

MSCPA Federal Tax Forum Update
Exempt Organizations
By Christopher E. Pulick

1. IR-2008-98, Aug. 19, 2008

WASHINGTON — The Internal Revenue Service released the revised instructions that tax-exempt organizations will need to fill out the redesigned Form 990, which must be filed starting with tax year 2008 (filed in 2009).

Most charities and other tax-exempt organizations must file an annual informational return with the IRS to maintain their tax-exempt status. Information reported on Form 990 is made available to the public.

“These instructions are the final step in a tremendous effort to bring the Form 990 up to date and to reflect the diversity and complexity of the tax-exempt community,” said IRS Commissioner Doug Shulman. “The revised form will give the IRS and the public a much better view of how exempt organizations operate. The improved transparency provided by these changes will also benefit the tax-exempt community.”

Form 990 had previously not seen major revisions since 1979. The revised instructions and redesigned Form 990 can be found on this Web site.

The [revised instructions](#) feature several new tools that make it easier to answer questions line-by-line and that facilitate uniform reporting. Input from the tax-exempt community played a major role in how the new instructions were designed.

“We were gratified by the amount of help the IRS received from the tax-exempt community through public comments to redesign the Form 990 and revise its instructions,” said Steven T. Miller, Commissioner of the Tax Exempt and Government Entities Division. “This input helped us achieve our goal of improving compliance while minimizing burden. We will now begin working with the tax-exempt sector to help organizations complete the form and prepare for the 2009 filing season.”

The IRS expects to release instructions to the 2008 Form 990-EZ, Short Form Return of Organization Exempt from Income Tax, in the next few weeks.

As part of the phase in of the redesigned Form 990 over a three-year transition period, many organizations not eligible to file the Form 990-EZ for 2007 will be eligible to file Form 990-EZ or Form 990 for 2008. A [summary of the transition period filing requirements](#) for Form 990, 990-EZ, and 990-N is also now available.

2. Publicly Charity Application and Approval

Temporary and final regulations (see TD 9423) eliminate the so-called advance rulings that previously granted public charity status for an initial five-year period, but required organizations to demonstrate that they received a substantial part of their support from public sources to receive a final determination letter. If an organization applying for exemption can reasonably be expected to meet the public support test during its first five years, the IRS will issue a determination letter stating that the organization is exempt under IRC Sec. 501(c)(3) and is classified as a public charity. The regulations also revise the compensation reporting rules, and allow use of the same accounting method for computing public support as that used in keeping the organization's books under IRC Sec. 446 . Subject to transition rules, the regulations are effective on 9/9/08 and apply to tax years beginning on or after 1/1/08.

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3. Exempt organization compliance at the IRS.

For many practitioners, the fiscal year 2008 EO Implementing Guidelines confirm what was already known. The IRS Exempt Organizations Division (EO) has replaced the random (and formerly infrequent) “audit lottery” with a new enforcement two-step: large-scale information gathering (soon to be enhanced by the newly revised Form 990), followed by targeted examinations. What the Guidelines describe is largely a mop-up of 2007’s ambitious compliance agenda, with liberal use of “compliance check” letters and questionnaires. Reflecting current trends, there are two new projects (and two continuing ones) concerning unrelated business taxable income and often-complex business relationships with taxable entities. On the customer service side, the focus continues to be electronic—an electronic case-processing system, the long-awaited Cyber Assistant for Form 1023, an electronic filing system for small organizations, and Web-based workshops and educational materials. ([G. Allison, 20 Taxation of Exempts, No. 1, 33 \(July/August 2008\).](#))

4. New form Phase-In.

The new Form 990 series returns will be effective for 2008 tax years (returns filed beginning in 2009). To allow organizations time to adjust to the new forms, the IRS is phasing in the new returns during a three-year transition period. During the transition, an organization’s annual filing requirement will depend on its financial activity. The charts below indicate annual exempt organization filing requirements during the transition period.

2007 Tax Year (Filed in 2008 or 2009)	Form to File
Gross receipts normally ≤ \$25,000	990-N
Gross receipts > \$25,000 and < \$100,000, and Total assets < \$250,000	990-EZ or 990
Gross receipts ≥ \$100,000, and/or Total assets ≥ \$250,000	990

2008 Tax Year (Filed in 2009 or 2010)	Form to File
Gross receipts normally ≤ \$25,000	990-N
Gross receipts > \$25,000 and < \$ 1 million, and Total assets < \$2.5 million	990-EZ or 990
Gross receipts ≥ \$1 million, and/or Total assets ≥ \$2.5 million	990

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2009 Tax Year (Filed in 2010 or 2011)	Form to File
Gross receipts normally \leq \$25,000	990-N
Gross receipts $>$ \$25,000 and $<$ \$500,000, and Total assets $<$ \$1.25 million	990-EZ or 990
Gross receipts \geq \$500,000, and/or Total assets \geq \$1.25 million	990

2010 Tax Year and later (Filed in 2011 and later)	Form to File
Gross receipts normally \leq \$50,000	990-N
Gross receipts $>$ \$50,000 and $<$ \$200,000, and Total assets $<$ \$500,000	990-EZ or 990
Gross receipts \geq \$200,000, and/or Total assets \geq \$500,000	990

For all years above, sponsoring organizations of donor-advised funds and controlling organizations described in section 512(b)(13) must file Form 990 regardless of the amount of their gross receipts or assets.

5. IRS Sends Compliance Questionnaire to Colleges and Universities

The IRS is sending a [compliance questionnaire](#) to 400 small, mid-sized, and large public and private colleges and universities as part of a [new compliance project](#) designed to give the IRS a better understanding of this large component of the tax-exempt sector. The questionnaire focuses on unrelated business income, endowments, and executive compensation practices.

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6. News Release 2008-102, 09/08/2008, IRC Sec(s). 6033

IRS Streamlines Application Process for New Tax-Exempt Organizations



The Internal Revenue Service and the Treasury Department today issued new regulations that will streamline the approval process for organizations seeking tax-exempt status as publicly supported charities. The new regulations do away with the so-called advance rulings that granted public charity status for an initial five-year period but required exempt organizations to demonstrate, after the initial period, that they in fact received a substantial part of their support from public sources to receive a final determination letter. The IRS was able to eliminate the advance rulings process because of the recent redesign of the Form 990, the tax return filed by organizations exempt from federal income tax. “The revised Form 990 enhances transparency for exempt organizations and makes it easier for them to show that they are 'publicly supported' charities, rather than private foundations,” said IRS Commissioner Doug Shulman. Private foundations under federal law are subject to more restrictions on the way they operate than publicly supported charities. To apply for exempt status either as a private foundation or as a publicly supported charity, an organization must file a Form 1023, the application for recognition of tax exemption. Over the years, approximately 95 percent of exempt organizations that received advance rulings were later recognized as publicly supported charities at the end of the five-year period. “Given the high 'recognition' rate and the redesigned Form 990, it makes sense to eliminate the burdensome advance ruling process” said Lois G. Lerner, Director of the IRS Exempt Organizations division. “Not only will the streamlined process aid exempt organizations, but it will also allow the IRS to redirect staffing to other program areas without compromising compliance.” The IRS will use the new Form 990 and other traditional techniques to continue to ensure organizations are complying with the rules for publicly supported charity status on an ongoing basis. Organizations that have already received an advance ruling under the old regime, but are still in their first five years of existence, can use their advance ruling letter as their final determination letter. In addition to the streamlined approval process, the new regulations include other modifications necessary to implement the redesigned Form 990. Organizations will begin filing the new Form 990 for their 2008 tax year.

7. Private Letter Ruling 200834015, 08/22/2008, IRC Sec(s). 168 Tax-exempt controlled entities—elections—extensions.



Dear _____:


This letter responds to your private letter ruling request, dated November 14, 2007, regarding an extension of time to make an election under  § 168(h) of the Internal Revenue Code (Code). Specifically, you requested an extension of time to make an election under  § 168(h)(6)(F)(ii) for Taxpayer, a tax-exempt controlled entity under  § 168(h)(6)(F)(iii). A tax-exempt controlled entity




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that makes an election under  § 168(h)(6)(F)(ii) can avoid limitations on the rehabilitation credit that otherwise would be imposed by  § 47(c)(2)(B)(v)(I).


Facts





Taxpayer is organized under the laws of State and is a Subchapter C corporation for federal income tax purposes. Taxpayer uses the accrual method of accounting and the calendar year as its taxable year. Taxpayer is wholly owned by Exempt Organization, which has received a determination that it is a tax-exempt organization described in  § 501(c)(3). Because Exempt Organization owns more than 50 percent in value of the stock of Taxpayer, Taxpayer is a “tax-exempt controlled entity” within the meaning of  § 168(h)(6)(F)(iii).





Exempt Organization formed Taxpayer during Month x, Year y, to act as the managing member of the Project LLCs. The Project LLCs own, and are engaged in the rehabilitation of, Project in City, State. The buildings within Project are historic structures and the rehabilitation of Project is intended to qualify for the  § 47 rehabilitation tax credit. The other members of Project LLCs are taxable investors.


The Project was placed in service in Year z. The taxable investors in Project LLCs required Taxpayer to make an election pursuant to  § 168(h)(6)(F)(ii) for Year z when Taxpayer filed its federal income tax for Year z. Taxpayer filed a timely federal income tax return for Year z, but failed to make the  § 168(h)(6)(F)(ii) election on that return. However, from the affidavit, the tax return, and the other materials submitted it is clear that Taxpayer at all times intended to make the  § 168(h)(6)(F)(ii) election. Upon discovering its failure, Taxpayer promptly sought an extension of time in which to file the election.

Applicable Law




 Section 47(a)(2) of the Code provides a rehabilitation credit for 20 percent of the qualified rehabilitation expenditures with respect to any certified historic structure.

 Section 168(h)(6)(A) provides that, for purposes of  § 168(h), if any property which is not tax-exempt-use property is owned by a partnership which has both a tax-exempt entity and a nontax-exempt entity as partners and any allocation to the tax-exempt entity is not a qualified allocation, then an amount equal to such tax-exempt entity's proportionate share of such property shall be treated as tax-exempt use property. Under  § 47(c)(2)(B), expenditures allocable to the portion that is tax-exempt use property (within the meaning of  § 168(h)) are not qualified rehabilitation expenditures.




 Section 168(h)(6)(F)(i) provides generally that any tax-exempt controlled entity shall be treated as a tax-exempt entity for purposes of  § 168(h)(5) and  (6). However, under  § 168(h)(6)(F)(ii), a tax-exempt controlled entity can elect not to be treated as a tax-exempt entity. Such an election is irrevocable and will bind all tax-exempt entities holding an interest in the tax-exempt controlled entity.


 Section 301.9100-1(b) of the Procedure and Administration Regulations defines the term “regulatory election” as including any election the due date for which is prescribed by a regulation.

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 Section 301.9100-7T(a)(2)(i) requires an election under  § 168(h)(6)(F)(ii) to be made by the due date of the tax return for the first taxable year for which the election is to be effective. Thus, the  § 168(h)(6)(F)(ii) election is a regulatory election.


 Section 301.9100-9100-9(c) provides that the Commissioner of Internal Revenue has discretion to grant a reasonable extension of time to make a regulatory election.


 Section 301.9100-1 though  § 301.9100-3 provides the standards that the Service will use to determine whether to grant an extension of time to make a regulatory election.  Section 301.9100-3(a) provides that requests for extensions of time for regulatory elections (other than automatic changes covered in § 301.9100-2) will be granted when the taxpayer provides evidence (including affidavits) to establish that the taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government.

 Section 301.9100-3(b)(1) provides that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer—


- (i) requests relief before the failure to make the regulatory election is discovered by the Service;
- (ii) failed to make the election because of intervening events beyond the taxpayer's control;
- (iii) failed to make the election because, after exercising due diligence, the taxpayer was unaware of the necessity for the election;
- (iv) reasonably relied on the written advice of the Service; or
- (v) reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make the election.

Under  § 301.9100-3(b)(3), a taxpayer will not be considered to have acted reasonably and in good faith if the taxpayer—

- (i) seeks to alter a return position for which an accuracy-related penalty could be imposed under  § 6662 at the time the taxpayer requests relief and the new position requires a regulatory election for which relief is requested;
- (ii) was fully informed of the required election and related tax consequences, but chose not to file the election; or
- (iii) uses hindsight in requesting relief. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

 Section 301.9100-3(c) provides that the Service will grant a reasonable extension of time only when the interests of the Government will not be prejudiced by the granting of relief. The interests of the government are prejudiced if granting relief would result in a taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made.



Analysis

Based on the facts as represented, we have determined that Taxpayer intended from the outset to make the  § 168(h)(6)(F)(ii) election, that its failure to make the election on its original return was inadvertent, and that Taxpayer is not using hindsight in requesting relief. Moreover, Taxpayer


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requested relief before the failure to make the election was discovered by the Service. We also have determined that Taxpayer acted reasonably and in good faith and that the interests of the Government will not be prejudiced by the granting of relief.


Conclusion

Based solely on the facts as represented and the applicable law, we conclude that the request for relief under  § 301.9100-3 should be granted. Accordingly, Taxpayer is granted an extension of time of 60 days from the date of this letter ruling to file an amended return making the election under  § 168(h)(6)(F)(ii). Taxpayer should attach this letter to its amended return.

Although this office has not verified any of the material submitted or facts assumed in support of the request for ruling, they are subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, this letter does not rule on whether Taxpayer is entitled to claim the rehabilitation credit under  § 47(a).

This ruling is directed only to the taxpayer requesting it.  Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.

Enclosed is a copy of the letter showing the deletions proposed to be made when it is disclosed under  § 6110. If you have any questions concerning this matter, please contact the individual whose name and telephone number appear at the beginning of the letter.

Sincerely,

Michael J. Montemurro

Branch Chief

Associate Chief Counsel

(Income Tax & Accounting)

Enclosure:

Copy for  § 6110 purposes

Note: All of above were extracted from RIA Checkpoint through October 10, 2008.