

Non-Profits & Association Forums: Exempt Organizations (2015) Year in Review

Association of Corporate Counsel National Capital Region

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Celia Roady



Celia Roady is a partner in Morgan Lewis’s Tax Practice. Celia focuses on tax and governance issues affecting tax-exempt organizations, including charities, foundations, colleges and universities, museums, and other nonprofit organizations. She was appointed by the Internal Revenue Service to be a member of its Advisory Committee on Tax-Exempt and Government Entities for 2010-2013. She has also been named by *Legal Times* as one of Washington, D.C.'s "leading lawyers" in the tax field and is listed in *Chambers USA: America's Leading Lawyers for Business* (2005–2015) and *The Best Lawyers in America* (2007–2016). She chairs the annual conference on “Representing and Managing Tax-Exempt Organizations,” sponsored by the Georgetown University Law Center. In 2004-2005, Celia served on the Governance Work Group of the Panel on the Nonprofit Sector, which was convened by Independent Sector to provide comments to the Senate Finance Committee. Celia is a graduate of Duke University, Duke Law School, and Georgetown Law School (LL.M.).

Cindy Lewin



Cindy Lewin is Executive Vice President and General Counsel at AARP. Before joining AARP in June 2010, Cindy served as general counsel at two other large national nonprofit organizations, the National Wildlife Federation and Volunteers of America, for twelve years, where she also served as Secretary or Assistant Secretary and had human resources, office services, facilities, and information technology reporting to her at various times. Before moving in-house, she was a partner at Lichtman, Trister, Singer & Ross, where her practice focused exclusively on nonprofit organizations, and prior to that she practiced at Arnold & Porter. Cindy is past chair of the Exempt Organizations Committee of the D.C. Bar Tax Section and also past chair of the Nonprofit Organizations Committee of the Association of Corporate Counsel. She was named one of “Washington’s Most Influential In-House Counsels” by *Legal Times* in 2011. In 2013, under her leadership, the AARP Office of General Counsel was recognized for Best Outside Counsel Management by the *National Law Journal*, and in 2014, won the In-House Innovators Award from the Association of Corporate Counsel – National Capital Area. Cindy served on Independent Sector’s 2014 Ethics and Accountability Advisory Group, and is on the Board of Directors of the National Human Services Assembly. Cindy is a graduate of Yale Law School and Wellesley College.

Alexander Reid



Alexander Reid is a partner in Morgan Lewis's Tax Practice where he advises tax-exempt organizations of all varieties, including charities, foundations, colleges and universities, museums, and other nonprofit organizations. Alex also counsels taxpayers seeking administrative guidance from the Internal Revenue Service and Treasury Department as well as on legislative matters with the U.S. Congress. Prior to joining Morgan Lewis, Alex served as legislation counsel for the Joint Committee on Taxation, where he advised members of Congress and staff regarding tax policy and drafted legislation, hearing publications, and technical explanations of tax legislation. He also served at the U.S. Department of Treasury, Office of Tax Policy, as a tax policy fellow. Alex is the former chair of the D.C. Bar Tax Section Steering Committee and the D.C. Bar Tax-Exempt Organizations Committee. He currently chairs the American Bar Association Tax-Exempt Organizations Current Developments Committee and serves as Continuing Legal Education liaison for the D.C. Bar Tax Section. Alex is a graduate of Yale University and New York University School of Law (J.D. and LL.M.).

Katherine Karl



Katherine Karl is the Deputy General Counsel of the American Cancer Society, where she leads the team that handles the legal issues that arise out of the public policy activities of the Society and its advocacy affiliate, the American Cancer Society Cancer Action Network, as well as the employment, litigation and tax issues faced by both entities. Before coming to the Society, Kate was in private practice with Caplin & Drysdale in the Exempt Organizations Group, where she advised a wide variety of tax-exempt organizations. Prior to her work with the firm, Kate was a law clerk for a federal district court judge in the Southern District of New York. Before attending law school, she worked on Capitol Hill for a senior senator and the Senate's Health, Education, Labor and Pensions Committee. Kate is a graduate of Cornell University and Yale Law School.

Exempt Organizations: 2015 Year in Review and a Look Ahead to 2016 Election Season

- 2015 was an eventful year in the EO world
 - Last minute tax legislation was included in the Consolidated Appropriations Act that Congress passed in December 2015; the bill included some significant change for EOs
 - Treasury/IRS issued several guidance projects affecting EOs
 - State AG litigation focused on 990 disclosure issues
 - 2016 campaign season will create both opportunities and challenges for 501(c)(3) organizations

2015 Legislative Developments

2015 Legislation: Permanent Extensions

- Sec. 111. – Permanently extends the charitable deduction for contributions of real property for conservation purposes and the enhanced deduction for certain individual and corporate farmers and ranchers.
- Sec. 112. – Permanently extends the ability of individuals at least 70½ years of age to exclude from gross income qualified charitable distributions from Individual Retirement Accounts
- Sec. 113. – Permanently extends and modifies the enhanced deduction for charitable contributions of inventory of apparently wholesome food for non-corporate business taxpayers.
- Sec. 114. – Permanently extends the special rule permitting exempt organizations with certain binding written contracts in effect on August 17, 2006 to receive payments of interest, annuities, rents and royalties from a controlled organization without recognizing UBIT, to the extent that the payments do not exceed fair market value.
- Sec. 115. – Permanently extends the rule providing that a shareholder's basis in stock of an S corporation is reduced by the shareholder's pro rata share of the adjusted basis of property contributed by the S corporation for charitable purposes.

2015 Tax Legislation: New EO Provisions

- Educational Institutions and Qualified Tuition Expenses
 - Sec. 212 – Reforms the reporting requirements for Form 1098-T so that educational institutions are required to report only qualified tuition and related expenses actually paid, rather than choosing between amounts paid and amounts billed, as under current law. The provision applies to expenses paid after December 31, 2015 for education furnished in academic periods beginning after such date
- Agricultural Research Organizations
 - Sec. 331. – Agricultural research organizations will be treated as public charities *per se*, without regard to their sources of financial support. The provision is effective for contributions made on or after the date of enactment
- Charitable Remainder Unitrusts
 - Sec. 344. – Clarifies the valuation method for the early termination of certain charitable remainder unitrusts. The provision is effective for the termination of trusts after the date of enactment

2015 Tax Legislation: IRS Administration Provisions Affecting EOs

- Administration – IRS Reforms
 - Sec. 404. – Requires the IRS to create procedures under which a 501(c) organization facing an adverse determination may request administrative appeal to the IRS Office of Appeals, including determinations relating to the initial or continuing classification of:
 - An organization as tax-exempt under section 501(a)
 - An organization described under section 170(c)(2)
 - A private foundation under section 509(a)
 - A private operating foundation under section 4942(j)(3)
 - Sec. 405. – Eliminates self-declaration for 501(c)(4) organizations. Requires 501(c)(4) organizations to file a notice of registration with the IRS within in 60 days of the organization's formation. The IRS recently issued Notice 3016-9 extending this date until 60 days from the date that the IRS issues regulations.
 - Sec. 406. – Permits 501(c)(4) organizations and other exempt organizations to seek review in Federal court of any revocation of exempt status by the IRS

2015 Tax Legislation: IRS Administration Provisions Affecting Eos (cont'd)

- Administration – IRS Reforms (cont'd)
 - Sec. 407. – Clarifies that taking official action for political purposes is an offense for which an IRS employee should be terminated. The bill amends the Internal Revenue Service Restructuring and Reform Act of 1998 to expand the grounds for termination of employment of an IRS employee to include performing, delaying, or failing to perform any official action (including an audit) by the IRS employee for the purpose of extracting personal gain or benefit for a political purpose
 - Sec. 408. – Treats transfers to organizations exempt from tax under sections 501(c)(4), (c)(5), and (c)(6) as exempt from the gift tax

2015 Tax Legislation: Treasury Appropriations

- Sec. 127 – Prohibits Treasury from issuing, revising, or finalizing any regulation, revenue ruling, or other guidance not limited to a particular taxpayer relating to the standard which is used to determine whether an organization is operated exclusively for the promotion of social welfare for purposes of section 501(c)(4)
- Also provides that “the standard and definitions as in effect on January 1, 2010, which are used to make such determinations shall apply after the date of the enactment of this Act for purposes of determining status under section 501(c)(4) of such Code of organizations created on, before, or after such date”

Treasury/IRS Developments

2015-2016 IRS Priority Guidance Plan First-Quarter Update Released

- 2016 projects outlined for Exempt Organizations
 1. Rev. Proc. updating grantor and contributor reliance criteria under sections 170 and 509
 2. Rev. Proc. to update Rev. Proc. 2011-33 for EO Select Check
 3. Proposed regulations under section 501(c) relating to political campaign intervention
 4. Final regulations and additional guidance on section 509(a)(3) supporting organizations
 5. Guidance under section 512 regarding methods of allocating expenses relating to dual use facilities
 6. Final regulations under section 529A on Qualified ABLE Programs. Proposed regulations were published on June 22, 2015
 7. Guidance under section 4941 regarding a private foundation's investment in a partnership in which disqualified persons are also partners

2015-2016 IRS Priority Guidance Plan First-Quarter Update Released (cont'd)

- 2016 projects outlined for Exempt Organizations (cont'd)
 8. Final regulations under sections 4942 and 4945 on reliance standards for making good faith determinations (published 09/25/15 as TD 9740)
 9. Final regulations under section 4944 on program-related investments and other related guidance (published 09/28/15 in IRB 2015-39)
 10. Guidance regarding the excise taxes on donor advised funds and fund management.
 11. Guidance under section 6033 relating to the reporting of contributions
 12. Final regulations under section 6104(c). Proposed regulations were published on March 15, 2011
 13. Final regulations under section 7611 relating to church tax inquiries and examinations. Proposed regulations were published on August 5, 2009

TE/GE FY 2016 Priorities Report

- Tax-Exempt and Government Entities Division Priorities for FY 2016 Report was released on October 1, 2015
- Projects a 3% increase in exemption applications in FY 2016
- In FY 2016, EO Rulings and Agreements anticipates having 100 determination specialists (down from 130) to review Forms 1023 and 1024 and to review sampled predetermination Forms 1023-EZ
- The 30 EO determination specialists pulled from EO Rulings and Agreements will be re-assigned to EO Examinations for FY 2016
- Streamlined case processing and continued improvements from the Lean Six Sigma recommendations are projected to mitigate the loss of the determination employees

TE/GE FY 2016 Priorities Report (cont'd)

- In addition to the determination specialists, 25 Tax Examiners will be reviewing the Form 1023-EZ
- Compliance risk with the Form 1023-EZ and the percentage of Forms 1023-EZ selected for pre-determination review will continue to be monitored
- Now assigning determinations applications directly to specialists rather than waiting for requests by agents or managers for new cases
- Cases will now be closed within 35 days if an applicant fails to respond to a request for additional information, as opposed to the previous 90 day window
- Not expecting longer processing times even with fewer staff and more applications

Notice 2015-62: Impact Investing

- On September 15, 2015, the IRS issued Notice 2015-62, confirming that private foundation managers may consider the relationship of an investment to the foundation's charitable purpose when determining if an investment is prudent under section 4944
- The guidance brings the prudent-investor standard for jeopardizing investments in line with state law (the Uniform Prudent Management of Institutional Funds Act)
- Notice 2015-62 was prompted by the White House's announcement about public-private partnerships in the clean energy sector to fund climate change solutions
- The White House initiative has garnered commitments of more than \$4 billion from major foundations, institutional investors and other long-term investors

Substantiating Charitable Contributions

- On September 17, 2015, the IRS proposed regulations for donee organizations to file information returns that would satisfy the substantiation requirement for charitable contributions of \$250 or more
- Currently, the donor must file a contemporaneous written acknowledgement to substantiate donations of \$250 or more.
- Under the proposed regulations, a donee organization could elect to file an information return to satisfy the substantiation requirement, which return would need to be filed with the IRS (and a copy provided to the donor) by February 28th of the year following the contribution
- The IRS proposed to develop a specific-use information return for donee reporting
- Comments were overwhelmingly adverse and proposed regulations were withdrawn on January 7, 2016

T.D. 9740: Foreign Equivalency Determinations

- On September 25, 2015, the IRS published final regulations for private foundations making good faith determinations that a foreign organization is equivalent to a public charity or private operating foundation (Treas. Reg. section 53.4942(a)(3)-(6)(i))
- The regulations finalized provisions in the proposed regulations that expanded the category of qualified tax practitioners on whose opinions foundations may rely in making equivalency determinations and eliminated foundations' ability to rely solely on grantee affidavits
- Qualified tax practitioners include attorneys serving as a foundation's in-house or outside counsel, CPAs, and enrolled agents who are subject to Circular 230
- An equivalency determination will generally be valid for two years

T.D. 9746: Type III Supporting Organizations

- On December 21, 2015, the IRS published final regulations on the payout requirements for non-functionally integrated Type III supporting organizations, adopting without major change the temporary regulations published in 2012
- Non-functionally integrated Type III supporting organizations must distribute annually a “distributable amount” equal to the greater of 85 percent of adjusted net income or 3.5 percent of the fair market value of the supporting organization’s nonexempt-use assets
- The preamble to the final regulations indicate that Treasury intends to publish proposed regulations “in the near future” that would:
 - Propose removal of the provision in these final regulations that reduces the distributable amount by the amount of taxes subtitle A of the Code imposes on a supporting organization during the immediately preceding taxable year
 - Propose specific rules regarding the requirements for Type III supporting organizations that support governmental supported organizations to be treated as functionally integrated Type III supporting organizations
 - Provide transition relief beyond the period provided in Notice 2014-4, 2014-2 IRB 274

Judicial Developments

Citizens United et al. v. Eric Schneiderman

- On July 27, 2015, the United States District Court for the Southern District of New York denied Citizens United a preliminary injunction to prevent the New York attorney general from requiring registered charities to disclose identifying information and major donors' contributions in order to solicit funds in the state, finding that the group is not likely to succeed on the merits of their claims
- On August 24, Citizens United filed a Notice of Interlocutory Appeal to the Second Circuit, but withdrew the appeal on October 23 following the filing of an amended complaint on October 21
- Defendant filed a motion to dismiss the amended complaint on November 20, and Citizens United filed its opposition on December 21
- The motion is still pending

Center for Competitive Politics v. Harris

Writ of Certiorari to SCOTUS

- On May 1, 2015, the Ninth Circuit affirmed the district court's denial of CCP's request for a preliminary injunction to prevent California from requiring it to disclose the names and contributions of significant donors on its Form 990 Schedule B to maintain its registered status to solicit funds in the state
- On November 9, the Supreme Court denied certiorari to CCP

Parks v. Comm’r, 145 T.C. 12 (2015)

- The IRS determined that a private foundation’s expenditures of \$639,073 over a three year period to produce and broadcast radio messages in Oregon in the weeks or months preceding statewide elections in which Oregonians voted on measures proposed by initiative or referral were taxable expenditures under section 4945
- A “taxable expenditure” includes amounts paid or incurred by a private foundation for “to carry on propaganda, or otherwise to attempt, to influence legislation” and “for any purpose other than one specified in section 170(c)(2)(B)”
- A communication will be treated as an “attempt to influence legislation” under the definition of direct lobbying communication if such communication “refers to specific legislation” and “reflects a view on such legislation”
- Based on the examples for grass roots lobbying, the Tax Court held that a communication can “refer to specific legislation” if it “employs terms widely used in connection with the measure or describes the content or effect of the measure”—the communication need not refer to the legislation by name

Parks v. Comm’r, 145 T.C. 12 (2015) (cont’d)

- “Reasoned written legal opinion” under section 53.4945-1(a)(2)(vi)
 - Legal counsel’s written response to taxpayer’s request for review of the radio messages stated “We have reviewed the text of radio spot M61#1. The Foundation is not permitted to support or oppose any political candidate or any ballot measures. . . . The conclusion of this radio spot is close to an endorsement of the ballot measure, but we do not think it goes too far”
 - Tax Court held that this did not constitute a “reasoned written legal opinion” because it did not “address the facts of the radio message or the substance of the applicable law, such as describing how the statements in the message are similar to, or distinguishable from, the regulatory examples that delineate what constitutes ‘reflect[ing] a view on’ a ballot measure for purposes of defining a ‘direct lobbying communication’.”
 - However, legal counsel’s written advice stating: “we urge you to simply stay focused on the facts. Do not succumb to emotion or generalizations of ‘good’ or ‘bad’ or ‘conservative’ or ‘liberal.’ It is certainly acceptable to use humor, sarcasm and imagery as long as they do not obscure the factual basis of your message” qualified as a “reasoned written legal opinion”

A Look Ahead: 2016 Election Year Issues for 501(c)(3) Organizations

Prohibition on Campaign Intervention: Basic Rules

- 501(c)(3) organizations are prohibited from participating or intervening in a political campaign on behalf of or in opposition to a candidate for public office
- Unlike the lobbying rules, there is no “insubstantial” exception. Engaging in *any* amount of campaign intervention is grounds for revocation of 501(c)(3) exemption
- Even minor violations can lead to an IRS audit, which is time-consuming, expensive, and may result in the IRS raising other issues
- The prohibition on campaign intervention applies to both U.S. and foreign elections

Campaign Intervention: Facts and Circumstances

- Some but not all “political” activities constitute campaign intervention
- The IRS uses a “facts and circumstances” test to determine whether an activity or communication is permissible or not
- Facts and circumstances tests involve weighing multiple factors and are inherently imprecise and susceptible to varying interpretations
- 501(c)(3)s that are heavily involved in advocacy campaigns and lobbying need to implement policies to demonstrate compliance

Defining Campaign Intervention: What Activities Are Permissible

- Direct lobbying of incumbents on legislative issues without reference to an upcoming election
- On-going issue advocacy that does not refer to a candidate or an election and is not made in connection with an election
- Providing background research to candidates on an even-handed basis
- Nonpartisan voter education that covers all major candidates and focuses on multiple issues; this includes debates, forums, town halls

Defining Campaign Intervention: What Activities Are Not Permissible

- Making communications that reflect positively or negatively on candidates or political parties, including through the use of code words such as “Tea Party”
- Engaging in issue advocacy that links candidates favorably or unfavorably to particular issues
- Preparing or reviewing issue papers for individual candidates; providing information to candidates on a selective basis
- Assisting leadership from only one party regarding issues or strategy for developing the party platform
- Using a 501(c)(3)s resources (including phone, fax, PDA, copier, mailing list, etc.) to carry out personal campaign intervention

Defining Campaign Intervention: Treatment of Issue Advocacy

- The IRS holds that 501(c)(3)s can take positions on public policy issues, including those that divide candidates. However, they must avoid any issue advocacy that functions as campaign intervention
- Issue advocacy can result in impermissible campaign intervention even if the statement does not refer to a candidate
- The IRS uses a facts and circumstances test to determine whether issue advocacy constitutes campaign intervention. Key facts include:
 - whether the statement identifies one or more candidates (unfavorable)
 - whether the statement expresses approval or disapproval for candidates' positions (unfavorable)
 - whether the statement is delivered close in time to an election (unfavorable)

Defining Campaign Intervention: Treatment of Issue Advocacy (cont'd)

- whether the statement addresses an issue that divides the candidates (unfavorable)
- whether the organization regularly makes similar statements on the same issue outside the election cycle (favorable)
- whether the timing of the statement relates to a non-election event, such as an upcoming vote by an incumbent (favorable)
- The uncertainty inherent in applying the facts and circumstances test means that issue advocacy referring to a candidate or relating to issues dividing the candidates should generally be avoided in an election year. A limited exception may apply if the issue advocacy is directed to an upcoming vote scheduled on a particular issue

Defining Campaign Intervention: Election Year Lobbying

- The IRS takes the view that grassroots lobbying can constitute campaign intervention if the communication refers to candidates, directly or indirectly, and reflects support or opposition for positions taken by the candidates. This can include criticism of past positions taken by incumbents
- 501(c)(3)s are not prohibited from engaging in grassroots lobbying during an election year but must tailor the message to avoid inadvertent campaign intervention
- During an election year, lobbying messages should avoid being favorable to or critical of candidates or incumbents or mentioning the upcoming election. Messages should focus instead on the underlying policy rationale for the advocacy

Defining Campaign Intervention: Websites And Social Media

- The IRS takes the position that 501(c)(3)s are responsible for the content on their own websites, as well as on any websites to which they link
- 501(c)(3)s should not link to candidate websites, candidate speeches, or articles about candidates
- 501(c)(3)s that host chat rooms or discussion groups on their websites or in other social media may be held responsible for content posted on those sites by others
- Disclaimers may not prevent attribution of statements by others for purposes of the campaign intervention prohibition

Defining Campaign Intervention: Candidate Appearances at Events

- Candidate appearances, particularly in relatively close proximity to an election, may be construed as campaign intervention
- If a candidate is invited to an event in his or her capacity as a candidate, the opposing candidate should be offered the opportunity to attend the same or an equivalent event
- If a candidate is invited to an event in a non-candidate capacity, there needs to be a clear relationship between the organization and the basis for the invitation. For example, a breast cancer organization may invite a candidate/breast cancer survivor to an event on that subject. In such case, the introduction should not mention her candidacy, and the candidate should be cautioned not to mention the upcoming election in her remarks