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2016 Priorities for Exempt Organizations Division

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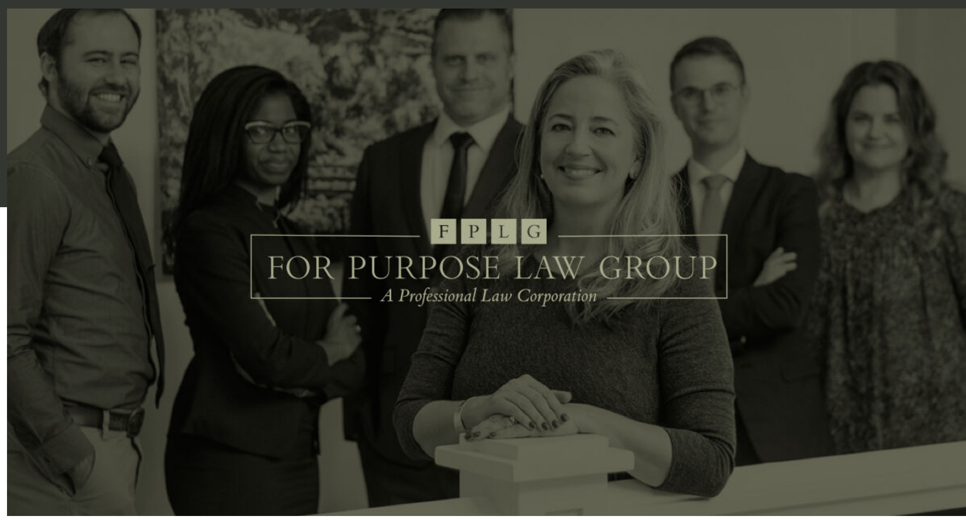

It’s no secret that it’s been a tough year for the Tax-Exempt and Government Entities Division of the IRS.

Actually, it’s been a difficult *few* years for these embattled federal regulators and the philanthropy community they serve.

There was the huge brouhaha surrounding former Division Chief Lois Lerner and allegations of political favoritism in Section 501(c)(4) approvals or denials.

There has been the years-long, enormous backlog of pending 501(c)(3) exemption applications that led officials to introduce the controversial Form 1023-EZ application form. Critics have warned that the 3-page 1023-EZ application is little more than a front-end, rubber-stamp of representations and promises by applicants.

While processing times have significantly improved, the overall success or failure of this program may not be fully known for a while.

And the primary cause of this long waiting time is that the tax agency’s budget has been severely slashed over and over.

Challenges to Planning Priorities

All of these factors are hurdles and challenges for the EO Divisions’ strategic planners when they meet each year to determine priorities and allocation of (scarce) resources for the following fiscal year.

In its recent “TE/GE Priorities for FY 2016,” the Division has stressed that “EO’s overarching compliance strategy is to ensure organizations enjoying tax-exempt status comply with the requirements for exemption and adhere to all applicable federal tax laws.” The goal is “…identifying and addressing existing and emerging high-risk areas of non-compliance” with the best use of its smaller-than-needed budget and workforce.

Examinations Focus

A key part of the Exempt Organization's function is to selectively examine organizations that already have been granted recognition of tax exemption.

> *The focus will be on significant compliance issues, not on the number of cases closed, and some issues may require a multi-year approach. EO will use the most appropriate, cost-effective and least intrusive compliance treatment. This will include educational efforts, compliance reviews, compliance checks, and correspondence and field examinations.*

The agency identifies "areas of high non-compliance risk through stakeholder input, reliable outside data, and public information." The focus will be on five key "issue areas":

- *Exemption*: Agents and examiners will look for "non-exempt purpose activity and private inurement." These are problems that rank high year after year. Notably, this is the only one of the listed categories that the agency indicates will be "enforced primarily through field examination."
- *Protection of Assets:* This category focuses on issues of "self-dealing excess benefit transactions, and loans to disqualified persons." There's, of course, some overlap with the "Exemption" category; the goal is to ensure that charitable funds are used for exempt purposes and not for the personal enrichment of insiders. Enforcement will be "primarily through correspondence and field examination."
- *Tax Gap*: These high-risk areas include "employment tax and Unrelated Business Income Tax liability." Nonprofit employers often overlook their responsibilities for general tax responsibilities that apply to all organizations with workers, both for-profit and nonprofit. The UBIT issue is tricky and complex, leading many organizations astray – even inadvertently. These examinations will be "enforced through compliance checks, correspondence audits, and field examination."
- *International*: The IRS is concerned not only about how U.S. exempt organizations spend their money and conduct activities domestically but also about their foreign operations and expenditures. The targeted examination issues in this category include "oversight on funds spent outside the U.S., including funds spent on potential terrorist activities, exempt organizations operating as foreign conduits, and Report of Foreign Bank and Financial Accounts (FBAR) requirements, enforced through compliance reviews, compliance checks, correspondence audits, and field examination." This comprehensive approach reflects the (sometimes substantiated) suspicions that foreign charities are fronts or

facilitators of terrorism.

- *Emerging Issues*: These areas of risk "include non-exempt charitable trusts and IRC 501(r) organizations." The new 501(r) classification was added to the Internal Revenue Code as a result of passage of the Affordability Care Act, and applies to 501(c)(3)s that run one or more hospital facilities. These audits will focus on "compliance reviews, correspondence audits, and field examination."

Determinations Focus

While the Examinations Section of this IRS Division is geared towards compliance reviews of existing 501(c)(3) organizations, the Determinations Section has the important responsibility of reviewing and approving (or denying) applicants' requests for tax exemption.

Before the introduction in July 2014 of the short-form 1023-EZ, applicants were required to complete a 26-page behemoth and submit considerable documentation about their organization structure and operational plans.

For many smaller applicants, this procedure has been streamlined into what some critics have characterized as "easier" to obtain than "a library card." For the most part, the up-front review will be minimal. In certain selected sample cases, there will be a more in-depth "predetermination review." The agency will also "… continue to review organizations that were granted tax-exempt status through the streamlined determination process and … will begin post-determination compliance enforcement" on organizations that applied through the Form 1023-EZ process."

Conclusion

Against the background of a limited budget, fewer employees, and ongoing scrutiny and controversy, the Tax Exempt and Government Entities (TE/GE) Division is moving forward in FY 2016 to do its best to oversee the administration of the federal tax exemption laws.