

FY2018 IRS Work Plan: Increased Scrutiny and Changes Coming for 501(c)(4) Applications

01.12.17 | Linda J. Rosenthal, JD



Each year, officials at the Internal Revenue Service release a roadmap for the upcoming fiscal year. On September 28, 2017, the agency released its [Tax Exempt and Government Entities FY 2018 Work Plan](#).

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We enter Fiscal Year 2018 as a more cohesive and efficient division than we were even a year ago.

This opening paragraph gives a [glimpse of the struggles](#) that this division has faced in the past several years, brought on – in no small part – by a shrinking workforce, budget cuts, and Congressional animosity arising from controversy over the supposed targeting of certain groups applying for section 501(c)(4), social welfare, status.

Tax Exemption Areas of Focus

Each year, the agency announces certain areas of focus for particular scrutiny. Among the items on the [list for fiscal year 2018](#) are the following:

- *For-profits converted to nonprofits:* There has been an uptick in recent years in entities that previously operated on a business model that have chosen to convert to nonprofit status. Before any such conversion is approved, the former for-profit must jump through many hoops. The FY 2018 Work Plan makes clear that EO officials will monitor these groups to ensure continued compliance with the much stricter requirements for 501(c)(3)

organizations.

- *Private benefit and inurement:* The agency will continue as usual to examine organizations “which show indicators of potential private benefit or inurement to individuals or private entities.” (We’ve previously explained these interrelated but not identical concepts; see [here](#) and [here](#).)
- *Form W-2/1099 matches:* One area of abuse among all types of entities that hire workers is the inadvertent or deliberate failure to properly classify these people as employees vs. independent contractors. It’s important for nonprofits as well as for-profits to get this classification correct; failure can result in consequences including stiff penalties.

Another area of concentration will be the monitoring of newly formed organizations that have recently received tax exemptions through the streamlined Form 1023-EZ. When the new procedure was adopted in mid-2014, a trade-off for the dramatically compressed process was the acknowledgment that an expedited, simpler approval process up front would require significant post-approval compliance efforts. The FY 2018 Work Plan indicates that this monitoring process will continue.

In a related point, the agency “expects to receive an increased number of determination applications in FY 2018...” Accordingly, “in early 2018, EO will implement revisions to the Form 1023-EZ – including a required activity description and additional questions on gross receipts, asset thresholds, and foundation classification. As a result of these changes, EO expects the average processing time for a Form 1023-EZ to increase.

The EO Division will “continue pre-determination reviews of a statistical sample of Form 1023-EZ applications and will continue to analyze the data from these applications to mitigate risks and identify opportunities to improve this form and its instructions.”

New Form 1024-A On the Way

There’s also a new Form 1024-A tax-exemption application on its way, scheduled for rollout in January 2018. That’s right: not a new 1024 that prospective 501(c)(4) organizations file, but a new 1024-A.

Notice was published in the Federal Register in late August, but it now contains a draft dated September 27, 2017. The comment period ended October 23, 2017. The draft is “subject to change and to OMB approval before being officially released.

“Curiously, the [draft Form 1024-A](#) is not mentioned in the [IRS Work Plan](#).” In addition, the draft 1024-A “looks very different from the” existing Form 1024. The draft form includes a statement that it is not to be relied upon for filing purposes, and is subject to change and to OMB approval before being officially released.

So what is this mysterious new tax-exemption application all about? Inquiring minds want to know, but according to the folks at the Public Policy Law Institute –

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[c]onfusion abounds about this new form. It's all the result of a misguided and poorly-drafted amendment to the Internal Revenue Code in 2015.

If you are one of the inquiring minds, check out [this blog post](#), which explains in considerable detail, the source of some of this confusion. Unfortunately, these experts offer a grim prognosis:

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So we're going to have more confusion about c4 applications for recognition, lots of questions that need to be answered on the form, but not for any clear purpose, and more work for we few struggling tax-exempt organization lawyers who have to explain why yet another layer of useless regulation is layered on protected speech. 'Yes, you have the right to associate and speak, but we're going to fine you \$20 a day for the privilege unless you give us this Form and possibly others.'

Conclusion

We'll update you on this and other developments affecting the 501(c)(4) social welfare classification as some of the confusion (hopefully) abates.