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Private Letter Rulings for Nonprofits Curtailed

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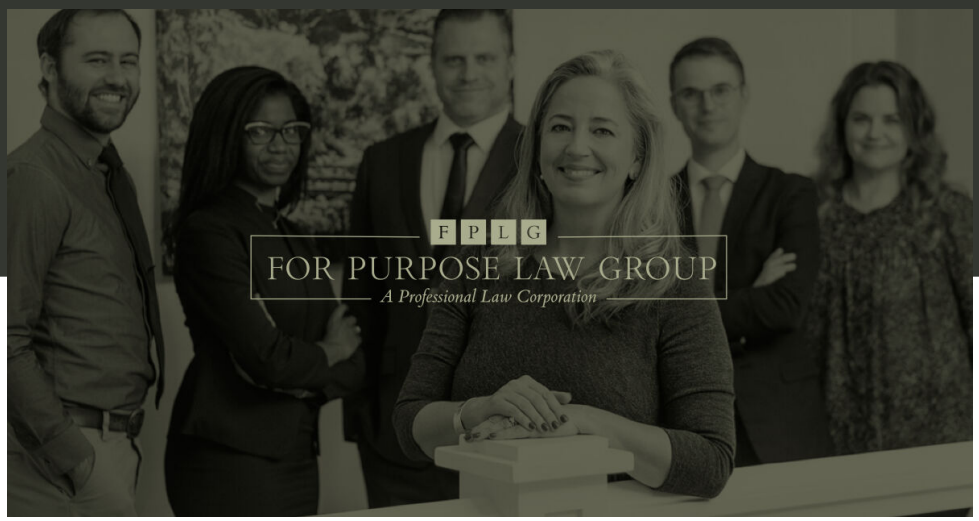

It's been a tough few years for the IRS Division that has primary responsibility to implement the laws for tax-exempt organizations.

The Tax Exempt and Government Entities (TE/GE) Division has endured – together with the IRS, generally – budget cuts and hiring freezes. It's also been caught up in the fallout from the long-running saga of former Exempt Organizations Unit Director Lois Lerner and the purported partisan review of 501(c)(4) organizations.

This has resulted in significant management turnover and disarray, haphazard reorganizations, and reduction of services to the nonprofit community it is tasked with regulating.

For example, the wait-time for approval of tax-exemption applications had swelled to 18 months or longer. The emergency remedy was adoption of a short-form exemption application, the Form 1023-EZ. But critics are slamming that solution as inadequate to do a proper advance screening for eligibility for 501(c)(3) status.

Recently, the IRS issued the annual (2016) rules for requesting advance approval of proposed activities or transactions. Unfortunately, it's another instance of an unfortunate reduction in services; a slashing of a function helpful – (indeed, necessary) – to the successful implementation of the tax-exemption laws and oversight of nonprofit organizations.

Private Letter Rulings: What are They?

If a party – here, a tax-exempt organization – wants to know whether a proposed transaction or change in operations or activities will jeopardize its exemption or cause other problems, it may be able to ask the IRS for advance approval. This is a request for a "private letter ruling (PLR)." Under certain conditions, the agency will review those specific facts and circumstances, analyze applicable law, and issue the PLR. This approval applies only to that organization and that set of disclosed circumstances, and may not be relied on by others or by IRS personnel in connection with any other case.

Each January, the IRS issues a series of documents called "revenue procedures" that detail the types of issues the IRS will entertain in connection with a request for a private letter ruling, and the specific steps to take. These guidance documents also announce the issues on which the agency will not accept requests at all.

Private Letter Rulings Changes for 2016

Tax-exemption law is complicated, and there are many unresolved issues. That's why private letter rulings are such valuable tools to help organizations stay in good-faith compliance.

In earlier years, a tax-exempt organization could request a private letter ruling from the Exempt Organizations Technical Branch (in the Washington, D.C., National Office), the group with the most knowledge of the applicable laws as well as hands-on experience with how nonprofits operate.

The permitted topics included experts whether the planned course of action would either adversely affect the tax-exempt status or would result in unrelated business income tax (UBIT).

There were certain issues that the Technical Branch would not address. For example, they would decline to issue a private letter ruling on matters that turned on factual calculations like whether the price for a proposed transaction was fair market value. They would also stay away from a few specific topic areas, like a 501(c)(3)'s question about entering into a joint venture with a for-profit firm.

2016, however, is an entirely different story. The scope of the permitted topics has been significantly reduced. This year's announcement, in Revenue Procedure ("Rev. Proc.") 2016-4, along with Rev. Proc. 2016-5 and Rev. Proc. 2016-8 "makes clear –

> *that tax-exempt organizations will no longer be able to receive a ruling or any comfort from the IRS that changes in their operations are consistent with their tax-exempt status. In other words, exempt organizations are on their own.*

There's another change, too. In earlier years, an organization could give official written notice to the IRS of a change in its activities. Sometimes, the agency would respond to such a letter, indicating that the changes were consistent with its exempt status, and that the tax-exemption was unaffected. This is no longer allowed. The current Form 990 instructions indicate that the proper way to inform the IRS of a change in activities is by including the notification on the Form 990.

Private Letter Ruling Duties Transferred

In March 2015, IRS Commissioner John A. Koskinen announced that the IRS is "under new management" due to major changes in management staff over the past few years.

Many of these management losses were in the Exempt Organizations Unit (formerly run by Lois Lerner). The Commissioner also explained there were changes in "organization and procedures" in that same – embattled – part of the IRS concerned with exempt organizations.

One significant change is that the responsibility for private letter ruling requests (including ones about "exemption requirements for, and tax treatment of tax-exempt organizations") was transferred away from the exempt organization experts, the EO Technical Branch.

These duties were moved to the Chief Counsel's Office: specifically, the Associate Chief Counsel (TE/GE). They are the official legal advisers for the Internal Revenue Service; note, though, that the staff of the EO Technical Branch are all lawyers, too.

Conclusion

The 2015 reorganization – along with the changes in the 2016 private letter ruling procedures for exempt organizations – have led to considerable confusion. They have also resulted in a counterproductive reduction of needed technical advice services to the nation's tax-exempt groups.