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NONPROFITS: INTERNAL REVENUE SERVICE

Tax Legislation: What was Left Out (Nonprofits)

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In *Nonprofits: What's in the New Tax Law*, we reported on the items of interest to nonprofits that had made their way into the final version of H.R.1, the Tax Cuts and Jobs Act that was signed into law at the White House.

Other proposals in the legislative package dropped off, especially in the December 2017 rush to put together a tax overhaul that would pass both the House of Representatives and the Senate. The final package was a cobbled-together menu of provisions that would bring in enough "yes" votes without losing too many potential "nos," and would make it past any procedural hurdles that apply when a "budget reconciliation" path (just 51 Senate votes needed) is chosen by Congressional leadership.

The tax legislation that was recently enacted was not a slow, thoughtful overhaul of the Internal Revenue Code so that the end result could be viewed as a purposeful and coherent tax policy statement.

Instead, bits and pieces of what was considered even briefly but ultimately omitted will likely pop up sooner or later in new bills. Anything that showed up in any preliminary version or tweaking of the tax act was an item of at least some interest to one legislator or another, and it's worth taking a look at what those items actually were.

Johnson Amendment: A Tax Act Survivor

The most significant item that may have – but didn't – make it into the new tax law was the elimination or at least modification of the politics ban on 501(c)(3) organizations – the Johnson Amendment. This has long been high on the wishlist of the GOP. Although we'll do a separate post on the post-Tax Act status of this significant omission, it's important to mention it first here briefly.

The proposed politics-ban change that emerged from the House of Representatives went through its own significant twists and turn but the final version would have allowed all 501(c)(3)s, not just religious ones, to engage in limited political activity.

The Senate version did not include any proposed changes, but the Senate conferees were ready to accept the House version until the Senate Parliamentarian firmly nixed it on procedural grounds under the “Byrd Rule.” When news broke that the final tax bill conference language would omit any Johnson Amendment change, many in the philanthropic community breathed a huge sigh of relief and declared “victory.”

This was a temporary reprieve in this long war about 501(c)(3)s and politics. The GOP’s gun jammed during this current battle, but it will be able to reload the weapon soon enough and continue forward.

Also, don’t forget that there’s a peculiar Executive Order – issued in May 2016 – that purports to block enforcement of the Johnson Amendment

More Tax Act Omissions

When the dust settled on the frantic tax-law writing – literally, handwritten notes in margins – and horse-trading to get each and every Senate vote, some provisions that might have made it in the final legislation got left on the cutting-room floor.

Like the future of the Johnson Amendment, one or more of these omitted items will likely pop up again:

Donor-Advised Funds

Donor-advised funds are the hot-ticket charitable-giving vehicle these days. As such, there are proponents as well as detractors. Congress and federal tax officials have taken an interest recently, particularly in the argument of DAF critics that too much money is being hoarded and not enough currently spent on charitable purposes.

So it’s no surprise that the House version included a requirement that community foundations and other DAF sponsors add information to their Form 990s showing the average amount of grants made during each year as a percentage of assets. The House bill also would have required these 990 filers to show whether they have a “policy” regarding the frequency and minimum level of distributions from their funds.
The final conference report omitted any such reporting requirements for sponsoring organizations of donor-advised funds.

“Newman’s Own” Exception

The late actor Paul Newman created a highly successful business of organic food companies. He also established a foundation to facilitate charitable giving by using the profits from the Newman businesses. Under a 1969 tax law provision, this type of arrangement (private foundations owning a large stake in a for-profit business) will result in a 200% excise tax imposed on the foundation in November 2018, in which case the foundation would have to sell its food business and dissolve.

The House bill would have created an exception to the general rule that a foundation cannot finance charitable giving using profits from its businesses. The Senate conferees were inclined to go along with this change approved in the House, but – again – the "Byrd Rule" became a technical obstacle. The Senate Parliamentarian officially ruled that the House's provision was not "germane" to the tax bill, so it had to be tossed.

Private Museum Restrictions

Last year, there was a splashy New York Times expose on the recent trend of ridiculously wealthy art collectors creating "art museums" on their private property and taking huge tax deductions for "donated" art. Congress took an interest and opened a probe. Originally, lawmakers included a provision in the tax overhaul requiring so-called art museums to be open to the public for a minimum specified number of hours. It did not survive the final cut, though. For the time being, at least, these art connoisseurs can gaze at these treasures in splendid privacy most of the time.

Unrelated Business Income Tax

While there were some significant changes to the UBIT rules in the final tax legislation, one provision did not make it all the way through the final cuts. There is no language that would have "clarified" that all 501(c) exempt entities are subject to the unrelated business income tax rules, even if their exemption under other Code provisions says so.

PF Investment Income Excise Tax

Under current law, private foundations are subject to varying levels of excise tax on their net investment income. Lawmakers proposed replacing existing rules with a single, 1.4% rate. This proposed "simplification" was not included in the final conference version passed by the House and Senate.

Taxation of Tuition Benefits

A proposal that launched howls of protest from many quarters was to repeal the exclusion from gross income for certain tuition reduction and other employer-provided educational assistance benefits offered to graduate students. Opponents argued it would kill off many graduate programs and cause severe hardship to current advanced degree-seekers. This trial balloon was mercifully blown out of the sky.

UBIT Research Income Exclusion

Lawmakers considered a change to the current exclusion from the unrelated business income tax of research income. That exclusion has been left untouched.

Private Activity Bonds

The new tax law does not incorporate an earlier House bill that would have repealed about 25% of the tax-exempt bond market by imposing a tax on interest earned on all "private activity" bonds. This would have included 501(c)(3) bonds, exempt facility bonds, and student loan bonds, among others.

Conclusion

Not to sound like a broken record, but these omissions from the final Tax Cuts and Jobs Act of 2017 are not necessarily gone for good. They are just gone for now. In many instances, there was no particular rhyme or reason why certain 501(c)(3)-related proposals made it to the finish line, while others did not.

Observers are also curious about the fate of other items that could have – but didn't – get past the starting line. For instance, there's been a lot of chatter in recent months about the use and abuse of the "conservation easement" – the so-called the "billion-dollar" loophole. Apparently, no serious consideration of any changes to existing rules was given during this current tax-legislation round. Reportedly, though, some Very Influential People are fond of this tax break, so perhaps it's no surprise that it escaped notice this time around.