tax year.

Automatic Revocation for 990 Nonfiling

- Most tax-exempt organizations are required to file an annual return or notice with the Internal Revenue Service.
- Section 6033(j) of the Internal Revenue Code automatically revokes the exemption of any organization that fails to satisfy its filing requirement for three consecutive years.
- The automatic revocation of exemption is effective as of the due date of the third required annual filing or notice.
- To restore exemption an organization must reapply using Forms 1023/1024 and pay application fees
Automatic Revocation (continued)

- Effective date will usually be the date the organization filed its application.
- They may request to have tax-exempt status reinstated as of the effective date it was automatically revoked with a letter attached to its application for exemption. Granted only if reasonable cause.
- If no longer exempt:
  - May have to file 1120/1041 income tax return.
  - Loss of exemption means taxation at corporate rates.
  - Investment income would be taxed.
  - Not all expenses can be used to offset income.

New Form 8940, Request for Misc. Determinations

The form can be used to make requests for:

- advance approval of certain private foundation set-asides;
- advance approval of private foundation voter registration activities;
- advance approval of private foundation scholarship procedures;
- exemption from Form 990 filing requirements;
- change in (or initial determination of) type of a Section 509(a)(3) supporting organization;
New Form 8940 (continued)

- advance determination that a potential grant or contribution is an unusual grant, excluded from certain public support calculations
- reclassification of foundation status, including a voluntary request from a public charity for private foundation status;
- termination of private foundation status under Section 507(b)(1)(B) (advance ruling request); and
- termination of private foundation status under Section 507(b)(1)(B) (60-month period ended).

Two Month Suspension of IRS e-File

- 990s could not be e-Filed during January and February 2012
- Organizations with an initial due date or first extension ending during this period should have requested an extension
- Organizations on final extension have been advised they will not be charged late filing penalties if they attach a Reasonable Cause Statement requesting penalty abatement as no further extension is permitted by law
- Alternatively the Organization can file on paper and be excused from mandatory e-File during this period
- No guarantee IRS will not send notices anyway—we have seen some
- States have conformed on a limited basis
IRS Exempt Organizations
Annual Report and Workplan

• Released February 8, 2012

• Available at:

• Contains both a look back at FY 2011 and forward look to plans for FY 2012

Annual Report Highlights

• Total number of EO employees has decreased from 910 to 889 over past 3 years, with largest decrease in Rulings and Agreements- other areas have remained fairly flat (including examinations)

• Examinations (audits) decreased from 15,342 in prior year to 14,863 in FY 11, with about 3,200 being compliance audits and the remainder being traditional audits

• New EO Examinations office in Ogden for resolving problems resulting from examinations (e.g., misapplied payments)
Annual Report Highlights (continued)

- Plain language updates to some of the audit letters
- Proposed Reg. 301.6104(c)-1: revised and eased barriers for disclosure of information to state charity regulators
- Rev. Procedure 2011-33: update on old Rev Proc providing grantor reliance on Pub 78; permits reliance on EO Business Master File; incorporates new automatic revocation procedures

2012 Key Workplan Highlights

- IRS is conducting a survey of randomly selected exempt organizations to analyze how to reduce the burden of preparing and filing annual exempt organization returns including:
  - Methods for Preparing, Recordkeeping, Resources Used to Gather Materials, Time spent on Tax-related Activities, Fees Associated with Tax Reporting Compliance
  - Voluntary and only taxpayers randomly selected may participate
  - Used for statistical or research purposes only
- Hospitals:
  - Review of Operations group started in 2011 completing community benefit reviews; will use information for research, education and compliance purposes
  - Continuing to work with Treasury to develop guidance on new Sec.501(r) requirements
2012 Key Workplan Highlights (Continued)

- 501(c)(4),(5) and (6) “self declarers”:
  - Can declare themselves exempt without a determination letter
  - IRS will review them to ensure they are classified properly and complying with rules

- Political Activity in Election Year:
  - As in previous year, IRS will be enforcing rules about political activity and campaign expenditures
  - Will focus its examination resources on serious allegations—to be reviewed by committee of career civil servants
  - Additional potential violations to be identified through risk modeling of Form 990 data and IRS will further refine its risk models based on examinations

2012 Key Workplan Highlights (Continued)

- 990-T and UBIT
  - Focus on organizations reporting UBI on 990 but not filing 990-T
  - Risk models to be developed for organizations with significant gross receipts but who don’t pay any tax
  - This work to be used in future UBIT project (i.e.- examinations)

- International
  - Continue to examine organizations who operate overseas to ensure activities are consistent with exempt purpose
  - Examinations will include number of large private foundations with international activities and assets/revenue greater than $500M
  - Continue to look at organizations who report foreign bank accounts
  - Plans to release 2 new publications describing special rules applicable to foreign and domestic charities engaged in international activities
2012 Key Workplan Highlights (Continued)

• Employment Tax Initiative—final year of 3 year project (discussed later)
• EO Examinations Resources Page on IRS.gov:
  • To help organizations understand what to expect in a compliance check or examination
  • Clarify steps on the process and to provide links to resources
• Colleges and Universities—final report of study based upon compliance questionnaire sent to 400 colleges in 2008 (interim report issued in 2010)
• Disaster Relief—identification of compliance issues that are most commonly associated with disaster relief efforts and develop communications plan to educate organizations

2012 Workplan Highlights (Continued)

• Group Rulings—develop questionnaire to be sent to cross section of group ruling holders and expand education in this area
• Private Foundations—examining a selection of the largest private foundations based upon information from 990-PFs
• EO Services and Assistance: project continuing to learn how small organizations receive tax-related information and how to develop improved outreach to them
IRS Fast Track Settlement Program

- Alternative dispute resolution process (during examinations) to avoid going to appeals, decrease time required (120 days), and reduce burden
- Involves mediated agreement
- May be initiated after an issue is “fully developed”:  
  - Notice of proposed adjustment given to taxpayer
  - Written response by taxpayer clearly defining position and basis for disagreement
- Certain issues not appropriate for Fast Track
- Consult carefully with your representative before opting Fast Track

Employment Tax Initiative

National Research Project —IRS believes $70 Billion is lost due to payroll tax issues

- 2000 examinations to be conducted annually for 3 years - includes 500 NFPs per year began in Feb 2010—this is final year—we have had several of these in our client base
- Examinations of random sample of NFPs based upon annual wages—compliant as well as non-compliant organizations will be studied
- Focus on employer vs. contractor and accurate compliance
- Be sure W-9 files are current and accurate
- Foreign withholding
3rd Offshore Voluntary Disclosure Initiative (OVDI)

- Nonprofits are subject to same reporting rules as taxable entities for various forms related to foreign activities.
- This can be due to foreign bank accounts, alternative investments and foreign subsidiaries.
- Common forms that may be required are TD F 90-22.1 (FBAR), 5471, 8865 and 926.
- In 2009 and 2011, the IRS conducted the OVDI and closed these programs. On Jan 9, the program was re-opened with no set end date, although it can be closed at any time.
- For most nonprofits, this is an opportunity to file past forms without penalty (and the potential penalties can be very severe).
- Consult your advisor.
- Also, FBAR filing for individuals with signing authority, but no financial interest in account extended to June 30, 2013 (FinCen Notice 2012-12).

Voluntary Classification Settlement Program

- Allows employers to voluntarily change prospective classification of workers (i.e., from independent contractors to employees).
- Only liable for 10% employment tax liability for most recent tax year, no penalties or interest and not subject to employment tax on affected employees for prior years.
- Cannot be under audit to participate.
- Carefully consider ramifications before applying - may affect pension, benefit plans.
- Consult with advisors.
Congressional Focus on the Tax Exempt Sector

- Sector has seen tremendous growth
- Congress may look at sector as a source of revenue
- Congress is concerned about abuses in the tax exempt arena and is reviewing IRS enforcement of the current tax laws
- Congress has been legislating to correct abuses and will continue to do so
- Congress has new community benefit requirements for tax exempt hospitals

Hospitals

NEW REQUIREMENTS IN ORDER TO KEEP 501(c)(3):
1. Community Health Needs Assessment (CHNA) every three years— for taxable years beginning after March 23, 2010— $50,000 penalty for noncompliance
2. Financial Assistance Policy
3. Limitation on Charges
4. Billing and Collection Practices
AND:
- Audited financial statements of hospitals must be attached to Form 990
- IRS review of tax exempt hospitals every three years
Tax Reform: Revenue Loss from 501(c)(3) Organizations

Federal
- Income Tax Exemption
- Charitable Deduction
- Tax Exempt Bonds

State
- Sales and Use Tax Exemptions
- Property Tax Exemptions
- Income Tax Exemptions (some states do not even tax UBI)

Tax Exempt Bonds

- The Federal government forgoes tax revenue from bondholders so that state and local governments, 501(c)(3) organizations and others can obtain financing at favorable rates of borrowing
- Arbitrage—Arbitrage profits earned on invested proceeds must be rebated to the Federal government
- What about interest earned on endowments that is in excess of the interest paid on the tax exempt bonds? (See Congressional Budget Office: Tax Arbitrage by Colleges and Universities --April 2010)
- The Administration’s budget again calls for limiting the exclusion of tax-exempt interest for municipal bonds (securities) to 28 percent
Options regarding Charitable Contributions

Cap the value of itemized deductions at 28%
Other Options (CBO report May 2011):
• Retaining the current deduction for itemizers but adding a floor.
• Allowing all taxpayers to claim the deduction, with or without a floor.
• Replacing the deduction with a nonrefundable credit for all taxpayers, equal to 25 percent of a taxpayer's charitable donations, with or without a floor.
• Replacing the deduction with a nonrefundable credit for all taxpayers, equal to 15 percent of a taxpayer's charitable donations, with or without a floor.

Letter from Congress to IRS—October 6, 2011

1. Overview of the Tax-Exempt Sector
2. Compliance
3. Unrelated Business Income
4. Audits
5. Current Tax-Exempt Enforcement Initiatives including Hospitals and Colleges and Universities
Attribution of Activities from Affiliates

- Congress is focusing on exempt organizations with complex corporate structures
- Attribution of activities from one corporate entity to another corporate entity may be appropriate when one organization is the “alter ego” of the other organization and corporate formalities are not respected
- Attribution of the activities of a taxable subsidiary to a tax exempt parent could jeopardize the tax exemption of the parent
- IRS has looked at the day to day activities rather than board overlap
- IRS has issued rulings that outline how favorable outcomes can be achieved.

Attribution of Activities Can be Avoided—Lobbying and Political Activity

IRS PLR-201127013 - Indirect political activities allowed
501(c)(3) can establish and control a 501(c)(4) to conduct political activities including PAC
Political activities of 501(c)(4) and its PAC will not be attributed to 501(c)(3) if:
- No 501(c)(3) assets are used for 501(c)(4) or PAC
- Organizations operate & administer their affairs independently
- Shared costs are properly allocated
Political Activity—Other 501(c) Organizations

Political activities are allowed, but:
- **Cannot be primary purpose**
- Subject to income taxes on lesser of political activities or investment income
  (IRS Form 1120-POL)
- Look at $\$ and activity (time sheets are very important records)
- Be careful to avoid substantial private benefit
- After the *Citizens United* case, there have been many organizations formed that are involved in political activities—Supreme Court to look at
- IRS had been pursuing whether to apply gift tax to contributions to 501(c)(4)s -- July 7th they announced that they will not pursue the issue without further guidance
- February 16, 2012 letter from four Senators to IRS Commissioner Shulman inquiring whether IRS intends to investigate 501(c)(4) organizations engaged in political activities

State Initiatives

- States are aggressively pursuing sales taxes, income taxes (alternative investments raise particular concerns) and pursuing unclaimed property (using third parties to pursue)
- If an organization has a meeting or expo in a state and sells items, there may be sales tax due on those items
- If an organization never filed a return, there is no statute of limitations
- Many states have voluntary disclosure programs and amnesty programs
Other State Initiatives

- California--Executive Compensation and Transactions with Insiders
- Massachusetts--Director Compensation
- Illinois--Denial of property tax exemptions for hospitals
- State of New York Governor’s Task Force on Not-For-Profits
- New York City review of property tax exemptions
- NAAG letter to Senator Baucus to enable state regulators to more freely use information shared by the IRS
- NY AG Announces Plan to Revitalize New York Nonprofits - “Revitalizing Nonprofits / Renewing New York”

Questions & Answers

To ensure compliance with Treasury Department regulations, we wish to inform you that any tax advice that may be contained in this presentation (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax related penalties under the Internal Revenue Code or applicable state or local tax law provisions or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.

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