COMMENTS PURSUANT TO INTERNAL REVENUE SERVICE ANNOUNCEMENT 2002-92, 2002-41 I.R.B. 709 ON PROPOSED REVISIONS TO IRS FORM 1023 AND INSTRUCTIONS

In Announcement 2002-92, 2002-41 I.R.B. 709 (Oct. 15, 2002), the Internal Revenue Service solicited comments regarding proposed revisions to IRS Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, and the accompanying Instructions for Form 1023.

The following Comments are the individual views of the members of the Section of Taxation who prepared them and do not represent the position of the American Bar Association or the Section of Taxation.

These comments were prepared by individual members of the Committee on Exempt Organizations of the Section of Taxation and its Form 1023 Task Force. Principal responsibility was exercised by Eve Borenstein, LaVerne Woods, and Betsy Buchalter Adler. Substantive contributions were made by Wendell R. Bird, Boyd Black, Michael A. Clark, Susan A. Cobb, Jennifer L. Franklin, Lauren K. Mack, Shannon K. Nash, Jennifer I. Goldberg Reynoso, Michael I. Sanders, Robin A. Smith, and T. J. Sullivan. The comments were reviewed by Richard S. Gallagher of the Section’s Committee on Government Submissions, by Carolyn M. Osteen, Council Director for the Committee on Exempt Organizations, and by Victoria B. Bjorklund, Chair of the Committee on Exempt Organizations.

Although many of the members of the Section of Taxation who participated in preparing these comments and recommendations have clients who would be affected by the federal tax principles addressed, or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a governmental submission with respect to, or otherwise influence the development or outcome of, the specific subject matter of these comments.

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EXECUTIVE SUMMARY

Every year, tens of thousands of charities apply to the Internal Revenue Service for recognition of their tax-exempt status by submitting IRS Form 1023, Application for Recognition of Exemption under Section 501(c)(3) of the Internal Revenue Code. The IRS recently released a draft of a substantially revised Form 1023, and, in Announcement 2002-92, 2002-41 I.R.B. 709 (Oct. 15, 2002), the IRS solicited comments to proposed revisions to Form 1023.

The proposed changes include the addition of substantial background information designed to serve as a guide for applicants, expanded instructions that include educational information, and the addition of many new questions, including more than twenty new “yes/no” questions that request information not specifically addressed in the current form. The Form 1023 Task Force’s comments address in detail first the new background information and instructions and then the form itself. In many instances the comments provide suggested alternative text.

The Task Force commends the IRS’s efforts to transform the form and instructions into a “plain language” document, and the educational outreach that the proposed changes reflect. The length of the comments reflects the Task Force’s desire to be responsive and helpful, the complexity of the form, the in-depth analysis necessary to determine an applicant’s qualification under Section 501(c)(3), and the multiple goals that the form and its instructions serve.
I. OVERALL COMMENTS

As members of the Committee on Exempt Organizations of the American Bar Association, Section of Taxation, we welcome the opportunity to respond to the request for comments on IRS Announcement 2002-92, regarding the IRS Form 1023 Application for Recognition of Exemption under Section 501(c)(3).

We salute the IRS EO Determination Customer Satisfaction Team for taking on the daunting, yet critically important, task of overhauling the Form 1023 and the associated Instructions. The draft reflects the Service’s obvious dedication to the goal of clarifying the application process and the underlying legal principles for applicants, and makes considerable progress in that regard. It is evident that the IRS is striving to create a process that is more accessible, an application that is easier to complete, and instructions that are more educational for users, as well as a form that facilitates expeditious handling of applications. We support plans to implement an interactive Form 1023 that can be completed online.

We hope that our comments will suggest further measures to accomplish the goals that we share for the determination process. We also hope that the re-evaluation of the determination process will not end with the current review of the Form 1023. We hope that the IRS agenda will include attention to larger policy issues concerning the determination process beyond the scope of the current review. These issues include 1) a review of whether the five-year advance ruling period, the Form 8734 Support Schedule for Advance Ruling Period, and the Form 8734 review process are effective and meaningful; 2) consideration of whether a “Form 1023-EZ” is a feasible option for small organizations, e.g., those below the $25,000 annual threshold for filing Form 990; and 3) consideration of whether the public support tests under Treasury Regulation § 1.170A-9(e) can be simplified and harmonized with those at Treasury Regulation § 1.509(a)-3 to eliminate needless complexity and confusion.

II. RESPONSES TO SPECIFIC IRS QUESTIONS

1. Are the key items captured on the cover check sheet? For the most part, yes. Please see detailed comments below.

2. Is the Overview section of the instructions resourceful or would it be better in another document, such as Publication 557? The Overview section of the Instructions is useful to an applicant and should be retained in the Instructions. As discussed in detail below, however, the Overview is directed primarily to public charities and is misleading and inaccurate with respect to private foundations. See detailed comments below.

3. Do the instructions help you to better understand the determination letter process? In some ways, yes. In some respects, however, they are rather confusing. See detailed comments below.

4. Are the application and the instructions easy to understand? The application and the Instructions are easiest to understand when both are
read simultaneously together. An applicant who is not accustomed to completing forms may have difficulty answering many of the questions in the application without consulting the Instructions. See detailed comments below.

5. **Are the application and instructions technically accurate?** Generally yes, subject to a variety of technical points discussed below.

6. **Will applicants be able to complete the form in less time than the current form?** No. Many of the questions in the draft Form 1023 need to be read simultaneously with the accompanying Instructions, which will result in applicants taking more time to complete the Form. In addition, the broader scope of the questions asked (e.g., relationships with directors and approval of such relationships; intellectual property rights) will likely result in greater preparation time.

7. **Based on the questions in the application along with the instructions, do you anticipate that there will be fewer contacts for additional information?** Possibly. The enhanced educational information in the Instructions, e.g., regarding the organizational test, should diminish the need for additional contacts. In addition, because the “yes” or “no” type questions in the draft Form 1023 are more specific and cover more topics than the questions contained in the current Form 1023 there should be fewer contacts for additional information.

### III. COMMENTS ON OVERVIEW AND INSTRUCTIONS

**A. Cover Sheet.**

1. The Instructions explain that “you” and “your” refer to the applicant organization. Including this information on the cover sheet, as well as in the Instructions, will reduce the likelihood of confusion.

2. To increase the chances of receiving a properly certified copy of the governing documents, the check-box Instructions should say: “An exact copy of your complete organizing documents, certified by the Secretary of State if you are a corporation or by the appropriate party if you are a charitable trust (see Instructions).”

3. The Instructions make clear that the “other knowledgeable person” that the IRS may contact for more information must be either an officer, director, or trustee, or a person authorized on Form 2848. We suggest modifying the cover sheet to say “or other knowledgeable person listed on Form 2848.”

4. The request for a “detailed description of your specific activities” should add “actual and planned.”

5. The cover sheet should include the address where the application is to be sent.
6. While the cover sheet captures the key items, applicants may confuse it with the instructions on how the package should be assembled. It may be helpful to add another box that refers to the assembly order of the entire package on page 5 or a statement similar to the “Where to File” statement at the end of this list of boxes. For example:

See Assembly Order of Application Package in the General Instructions for the order in which the application package should be assembled.

B. Overview of Section 501(c)(3) Organizations.

1. General Comments.

We applaud the move to include educational background materials on Section 501(c)(3) organizations within the Instructions to the Form 1023. Overall we support this approach. It seems more helpful to the applicant to have all basic information contained in a single publication, rather than referring the applicant to separate documents, such as Publication 557.

We recognize that it is difficult to strike a balance between providing sufficient information to the applicant to facilitate complete and accurate preparation of the form, and overwhelming the applicant with too much information, in too much detail, that may not be of relevance to the particular applicant. We have suggested specifically some areas where we believe the information in the Overview could be augmented, on the one hand, and eliminated, on the other hand.

We also recognize the tension between explaining legal concepts in plain language, and at the same time being completely accurate from a technical standpoint. Much of the difficulty in this area of course arises from the inherent complexity of the law, and there is no easy solution. We have identified instances where we believe that concepts could be described in a more approachable manner, and, conversely, where we believe that technical accuracy has been sacrificed to too great a degree. To the extent possible we have provided suggested replacement language.

Specific comments follow, identified by the Instructions section heading, in the order in which they appear.


The reference to nonprofit mailing privileges is very helpful. We suggest adding a cross-reference to the web site or publication where the applicant can obtain instructions for applying for those privileges.

3. “Inurement to Insiders” and “Excess Benefit Transactions.”

We see two significant technical issues with the presentation: 1) the Overview does not distinguish between the rules applicable to public charities and those applicable to private foundations; and 2) the Overview does not distinguish between the concepts of an “insider” under Section 501(c)(3) and a “disqualified person” under Section 4958.

The language under the heading, “Jeopardizing Tax-Exempt Status,” states: “All charitable organizations must abide by certain rules.” The next two sections go on to describe inurement to insiders and excess benefit transactions. The presentation leaves the clear impression that those two sets of rules apply to all charitable organizations, when in fact the excess benefit transaction rules under Section 4958 apply only to Section 501(c)(3) public charities and have no application to Section 501(c)(3) private foundations.

We suggest that a better way to organize the topics is to present first those rules that apply to all charitable organizations, and then to call out the special rules that apply only to public charities (e.g., Section 4958), and those that apply only to private foundations. In particular the discussion of the rules concerning lobbying, while technically applicable to all charitable organizations, should include a statement that additional restrictions apply to private foundations, and should refer the applicant to the section on special rules for private foundations.

Indeed, the Overview says almost nothing at all about the special rules for private foundations. This is a conspicuous omission, given the substantial increase in the use of private foundations in recent years. While most applications prepared without legal or accounting assistance are likely to be from public charities, the consequences of private foundation non-compliance are so severe that we believe it is worth the effort to include some very basic information about private foundation rules with a cross-reference to the appropriate IRS publication.

We further suggest adding text along the following lines: “For more information on the excess benefit transaction rules governing public charities, see… For more information on the self-dealing rules that govern insider transactions with private foundations, see…” with cross-references to IRS publications.

b. Distinction between Inurement and Excess Benefit.

The Overview’s descriptions of private inurement to insiders under Section 501(c)(3) and excess benefit transactions under Section 4958 both use the term “insider” to identify the persons to whom those rules apply. This of course is not the terminology used in the law.

The term “insider” does not appear in the Internal Revenue Code or regulations. It is customarily used as a shorthand for “private shareholder or individual,” under Section 501(c)(3), and “persons having a personal and private interest in the activities of the organization,” under Treasury Regulation § 1.501(a)-1(c). We have no objections to its use in this context.

The applicable term in the Section 4958 context, however, is “disqualified person.” Section 4958(a); Treas. Reg. § 53.4958-3. A fundamental question regarding the relationship between the Section 501(c)(3) private inurement rules and the Section 4958 intermediate sanctions rules is whether the definition of an insider is co-extensive with the more precisely articulated definition of a disqualified person. The manner in which the Overview equates the two, while it simplifies the presentation, is, at this early stage in the development of the law concerning Section 4958, both technically inaccurate and misleading.
We suggest that the best approach, as noted above, is to create a separate section describing the special rules for public charities (e.g., Section 4958), in which the terminology “disqualified person” should be used. That term should be distinguished from the “disqualified person” terminology that should be used in the suggested section on special rules for private foundations. Specifically, the Instructions could state:

The law applies different rules to transactions with “disqualified persons” depending on whether the organization is a private foundation or a public charity. The term “disqualified persons” generally includes all so-called insiders; however, you should note that the identity of your disqualified persons may differ somewhat depending on whether you are a private foundation or a public charity.

c. “Excess Benefit Transactions.”

The first sentence under “Excess Benefit Transactions” is somewhat confusing as a technical matter. There is no tax on the organization, so it is somewhat odd to say that the organization has engaged in an excess benefit transaction. We suggest that the language after the comma in the first sentence be deleted, and that the first and second sentences read as follows:

Where a Section 501(c)(3) organization provides an excess economic benefit to an insider, the IRS may impose an excise tax on any disqualified person who improperly benefits from such “excess benefit transaction.” Tax may be imposed as well on organization managers who participate in the transaction knowing that it is improper.

4. “Private Benefit.”


We recommend replacing the first two sentences with the following language, which paraphrases Treasury Regulation § 1.501(c)(3)-1(c)(1):

An organization’s activities must be directed primarily to accomplishing charitable, educational, religious or other exempt purposes.

We believe the suggested language is both technically more accurate and less confusing to the reader.

We also suggest adding something along the following lines:

An organization formed to aid a specific named individual (e.g., an accident victim) or an identified group of individuals (e.g., a particular family that has suffered hardship) is treated as serving private interests, and will not qualify under Section 501(c)(3).
b. **Substantiability.**

We suggest revising the second bullet point to read as follows:

Private benefit will not jeopardize exempt status unless it is substantial in relation to the public benefit provided.


c. **Compensation.**

The discussion of inurement makes clear that it does not include reasonable payments for services rendered, etc. A similar disclaimer should be added to the discussion of private benefit.

5. **“Substantial Lobbying.”**

We recognize that this section is of necessity an incomplete description of the issues involved in a Section 501(c)(3) organization’s lobbying activities. Nevertheless, we believe it should be revised in order not to be misleading.

a. **Private Foundation Issues.**

First, the description as written applies only to public charities. It does not address the rules applicable to private foundations. As suggested above, there should be a separate section that describes the rules for private foundations. The “Substantial Lobbying” section should note that special rules apply to private foundations, and should refer the reader to that separate section.

b. **Exceptions and Section 501(h).**

As the section applies to public charities, it is significantly incomplete. At a minimum, it should specify that there is a variety of exceptions to the rules concerning lobbying and should refer the applicant to Publication 557 for more information. It should also give a very basic explanation of the election under Section 501(h). Ideally the Form 5768 would be incorporated into the Form 1023, or at a minimum included with the Form 1023 package.

6. **“Political Campaign Intervention.”**

Overall, this is a very helpful section that is accurate for both public charities and private foundations.

The parenthetical in the second sentence should read “*oral* or written,” rather than “verbal or written.”

7. **“Public Charity versus Private Foundation.”**

The distinction between public charity and private foundation is without doubt one of the most confusing concepts for applicants. We recognize that the highly technical nature of the
subject matter makes communicating the essential concepts accurately in plain language a great challenge.

a. Use of “Public Charity.”

We support the use of the term “public charity” to describe a non-private foundation. While the term does not appear in the Code or the Treasury Regulations, it is commonly understood and much less confusing for applicants than “non-private foundation.”

b. First Paragraph.

We recommend revising the first paragraph as follows:

Every organization that qualifies for exemption under section 501(c)(3) is also classified as either a “public charity” or a “private foundation.” This classification is important because different tax rules apply to these two types of section 501(c)(3) organizations. The two classifications have different reporting requirements, different rules regarding lobbying activities, different rules regarding grantmaking procedures, and many other significant differences. The rules regarding the deductibility of charitable contributions are also substantially different. While donations to both public charities and private foundations are deductible as charitable contributions, the rules for donations to public charities are more favorable and often result in a larger deduction than for a donation to a private foundation.

c. Public Support Test.

(i) Ten Percent/Facts and Circumstances.

The second bullet should state that there are three public support tests, rather than two, and should describe the “ten percent/facts and circumstances” test of Treasury Regulation § 1.170-9(e)(3). This test is the basis under which many organizations (particularly small and/or new organizations) qualify as public charities, and it should be included here. (We note that the “facts and circumstances” test is referred to for the first time without any background in the Note carrying over from page 16 to 17 of the Instructions. For the reference to be meaningful the test should be described in the Overview.)

(ii) Section 509(a)(2).

The description of the Section 509(a)(2) test is technically inaccurate. It states: “In this test, an organization must receive at least one-third of its total support from gifts, grants, …” To reflect accurately the statutory requirement, it should state, “In the second test, an organization must receive more than one-third of its total support from gifts, grants, …” Section 509(a)(2)(A).
(iii) **Suggested Language.**

We recommend revising the second bullet point to read as follows:

Organizations that receive funds from many sources and/or the government—There are three different “support tests.”

(1) Under the first test, an organization must generally receive at least one-third of its total support from governmental agencies, contributions from the general public, and contributions or grants from other public charities. The amount of contributions from a single donor or other funding source, other than a governmental agency or public charity, that may be included in the calculation is limited.

(2) Under the second test, an organization must generally receive at least ten percent of its total support from the sources noted above. In addition, the organization must show, on the basis of certain factors, that it is organized and operated in a manner designed to attract public and governmental support on a continuing basis. *See* Publication 557 for a more detailed description of this test.

(3) Under the third test, an organization must generally receive more than one-third of its total support from gifts, grants, contributions, membership fees and from gross receipts from activities that accomplish its exempt purposes (e.g., revenues from the sale of goods and/or services) or that are not an unrelated trade or business. In addition, the organization’s investment income and net unrelated business taxable income may not generally exceed one-third of its total support. The amount of gross receipts from a single payor that may be included in the calculation is limited.

(iv) **“Calculations.”**

The final paragraph in column two states:

> These are very detailed tests with specific rules that differ for each test. Review the specific instructions when making the calculations.

It is unclear to what “calculations” this refers. The Form 1023 does not include line items for the applicant to make calculations of public support, in the manner that the Form 990, Schedule A, Part IV “Support Schedule” does.
(v) **Advance Ruling Period.**

The section should include a brief overview of the five-year advance ruling period for new organizations under the public support tests.

d. **Supporting Organizations.**

(i) **Identify by Name.**

The third bullet point should include the term “supporting organizations” in its caption. This will help the applicant relate the description in the Overview to Schedule D of the Form. It would be helpful to have additional captions identifying the three public support tests.

(ii) **Multiple Supported Organizations.**

The section should clarify that a supporting organization may support more than one public charity. The current text refers to “another public charity” and is inadvertently misleading. The Treasury Regulations allow a supporting organization to support multiple public charities identified in the governing documents either by name or (for Type 1 supporting organizations) by class. Treasury Regulation § 1.509(a)-4(d)(2).

(iii) **Non-Section 501(c)(3) Supported Organization.**

This section should clarify that a supporting organization may support the charitable activities of certain other categories of non-charitable Section 501(c) organizations if they are publicly supported.

e. **“Foundation” in Name.**

The final paragraph of this section, which informs the applicant that the classification as a “private foundation” has nothing to do with the organization’s name, is a welcome plain language addition.

8. **“Private Operating Foundations.”**

Rather than stating that a private operating foundation is a “blend of a public charity and a private foundation,” we suggest that this section state:

A private operating foundation is generally subject to the special rules and requirements for private foundations, other than the 5% annual distribution requirement. Private operating foundations are subject to more favorable rules than other private foundations, however, with respect to the charitable contribution deductions available to donors and the ability to attract grant funding from private foundations.

This suggested language explains to the applicant why private operating foundation status may be desirable.
C. General Instructions.

1. General Comments.

a. Commendations.

The draft Instructions represent a considerable improvement over the current Instructions and are obviously the result of a good deal of work and careful thought. In particular, we commend the following:

- Information concerning the advisability of providing a certified check or money order;
- Instructions regarding including the name and EIN on all attachments;
- List indicating the order in which documents should be submitted;
- The clear statement that applications filed within 27 months after the end of the month of formation will, if approved without material amendment, result in retroactive exemption to the date of formation;
- The clear statement that substantiation for contributions may be provided electronically;
- The reference to state regulation of charitable solicitations;
- Helpful “Notes” to applicants to alert them to consistency issues regarding their responses.

b. Suggestions.

(i) Incorporating Additional Forms.

In addition, we suggest that the following would also be highly desirable:

- Include Form 2848 in the Form 1023 packet;
- Include Form 5768 in the Form 1023 packet;
- Include Form SS-4 in the Form 1023 packet.

(ii) Moving Sections to “Overview.”

Many of the sections in the General Instructions have little to do with completing the Form, e.g., “Public Inspection,” “Contributions – Substantiation and Disclosure Rules,” Solicitation of Funds,” and “Unrelated Business Income Tax (“UBIT”).” These sections would more appropriately be included in the Overview.
2. **“Obtaining Tax-Exempt Status.”**

   a. **Financial Data.**

   The Instructions provide:

   One of the key pieces of information requested is financial data. This data, whether budgeted or actual, should be consistent with other information presented in the application. For example, … Budgeted financial data should be prepared based upon your current plans. We recognize that the organization’s actual financial results may vary from the budget.

   The impetus for including this explanation, we assume, is to emphasize that in the review process the IRS will be vetting whether the plan of operations is in line with charitable purposes. We believe it is valuable to emphasize that operational plans should be consistent with financial resources, and that charitable organizations and their fiduciaries must utilize those resources appropriately. We suggest that the Instructions should indicate that it is advisable to have an appropriate business plan in place prior to preparing the exemption application. Where such a plan is in place, applicants are better able to complete the Form’s questions and provide narrative and financial information.

   b. **Public Support.**

   The Instructions at paragraph 3 incorrectly state that applicants requesting public charity status under the so-called “support tests” should present “financial data [to] show contributions or receipts from providing exempt services [being paid by] multiple donors or payers.” The revenue presentation format used in the Form requires aggregation of donations and program fees, and this sentence is therefore misleading. The statement is also incorrect as a technical matter, because an organization may satisfy a public support test when all its support is from a single publicly supported charitable donor.

3. **“Assembly of Application Package.”**

   The Instructions on how to assemble the application package will be very helpful to applicants as well as to IRS staff. We have a few suggestions and questions.

   a. **User Fee.**

   The Instructions may be a bit confusing. The first “document” for the package is the “User fee check attached.” The next document is the Form 2848, Power of Attorney and Declaration of Representation. The third document is the Form 1023. Isn’t the user fee supposed to be attached to the Form 1023? If yes, perhaps the “User Fee Attached” should be moved to be the second document in the package order or it should be clarified that the user fee is attached to the Form 1023. It may be helpful to design a specific place on the form where it should be attached.
b. Chronology.

The references to “organizing document” and “amendments…in chronological order” are confusing for charities organized as nonprofit corporations, since many organizations amend and restate the entire Articles of Incorporation rather than just filing an amendment of a particular paragraph or section. We suggest asking for the original organizing document and, if amended, copies of all amendments in chronological order.

c. Form 5768.

It may be helpful to add Form 5768, Election/Revocation of Election by an Eligible Section 501(c)(3) Organization to Make Expenditures to Influence Legislation, to the list as an optional document (unless it can be incorporated into the Form 1023), perhaps placed before the miscellaneous correspondence.

d. Miscellaneous Correspondence.

The term “miscellaneous correspondence” is unclear. We suggest adding examples of what you have in mind.

4. “After you submit Form 1023.”

The explanation of what happens “after you submit Form 1023” would be even more helpful if the Instructions added that the “letter stating that you are exempt under section 501(c)(3) will also indicate whether you are a public charity or a private foundation.”

5. “Reporting Unrelated Business.”

Perhaps the heading should be “Reporting Unrelated Business Income.”

We question whether it is necessary to include this section. This information is better provided to the applicant once it has obtained a determination letter and is not necessary for purposes of completing the application.

In particular, the second bullet point, regarding treatment of a limited liability company as a disregarded entity, seems unnecessary and confusing, and of only limited relevance to most applicants. We recommend its deletion.

6. “Canadian Organizations.”

The information provided regarding Canadian organizations is technically inaccurate and contrary to IRS Notice 99-47, 1999-36 IRB 391 (September 7, 1999). That Notice states that, pursuant to Article XXI of the Income Tax Treaty between the U.S. and Canada, and pursuant to a mutual agreement entered into by the U.S. and Canadian competent authorities, “Recognized religious, scientific, literary, educational, or charitable organizations that are organized under the laws of either the U.S. or Canada will automatically receive recognition of exemption without application in the other country (emphasis added).”
Pursuant to the Notice, a Canadian registered charity (i.e., a Canadian organization that has received a determination of registered charity status from the Canada Customs and Revenue Agency, formerly known as Revenue Canada), is automatically treated as a Section 501(c)(3) organization, and is not required to file Form 1023.

IRS Notice 99-47 further provides that all Canadian registered charities are presumed to be private foundations, unless the registered charity submits financial information to the IRS to enable the IRS to determine that the organization is a public charity.

Accordingly, the information regarding Canadian charities should make it clear that Canadian registered charities are not required to file Form 1023 in order to be recognized under Section 501(c)(3), but may use certain portions of the Form to apply for recognition of public charity status, and in order to be listed in IRS Publication 78.

We recommend that this section be rewritten to provide as follows:

Canadian organizations that have received a Notification of Registration from the Canada Customs and Revenue Agency (formerly Revenue Canada), and whose registrations have not been revoked (referred to as “Canadian registered charities”), are automatically recognized as Section 501(c)(3) organizations and are not required to file Form 1023. Canadian registered charities are also presumed to be private foundations. A Canadian registered charity may complete certain portions of the Form 1023 in order to be listed as a Section 501(c)(3) organization in IRS Publication 78, Cumulative List of Organizations, or to request classification as a public charity, rather than a private foundation. A Canadian registered charity should complete only the following:

D. Specific Instructions.

1. Part I, Item 1. Full Name of Organization.

The Instructions require additional information that is not apparent from the Form. Applicants are directed to provide a “common” or “dba” name. The 2001 Form 990 instructions similarly allow an organization to provide a second name, which will allow data searches for such names. We are pleased to see this feature included in the Form 1023. We believe that applicants are likely to miss this instruction, however, and it should be noted on the Form itself.

Some organizations in fact have a parenthetical in their legal name (e.g., A Better Charity (ABC)). Accordingly, as noted below, we suggest that line 1 have a separate entry for the organization’s legal name (e.g., upon line 1a or upon a divided box entry as occurs at lines 3 and 4), and that an additional entry be provided for any other operating name.

The “Location Address” is defined as the address where books and records are kept. The operating location may be different from the location of books and records. Which address is the IRS seeking?

It might be helpful to applicants if the Instructions at this point noted that if the organization has one street address location, the public will be able to access documents that are subject to public inspection at such location.


a.  EIN Pending.

While the Instructions appropriately tell the applicant not to apply for an EIN more than once, they do not address the situation where an applicant has filed an SS-4 but has not yet received an EIN. It would be helpful to have a box that indicates “EIN pending.”

b.  Form SS-4.

It would be very helpful to include a Form SS-4 in the Form 1023 packet or to integrate the Form SS-4 into the Form 1023, if feasible.


We recommend revising the “Note” to tell the reader to “make sure” (rather than just “check … for consistency”) that the bylaws are consistent with the annual accounting period stated in item 6. The draft language is courteous but we suggest that the IRS would have less trouble with inconsistent dates if the Instructions forthrightly tell people to make sure the dates are the same in both places.

5.  Part I, Item 7. Primary Contact Person.

The Instructions imply that it is only a “primary contact person” who might need a power of attorney. For clarity’s sake, it should be noted here that any party who is authorized to speak with the IRS about the application, if not an officer, director, or trustee, will need a power of attorney.


The Note should affirmatively instruct applicants to make sure the web site information is consistent with the Form 1023 information, rather than suggesting gently that they check for consistency.
7. Part II. User Fee Information.

a. Attaching the Check.

We strongly support the incorporation of the IRS Form 8718 directly into the Form 1023. The Instructions do not indicate where the fee should be attached, however. The form should be designed with a specific location for attaching the check.

b. Average Gross Receipts.

The Instructions should indicate how the applicant is to determine average annual gross receipts for eligibility for the $150 user fee.

8. Part III. Information about Your Officers, Directors, Trustees, and Their Transactions and Agreements with You.

a. Order of Parts.

Overall, we believe that it is appropriate for Form 1023 to address issues of private inurement, private benefit and self-dealing, and that the questions reflected in the draft elicit the relevant information. The placement of this section within the application is somewhat illogical, however. We recommend moving Parts III and IV to follow current Parts V, Organizational Structure, Part VI, Information about the Required Provisions in Your Organizing Document, and Part VII, Information about Your History. The analysis concerning an organization’s satisfaction of the organizational test logically comes before an analysis of private inurement and related issues.

b. Item 1. Address.

The Instructions should clarify that the IRS is seeking the individual’s preferred address, and should note the public nature of the information. A suggestion that the applicant avoid providing unnecessary personal information (e.g., social security numbers, cell phone numbers, etc.) might also be helpful.

c. Item 2. Relationships.

We suggest that the Instructions include examples of “business relationships” to help the applicant understand this term. Examples might include employment, contractual relationships, and common ownership of a business.

The Instructions should also note that when there are relationships, the IRS may request additional information on how the organization addresses conflicts of interest.


The Instructions for Item 3 explain compensation clearly, but the second paragraph should be revised to be consistent with Form 990 so that applicants must disclose the salary,
benefits, expense allowances, etc. for their officers, directors, and trustees. The Instructions should specify that “compensation” includes non-cash compensation.

The suggestion to include “a brief resumé for each compensated individual” incongruously follows an instruction to submit a “breakdown of compensation.” Does the Service want information on the person’s qualifications, a job description, a brief summary of the compensation/benefits package, or all three? If the purpose of the resumé is to assist in establishing whether compensation to a particular individual is reasonable, this should be explained.

e. Item 5. Substantial Influence.

The question concerning whether officers, directors, or trustees have “substantial influence” over other organizations is confusing. The standard of “substantial influence” appears in the Section 4958 intermediate sanctions rules, but in that context the term deals with the level of a person’s influence over the covered organization (i.e., a Section 501(c)(3) or (c)(4) organization), and not with any other entity. “Substantial influence” is defined in the Instructions as “the ability to affect decisions, such as by being a director or officer, major shareholder or owner of an exempt or for-profit entity.” If the point of the question is to address situations in which an applicant organization may be engaging in transactions with a legal entity that an insider with respect to the applicant controls or otherwise influences, we urge the IRS to use a term other than “substantial influence,” to avoid confusion with the context in which this term is used in Section 4958(f). For purposes of that Section, the term “substantial influence” has a detailed definition at Treasury Regulation § 53.4958-3(c) that does not apply in the context described here.

f. Items 4 and 5. Conflicts of Interest.

The Instructions to both Items 4 and 5 ask for “explanations” as to how “conflict of interest was resolved to reach an unbiased decision.” Conflicts of interest are not really “resolved.” Perhaps the instruction should instead ask for an explanation of what steps the organization has taken to ensure that fiduciaries have the necessary information and take appropriate action when a conflict of interest exists.

9. Part IV. Information About Your Members.

The scope of the term “member” should be clarified. Is it intended to include corporate as well as individual members? Is it intended to encompass only “members” who have voting rights or another role in governance, or also to extend to “members,” e.g., of a museum, who have rights only to defined goods and services?


a. Item 1. Trust.

The Instructions helpfully provide that for trusts created under wills, the applicant should include a copy of the death certificate or statement indicating the date of death. In our experience, the IRS has historically also required that, for applicants organized as trusts, the
applicant must provide an indication that the trust in fact has a corpus, e.g., a bank or brokerage account statement of the trust. Presumably this is because state law generally provides that in order for a trust to exist, it must have a trustee, beneficiaries, and trust corpus. Typically the date on which the trust first has corpus is the trust’s organizing date. If it is IRS policy to require such documentation, then it should be stated in the Instructions.

b. **Item 3. Corporation.**

The third paragraph, concerning limited liability companies, is likely to be very confusing to applicants. We suggest deleting it and replacing it with the following:

In general, a limited liability company (LLC) is treated as a partnership for federal tax purposes. Partnerships are not eligible for exemption under section 501(c)(3). An LLC seeking separate tax exemption may nevertheless file its own exemption application. In this case, it will be treated as a corporation, rather than a partnership. An LLC in which a section 501(c)(3) organization is the sole member is treated as a division of its section 501(c)(3) member, rather than as a separate legal entity, and is not required to apply for its own federal tax exemption.

An LLC does not have Articles of Incorporation. Instead, its organizing document is its state-approved “Articles of Organization.” If it has adopted an “operating agreement,” then this document is also part of its organizing documents.

c. **Amendments.**

Part V, items 1-3 request that “any amendments” be attached along with the creating/initial organizing document. Thereafter, potential deficiencies in those documents are the subject of Part VI. Users are directed, if making a “Yes” answer in Part VI, to ensure that correction occurs through the adoption of relevant amendments. Since the submission of all amendments is already required pursuant to the preceding Part V, this Part creates a circular handling of these items. We suggest that Part VI be reworded or reconfigured.

11. **Part VI. Information About the Required Provisions in Your Organizing Document.**

a. **Typo.**

There is a typo in the eighth line, first paragraph. The “the” should be omitted.

b. **Model Language.**

We support the detailed explanation of two key elements of the organizational test: (1) limiting the purposes of the organization to one or more exempt purposes; and (2) dedication of assets to an exempt purpose.
12. Part VII. Information About Your History.

a. Definition of “Successor.”

(i) Overlapping Boards.

The definition of “successor” needs refinement. An organization may have the same officers, directors, or trustees as another organization (either one that exists or one that no longer exists), without being a “successor,” if the purposes and activities of the new enterprise are distinct from those of the other organization. At the same time, an organization that does not have the same board members and officers as another organization, but which has a majority of overlapping board members and officers and has identical or similar purposes to the other organization may indeed be a successor.

(ii) “Taken Over.”

The language “taken over” is quite vague. It would be helpful to be more precise about the types of transactions covered. For example, the definition as currently stated would include a public charity that receives a liquidating distribution of investment assets from an unrelated terminating private foundation for use in the public charity’s programs. We do not believe that this is what the IRS intends to cover. Moreover, successor status should arise only when an organization carries on as a substantial portion of its activities programs previously conducted by another organization. We suggest the following to replace the first two paragraphs under this heading:

You are a successor organization if you operate as a substantial part of your activities a program that was previously carried on by another organization. You are also a successor organization if a majority of your officers, directors, or trustees are also officers, directors, or trustees of another organization with similar or identical purposes. In addition, you are a successor organization if you are the corporate successor to another organization, such as an unincorporated association or a charitable trust that previously carried on your activities or a for-profit corporation that has converted to a nonprofit form.

b. Item 2.

The third bullet point should be revised to read: “Explain how the other organization’s assets were acquired.”
c. **Item 3.**

The Instructions to this question state that if the applicant is a successor to an organization that previously filed a Form 1023, 1024 or 1028, then the applicant must explain how the application was resolved and include a copy of any denial letter. They do not address the situation where an organization *did* obtain an exemption letter (e.g., a Section 501(c)(3) charitable trust that is converting to corporate form). Should a copy of that exemption letter be included? It might be helpful for the Instructions to so specify.

13. **Part VIII. Information About Your Specific Activities.**

a. **Item 1. Political Candidates.**

The “Note” after Item 1 describes the prohibition against supporting or opposing candidates for public office, and then states, “If you answer ‘Yes’, you should reconsider whether the filing of application Form 1023 is appropriate for your organization.” In our view, the statement is too diplomatic, and should state more forcefully:

> If you plan to support or oppose candidates for public office in any political campaign, then you will not qualify under section 501(c)(3) and should consider whether another category of federal exemption may apply to your organization. Refer to Publication 557 for a description of other sections under which you may qualify, for which Form 1024 is the appropriate application.

b. **Item 2b. Section 501(h) Election.**

(i) **Form 5768.**

We are pleased to see that organizations will be able to submit Form 5768 along with Form 1023. Toward that end, we strongly suggest either providing a box to check on Form 1023 to make the election, or including Form 5768 in the booklet for the convenience of organizations trying to put their own applications together.

The Instructions should indicate that the form will be returned to the applicant (or the election will not be effective) if the Service determines that the organization is not an eligible organization as part of the determination letter process.

(ii) **Section 501(h) Election.**

The discussion of the Section 501(h) election does not provide applicants with sufficient background or context for making a decision concerning the election, however. The description, combined with the title of Form 5768, Election/Revocation of Election by an Eligible Section 501(c)(3) Organization to Make Expenditures to Influence Legislation, creates the false impression that an organization must make the election *in order to make expenditures* to influence legislation.

We recommend stating:
If you are eligible to make the election under section 501(h) and you complete and file Form 5768, your expenditures to influence legislation will be subject to a mathematical test that looks only to the percentage of your expenditures used for such activities, as opposed to the time involved or other factors. For more information to help you determine whether to make the election, see Publication 557. If you do not make your election at this time you may make it at any later time and it will be effective as of the beginning of the year in which you make it.

c. Item 3a. Fundraising.

The Instructions focus on potentially abusive areas. It would be helpful to include other examples such as direct mailings, personal solicitations and telephone solicitations. Not all fundraising involves an event. Also, it may be helpful to give multiple examples of “directly” (e.g., by employees, by members for an organization with individual members, or by board members).

d. Item 3b. Fundraising.

The Instructions indicate that an organization “should also include the percentage of your total time spent on fundraising compared to your total activities.” As an initial matter, applicants are generally new organizations that are quite unlikely to have any data on this point. More importantly, many organizations (e.g., community foundations) have as their sole purpose raising funds for distribution to other charitable organizations. For these organizations, nearly all of their time, with the exception of grantmaking and investment decisions, will be spent on fundraising. The Instructions inaccurately imply that a substantial percentage of activities devoted to fundraising may pose a bar to exemption. We recommend deleting the sentence quoted above.

e. Percentages of Time.

The Instructions in several places (including Items 2a, 3b, 4, 5, 6, and 15) ask organizations for information concerning “the percentage of your total time spent on” fundraising, unrelated business activities, etc. From a practical standpoint, most applicants are new organizations and will be completely unable to provide accurate estimates of this information. Moreover, we have concerns regarding the underlying legal basis for the question. The question presumably is aimed at determining the substantiality of various activities that the Service might consider would jeopardize an organization’s qualification for exemption. In many cases, however, the “time” spent on an activity is only one factor to be taken into account. For example, in the unrelated business income area, so long as an organization spends an amount on exempt activities that is commensurate in scope with its resources, the amount of time the organization devotes to activities that produce unrelated business income should not affect its qualification for exemption. Revenue Ruling 64-182, 1964-1 C.B. 186.
We also note that even substantial business activities conducted with a fundraising purpose do not disqualify an organization from exemption. See Treas. Reg. § 1.501(c)(3)-1(e), which states:

an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities if the operation of such trade or business is in furtherance of the organization’s exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513.

In the determination letter process, we suspect it is a rare case in which it is possible to say with certainty that lobbying, fundraising costs, and unrelated business activities are so substantial to preclude recognition of exemption. Given the difficulties of measurement, we suggest that all of the Instructions requiring a detailed estimate of the “time” the organization spends on a particular activity should be omitted and left to follow-up by determination specialists in the few cases where sufficient operations have occurred to make this a fruitful inquiry.

f. Item 4. Other Gaming.

The Instructions should provide a brief discussion of the consequences of engaging in other gaming activities, and should refer the applicant to Publication 3079, Gaming Publication for Tax-Exempt Organizations.

g. Item 5. UBIT.

The example concerning the unrelated business income tax is technically inaccurate. It states: “For example, the sale of advertising in your annual year book is generally an unrelated business activity.”

That is not the case. The sale of advertising in an annual year book by students is generally not an unrelated business activity, pursuant to Treasury Regulation § 1.513-1(d)(4)(iv) Example 5 (solicitation and sale of advertising in campus newspaper by students under the supervision and instruction of the university is not an unrelated trade or business).

h. Item 7. Economic Development.

The Instructions should include information on what factors are likely to cause economic development activities to qualify for Section 501(c)(3) status.

i. Item 13. Scholarships.

We suggest revising the Instructions as follows: “Answer ‘No’ if you are providing funds only to another organization for its financial aid program and you have no role in selecting the individual recipients.”
j. **Item 11. Tax-Exempt Bonds.**

Bond offering documents rarely if ever exist at the time the borrower files Form 1023. The Instructions should request the offering documents for the bonds only if the bonds have been issued.

k. **Item 14. Intellectual Property.**

We assume that the question is intended to elicit information concerning ownership rights that private individuals may have in intellectual property used by the applicant that might result in private inurement or excess private benefit. If that is the intention, in our view the question is both confusing and too broad. Applicants in general will not have background in intellectual property rights or access to information concerning what is and is not permissible in this area. Indeed, we note that there has not been any definitive guidance issued in this area, and we are concerned that IRS reviewers will have no meaningful standards for evaluating the information elicited.

The question in addition asks an applicant whether it charges for any use of intellectual property, and asks the applicant to distinguish any such activity from “commercial operations.” We suggest that this inquiry be separated from the question concerning ownership, because it addresses a different issue from that of private inurement or excess private benefit, i.e., the “commercial hue” of an organization’s operations.

In our experience applicants tend to be very confused by both of these inquiries when they are made in follow-up correspondence under the current determination process. We believe that it is unlikely that applicant responses will be meaningful unless the Instructions provide guidance on the types of intellectual property rights that the question is intended to cover, such as patents, copyrights, etc., and the factors that may distinguish an applicant’s activities from commercial operations. In addition, the Instructions should state how the information provided by the applicant will be evaluated.

We suggest as an alternative the following:

Do you have, or do you expect to create or acquire, ownership rights in written or recorded materials (books, publications, audio or videotapes, or electronic media of any kind), patents (for example, scientific discoveries), copyrights, or other intellectual property assets? If “Yes,” attach a description and answer (a) and (b) below.

(a) Do you, or will you, own these written or recorded materials, patents, copyrights, or other intellectual property assets? If “Yes,” state the percentage of your ownership and identify any co-owners that are members of your governing body, officers, employees, substantial contributors, or members of their families.
(b) Do you, or will you, pay another person or organization for the right to use the intellectual property? If “Yes,” indicate how much you pay and how the amount of the payment is determined.

1. **Item 15. Services to Other Exempt Organizations.**

   (i) **Related Organizations.**

   The “Note” should make clear that a Section 501(c)(3) organization may provide ordinary business services to other Section 501(c)(3) organizations under common control without any adverse impact on its qualification for exemption.

   (ii) “Consulting.”

   We recommend deleting the word “consulting” because it may be interpreted to describe educational activities that further an exempt purpose.

2. **Item 16. Internet Activities.**

   Item 16 would be clearer if the Instructions specifically excluded from the definition of web site activities an organization’s use of email for ordinary communications in addition to simple maintenance of its web site.

3. **Item 18. Foreign Organization.**

   The Instructions refer to organizations formed “under the jurisdiction of the United States,” etc. This will not be clear to smaller organizations. We suggest replacing “jurisdiction” with “laws” so that the phrase reads “under the laws of....”

4. **Item 18a.**

   The Instructions should specify that a foreign organization may qualify under Section 501(c)(3), to avoid any confusion. Revenue Ruling 66-177, 1966-1 C.B. 132.

5. **Item 19. Contributions to Foreign Organizations.**

   The Instructions state that if an organization contributes to a foreign organization, it must “explain how you maintain control and discretion over the use of the funds or materials you donate.” The question addresses issues considered in Revenue Ruling 75-65, 1975-1 C.B. 79. In that ruling, the domestic charity maintained control and responsibility over the use of any funds granted to a foreign organization by making an investigation of the purpose to which the funds would be put, by then entering into a written agreement with the recipient, and finally by making field investigations to see that the money was spent in accordance with the agreement. The Instructions should inform the applicant that this would be an appropriate procedure (and an appropriate response to the question).

   This question will encompass “friends of” organizations, i.e., domestic charities that have some relationship with one or more foreign charities. Such organizations solicit funds in the
U.S., and make periodic distributions to foreign charities. These arrangements often raise the legal issue of whether donors “earmark” funds for distribution to particular foreign charities, and utilize the “friends of” organization as a conduit or mere agent. In these situations, the pertinent question is how the organization maintains control and discretion over the funds donated to it in a manner that prevents it from being a conduit. It would be helpful to have some discussion and education concerning this issue in the Instructions. See Revenue Ruling 66-79, 1966-1 C.B. 48; Revenue Ruling 63-252, 1963-2 C.B. 101.

q. Item 20.

An applicant may infer from the Instructions as drafted that a Section 501(c)(3) organization may not carry on activities in a foreign country. The Instructions should specifically state that a domestic charity may qualify under Section 501(c)(3), even though it conducts some or all of its activities outside the U.S. Revenue Ruling 68-165, 1968-1 C.B. 253; Revenue Ruling 68-117, 1968-1 C.B. 251; Bilingual Montessori School of Paris, Inc. v. Commissioner, 75 T.C. 480 (1980).

14. Part IX. Narrative Description.

a. Move Narrative Description.

We suggest putting the narrative description before the Yes/No questions of Part VIII for two reasons. First, it allows the organization to tell its story and provide context for the reviewer before the reviewer gets to the potentially difficult questions. Second, it is easier for the applicant to move from the descriptive to the specific questions. We suggest that it is easier for both the applicant to present its “story” (e.g., the overview of its mission and programs) and for the IRS agent to review the application and understand the applicant’s “story” if the narrative description section is moved more toward the beginning of the draft Form 1023 (perhaps to Part III).

b. Web Site.

The Note suggests that an applicant may attach a copy of its web site. Because web sites are frequently updated, we suggest modifying the Instructions to request a printed copy of the web pages as of the date of the application.


a. Current Year Data.

The Instructions in the fourth paragraph should clarify whether current year data may be projected, or must be actual.

b. Preceding Years Data.

The Instructions should clarify that the sixth full paragraph applies only to applicants that have been in existence for four years or more.
c. **Line 1.**

The Instructions incorrectly indicate that fees for exempt function services are included on line 6. The correct line is line 10.

d. **Line 3.**

We suggest revising to read: “Include gross income from assets held for investment purposes, such as dividends, interest, and payments received on securities loans, rents, and royalties.”

e. **Line 10.**

While the question on the form at Part X, Line 10 asks for “gross receipts,” as that term is defined in Section 509(d)(2), the Instructions are broader and quite confusing. They refer to “income from activities that you conduct to raise funds or to further your exempt purposes (emphasis added).” “Fundraising income” is then defined effectively as income from activities that are not unrelated trades or businesses within the meaning of Section 513.

The references to “fundraising activities” and “fundraising income” should be eliminated. Presumably the point of line 10 is to capture all Section 509(d)(2) support. This encompasses both gross receipts from exempt functions, and from any activity that is not an unrelated trade or business. It is not necessary to use the ambiguous “fundraising activity” language in order to describe the revenues at issue. Using the term “fundraising” will likely confuse the applicant, because of the common understanding of “fundraising” in the context of soliciting contributions (line 1 income).

Please note our comments below concerning eliminating the “support schedule” presentation of financial data on Form 1023 and substituting lines 1-12 of Form 990. This would eliminate the confusion and ambiguity created by having to characterize “fundraising income” on the Form 1023.

f. **Lines 16, 17 and 23.**

At lines 16, 17, and 23, the Instructions assume that the applicant knows the names of those whom it will employ or to whom it will make grants, because the Instructions ask for the names of specific individuals who will receive funds. Many organizations will not be able to identify specific individuals by the time they file the application. For example, private foundations seeking approval of individual grant procedures cannot identify scholarship recipients because they cannot select them until the Service has approved their procedures. Other organizations cannot name those whom it may hire in Year 2 if funds allow them to go forward as planned. The Instructions should make clear that the names are required if known to the applicant; otherwise, identifying a recipient by job title or grantee category is acceptable.

g. **Lines 19 and 23.**

The level of detail required concerning employees and independent contractors is unduly burdensome on the applicant and not necessary unless private inurement or substantial private
benefit issues have otherwise surfaced on the application. We recognize that the Instructions reflect the level of detail required under the current Form 1023, but are also aware that IRS determination staff rarely request this level of detail, and suggest its elimination.

h. Line 23.

The Instructions provide: “submit an itemized list showing the name, a brief description of the purposes or condition of payment, and amount paid. Any contracts or agreements for these services should be submitted.” The Instructions specifically encompass fees for professional services from legal counsel.

The Instructions raise a significant concern with respect to attorney/client privilege. As drafted, the Instructions require submitting copies of engagement letters, including the subject matter of the engagement. These matters are subject to attorney/client privilege unless waived by the client. Attaching these documents to a Form 1023 would create a waiver of the privilege, and would also make all such documents subject to public disclosure. At a minimum, the purposes of an engagement and any contracts or agreements with attorneys should not be required. We further suggest that it is sufficient to require copies of only those agreements that directly or indirectly involve disqualified persons.


a. Private Operating Foundations.

The title of this section is inadvertently misleading because the questions refer to private operating foundations as well as public charity status.

b. Box (h). Ten Percent/Facts and Circumstances Test.

The Box (h) Instructions refer to the ten percent/facts and circumstances test for public support and direct the applicant to Publication 557 for more information. This is the only place where that very useful test is mentioned. The references on page 17, columns 2 and 3, to the public support formula in Schedule A of Form 990 are helpful but incomplete, because that formula does not help an applicant to determine whether it can satisfy the facts and circumstances test. As noted above, more information on this test would help smaller organizations learn from the start how to secure public charity status.


The Instructions require an applicant that has received an unusual grant to submit a list including the name of the contributor, the date and amount of the grant, and a description of the grant. In the context of public charities, this information impermissibly discloses the donor taxpayer’s confidential information. While we are pleased to see a mechanism for addressing unusual grant issues in the context of Form 1023, this information should not be made subject to public disclosure. Also, because the unusual grant concept is a common source of confusion, the Form should instruct applicants to review the Instructions for the definition of an unusual grant before completing this section.
IV. COMMENTS ON DRAFT FORM 1023

A. Page 1: Header.

1. Toll Free Number.

We applaud the reference to the IRS EO Customer Services toll free number as a resource for assistance with questions on the Form. We similarly applaud the clarification that the terms “you” and “your” refer to the applicant organization and find that this convention makes the application’s text easier to follow.

2. Definitions.

The directive to refer to the Instructions for a definition of all bold items is of questionable utility, as those who might not carefully read (or remember) this part of the header might miss this convention for referencing a relevant instruction. We encourage page cross-referencing to the Instructions for each Item on the Form.

3. Public Inspection.

The note that the application will be open for public inspection if approved should be highlighted more prominently on the front page of the Form. Additionally, we suggest that a cross-reference be included here to the discussion in the Overview and Instructions regarding public inspection, where a further reminder about privacy concerns could be posted.

B. Part I, Identification of Applicant.

1. Item 1. Operating Name.

As noted earlier, we suggest that Item 1 be bifurcated to allow one line for the applicant’s legal name (i.e., name as shown in organizing document, as the Form currently requests) and another line for an operating name, if any (rather than reporting any such name “in parentheses” as the Instruction requires).

2. Item 3. Mailing Address.

The Item 3 entry for “Mailing Address” should not use a prompt for “number and street,” as many rural route addresses do not comply with such format.

3. Item 4. Location Address.

Item 4 requires a “Location Address” (if different from the Item 3 mailing address). As noted earlier, the Instructions define “location address” as the address where books and records are kept. Because that address may be different from the operating location, the Form should indicate which address is to be entered.
4. **Item 5. EIN.**

Item 5 assumes that the applicant has already procured an “EIN” or is now doing so via an attached SS-4. The Form should direct applicants either to indicate “EIN pending” or to call for assistance if the applicant has filed an SS-4 but has not yet received an EIN.

C. **Part II, User Fee Information.**

1. **Average Gross Receipts.**

The Form should direct the applicant to an instruction that explains how to measure “average annual gross receipts” over a four-year period.

2. **Item 2. Attaching Check.**

   Item 2 should direct the applicant to the place to attach payment either on the Form 1023, or the Form 2848, depending on how the question of document assembly is resolved with respect to the “user fee attached” question noted earlier.

D. **Part III, Information about Your Officers, Directors, Trustees, and Their Transactions and Agreements with You {Suggested Part VI}.**

1. **Order of Parts.**

   As noted earlier, we believe this section quite appropriately asks for information bearing on private inurement, private benefit and self-dealing issues. We have recommended moving the placement of this section, however. Specifically, we suggest that Part III and IV follow Part V – VII. The heading above, and those following, use {brackets} to denote our suggested reordering.

2. **Item 1. Address.**

   As noted earlier, the Instructions for this Item should clarify that the IRS is seeking the individual’s preferred address (home or business), and emphasize that the information provided here will be fully disclosed under the public inspection rules for Form 1023, assuming the application is successful.

3. **Header.**

   We believe that applicants are likely to miss the header explaining that the “Yes” or “No” questions in Items 2-5 relate to past, current, and planned transactions and agreements. Instead, we suggest that the text on each of the Items reflect such reach.

   Item 2 should state: “Are any of your officers, directors, or trustees related to each other, have those serving in the past been related to each other, or is it contemplated that officers, directors or trustees will in the future be related to each other?”
Item 3 should state: “Have you provided any compensation (cash, services, or property) to any of your officers, directors, or trustees in the past, do you do so now, or do you expect to do so in the future?”

Item 4 should state: “Have you entered into any written or unwritten leases, contracts, or other agreements in the past, are you doing so now, or do you contemplate doing so in the future?”

Item 5 should be introduced with the text: “In the past, at the present, or in the future has it been the case that any of your officers, directors, or trustees . . .”

4. **Item 2. “Related.”**

Item 2 should be augmented by an additional sentence explaining that the term “related” includes not only family relationships, but also business relationships such as ownership, employment, etc.

5. **Item 3. “Compensation.”**

Item 3 should use more open-ended terminology with respect to compensation (e.g., “any compensation (cash, services, or property).”

6. **Item 4. Agreements.**

As noted above in our comments on the Instructions, Item 4 should reference “written or unwritten agreements.”

7. **Item 5. Substantial Influence.**

As noted earlier with respect to the Instructions, the use of the term “substantial influence” in Item 5 is imprecise and potentially confusing.

E. **Part IV, Information About Your Members and Other Individuals and Organizations that Receive Benefits from You {Suggested Part VII}.

1. **Items 1-3.**

We suggest you replace the opening clause in Items 1-3, “Are any of your benefits limited to,” with the alternative phrasing: “Do your activities provide direct, or substantial indirect, benefit to”.

2. **Item 2.**

The Instructions and text at Item 2 should provide or refer to a clear definition of “members.” As noted earlier, it is not clear whether the term covers both corporate and individual members, nor whether the applicant should answer only with respect to members who have voting rights or another role in governance, or with respect to those whose rights only grant access to certain goods and services.
3. Items 1 and 3.

Items 1 and 3 are potentially confusing to readers, because they differ by only one word (where the word “individual” appears in Item 1, the word “organization” appears in Item 3). In addition, they appear out-of-sequence and should be placed together.

F. Part V, Organizational Structure {Suggested Part III}.

1. Order of Parts.

Note that our preferred ordering would have this Part immediately follow the User Fee, Part II section of the Form.

2. Item 3.

Item 3 should direct limited liability companies to the Instructions. We have earlier provided a suggested paragraph to explain the unique circumstances these entities face in the application process.

G. Part VI, Information About the Required Provisions in Your Organizing Document {Suggested Part IV}.

1. Order of Parts.

We have earlier noted that current Part V and VI (our suggested reordering would have these as Part III and IV) are inherently circular, with the latter part being a “check” on the former. We suggest that the last sentence of Items 1 and 2 be changed to state: “If “Yes,” STOP and do not proceed with this application until you have amended your organizing document.”

2. Items 1 and 2.

In accord with the preceding suggestion, Items 1 and 2 could include a reminder that the required amendments will need to be provided as attachments to the preceding Part.

H. Part VII, Information About Your History {Suggested Part V}.

1. Header.

The phrase “your history with the IRS” in the header preceding the “Yes” or “No” items is not an accurate description of the entirety of information elicited in this Part. We suggest that the words “with the IRS” be deleted.

2. Revisions.

This section would be easier for the applicant to complete if a flow-chart approach allowed skipping non-applicable questions. We suggest the following:

a. Alter Item 1 to conclude, “If “Yes,” complete Schedule G and skip to Item 3.”
b. Renumber Items 3-5 as 2a, 2b, and 3, respectively.

c. Alter Item 2 to continue beyond its current close: “, and answer Items 2a and 2b as appropriate.”

3. Item 3.

The text at Item 3 (which we suggest be renumbered 2a) should be augmented by a directive to attach a copy of any IRS correspondence denying exemption to the applicant.

I. Part VIII and IX.

We earlier suggested switching the order of Parts VIII and IX in the current draft so that the narrative description of Part IX would be completed prior to the Yes/No questions of Part VIII. We strongly urge this reordering both because it will allow an applicant to tell its story and because it will provide context for the IRS reviewer before the applicant (and the reviewer) gets to the more involved specific questions about activities.

J. Part IX, Narrative Description of Your Activities {Suggested Part VIII}.

1. Header.

The Header to this Part is roughly the same length as the Instructions to this Part (see Form 1023 Instructions at Page 13). We urge that the Instructions for this Part be printed in full in the text of the Form, under an overall introduction that states as follows (new language in italics):

Describe your past, current, and planned activities in a narrative fashion in the space provided below or on an attachment to the application. List the activities in the order of their relative importance to the accomplishment of your exempt purpose, taking into account the amount of funds that have been or are anticipated to be raised or expended for the activity and the time available from volunteers and your officers and directors. {Continue with text from Instructions}.

2. Bullet Points.

We would, however, make two alterations to the bullet points portion of the present Instructions at page 13 prior to incorporating them into the Form. As earlier noted, applicants will rarely be able to answer questions concerning “the percentage of your total time spent on” activities. We thus suggest deleting the Instruction’s bullet point asking what percentage of total time is allocated to each activity. Similarly, as noted earlier, many applicants are new organizations that have not yet attracted funding. The Instruction’s bullet point asking “how is the activity funded?” should also be deleted.
K. Part VIII, Information About Your Specific Activities {Suggested Part IX}.

1. Header.

As noted earlier with respect to the header to Part III, although the header to this Part explains that the “Yes” or “No” questions employed in each item relate to past, current, and planned activities, this directive is likely to be missed or forgotten as an applicant completes the 23 items comprising the Part. Instead, we suggest that the text of each Item be reworked to reflect a comprehensive reach regarding past/present and anticipated activities.

2. Item 1.

Those answering “Yes” to Item 1 should not only be required to attach an explanation, but be directed to the relevant portion of the Instructions.

3. Item 2b.

As we earlier noted, we welcome the opportunity for those desiring to make the Section 501(h) election to do so with the Form 1023. However, the wording of Item 2b is awkward and implies that only those filing Form 5768 may make expenditures to influence lobbying. The text should be reworded to state:

2b -- If you meet the requirements of section 501(h) and file Form 5768 your legislative activities will be evaluated solely by the dollar expenditure limits set by that section. Have you filed Form 5768? If “Yes,” attach a copy of Form 5768 that was already filed with the IRS.

4. Form 5768.

It would be extremely helpful to applicants if they could either check the box in this Item to make their Section 501(h) election, or, if that is not possible, have access in the Form 1023 booklet to a Form 5768 that could be completed and filed by enclosure with the application. We suggest that a separate Item 2c be added to allow one of these mechanisms.

5. Item 3b.

Rather than have Item 3b ask for “net income or losses” from fundraising activities that are conducted by outside contractors, we believe it would be more fruitful to ask for a description of the basis upon which the contractor is compensated.


We appreciate the desire to have an open-ended question on bingo and other gaming activities, particularly if the activities will be conducted by contract with another organization. However, it is unlikely that applicants that conduct such activities under a contract will be able to provide any accurate or useable data on time spent on these activities compared to the organization’s total activities. For those organizations that are directly conducting such
activities, asking for time measures is both burdensome and not relevant, given that an organization may qualify for exemption even when carrying on substantial trade or business fundraising activities as set out at Treasury Regulation § 1.501(c)(3)-1(e)(1).

7. **Item 5.**

The wording of Item 5 implies that “fundraising, . . . bingo or other gaming activities” are per se unrelated activities. We would suggest the question be reworded to: “Do you conduct unrelated business activities?”

8. **Item 8.**

Item 8 is a highly specific question that now has all applicants answering two subparts. We suggest the entire Item be simplified by altering Item 8a so that it concludes with: “If “Yes,” complete Item 8b and attach a description of your program, including how participants qualify. If “No,” skip to Item 9.”

Item 8a is straightforward, but there should be an additional part to the question, which asks whether the applicant satisfies the safe harbor of Revenue Procedure 96-32. If so, the applicant should check the box. In addition, it is unrealistic to ask that the applicant attach a signed management agreement. Such agreements rarely, if ever, exist at the time an applicant is submitting its Form 1023.

Item 8b implies that providing housing through a limited liability company or a partnership carries a negative inference. All housing financed with low-income housing tax credits is conducted through this type of structure and no negative inference should be associated. Moreover, as stated above, final signed operational documents are almost never available when an applicant is submitting its exemption application, and the fact that an applicant does not yet have such documents should not delay processing or cause a denial of the application. Finally, the fact is that these documents are generally voluminous and review of them is administratively burdensome and time-consuming to the IRS.

Members of the ABA Section of Taxation Committee on Exempt Organizations Task Force on Joint Ventures have suggested an alternative approach in their May 2002 submission to the IRS’s TE/GE Division. The Task Force has presented an example of a limited partnership financed with low-income housing tax credits that, the Task Force believes, should be acceptable under Revenue Ruling 98-15. In addition, a coalition of nonprofit housing organizations has proposed amplification of Revenue Procedure 96-32, to include nonprofit organizations that plan to serve as general partners in partnerships and limited liability companies using the low-income housing tax credit. Both of these proposals would offer a safe harbor to nonprofits that plan to serve in partnerships with for-profit investors which, if satisfied, would avoid the need to submit the partnership documents. A safe harbor approach would be preferable to having to submit cumbersome documents when same become available.

9. **Item 16.**

As noted earlier, the language in Item 16 is overbroad and potentially confusing. We suggest the word “consulting” be deleted from the question.
10. Item 18a.

The phrasing of Item 18a is confusing. It should refer not to organizations being formed “in” a foreign country, but to organizations formed “under the laws of” a foreign country.

L. Part X-A, Financial Data (Statement of Revenue and Expenses).

1. General Comments.

a. Revenue Presentation.

The presentation of revenues in lines 1-14 maintains (with one substantive addition) the line items and formatting that the present Form 1023 follows. We strongly recommend revising this section of Form 1023 to follow lines 1-12 of the Form 990, [Annual] Return of Organization Exempt from Income Tax, to provide greater consistency and simplicity for both exempt organizations and IRS reviewers. We believe that it would be extremely helpful to applicants if the Form 1023 provided an introduction to the revenue categories that most exempt organizations will be required to report on Form 990 (i.e., gifts, program service revenue, membership dues, various investment income categories, etc.)

It is not clear what purpose the current Form 1023 format serves. We note that the revenue categories are similar to (although not identical to) the revenue categories on the Form 8734 Support Schedule and on the Support Schedule at Part IV-A of the Form 990 Schedule A. Those schedules are relevant only to public charities that are classified as non-private foundations under the public support rules of Sections 509(a)(1) and 170(b)(1)(A)(vi) or Section 509(a)(2). The public support rules are extremely technical and confusing. It is unnecessary and burdensome to require all applicants to struggle to fit their revenues into categories based on those rules. Many applicants, including all private foundations, schools, hospitals and churches, will never be required to demonstrate public support.

Moreover, we understand that applicants rarely seek a definitive Section 509(a)(1)/170(b)(1)(A)(vi) or Section 509(a)(2) classification ruling. In the limited cases in which an applicant does seek such a ruling, the Form 1023 could require additional information for calculating public support at Part XI.

Because this section of Form 1023 does not mirror either Form 990 or the support schedule format of Form 8734 and Part IV-A of the Form 990 Schedule A in either line items or order of presentation, many new charitable organizations must report their income using three different formats (Form 1023, Form 990, and Form 8734) in a very short period. We believe that this burden could be reduced significantly, without impeding IRS reviewers’ ability to evaluate applications, if the IRS were to adopt the Form 990 categories for Form 1023.

b. Expense Presentation.

We have similar concerns with the expense lines of the Form 1023: they do not track the specific categories that most applicants will be required to use at Part II of the Form 990 (lines 22-44), or the common expense categories that public and stakeholders are accustomed to seeing in annual reports of charitable organizations. In addition, the abbreviation of expenditure...
categories to only seven common ones (grants, compensation/salaries, interest, occupancy, depreciation, professional fees and fundraising expenses) virtually ensures that an applicant must prepare an attachment to detail all other expenses (as line 24 requires).

If Form 1023 tracked the Form 990 categories, on the other hand, many applicants would be able to provide thorough information without attachments. Moreover, the experience of completing Form 1023 would introduce new organizations to the categories they will have to use each year on Form 990. This may increase the likelihood of accurate Form 990 reporting as well as clearer data on Form 1023. Therefore, we suggest that the Form 1023 expense reporting follow Form 990 lines 22-44.

2. Comments on Specific Lines.

   a. Line 2.

   If our prior suggestion to revise Form 1023 to follow Form 990 revenue reporting is not followed, we strongly urge that the line for “membership fees received” be deleted. We understand that this category is used to capture a specific revenue stream that must be isolated for testing public support qualification under Section 509(a)(2), but that for all other purposes is considered gift income. Deletion of this line would thus result in the associated revenues properly being reported on Line 1. We note that the prior version of the Form 8734 (rev. August 1999) had an instruction (see Form 8734 Attachment, STF FED70111) that directed that membership fees be tested for reporting upon either line 1 of this Part (as gifts, if appropriate) or line 10 (if gift characterization is not appropriate because admissions, merchandises, services, or use of facilities are provided to members in exchange for their fees). This methodology should be used in Form 1023 as well.

   b. Line 4.

   If our prior suggestion to revise Form 1023 to follow Form 990 expense reporting on this Part is not followed, the text here should be revised to delete the reference to “businesses you acquired after 6/30/75” to comport with the deletion of that text from the Form 8734 in its latest revision (January 2002). The inclusion of that phrase is confusing, and although technically accurate under the public support test(s) of Section 509(a)(2), is material to only one or two specific exempt organizations.

   c. Lines 16, 17, and 23.

   As noted in the comments to the Instructions, the directives at Lines 16, 17, and 23 requiring the attachment of “an itemized list” assume that an applicant will be able to predict the future regarding those whom it will employ or to whom it will make grants. The directive should instead reference the Instructions, as revised, for details on the information to be provided.

   d. Lines 19 and 23.

   Our comments to the Instructions also noted concerns with respect to confidentiality and the burden created by the directives for attachments to Lines 19 and 23. As with the prior
comment, the directive to Line 19 should not require an “itemized list” but should instead reference the Instructions, as revised, for details on what is to be attached.

M. Part X-B, Financial Data, Balance Sheet.

The header of this sub-Part should be changed to reflect the Instructions’ direction to provide a balance sheet “for your most recently completed tax year.” That directive is a welcome change from the present Form 1023, which requires the date on the balance sheet to be the same as the truncated ‘current tax year’ reported on in the prior sub-Part’s column (a). The header to the dollars column should ask for the end date of the tax year.

N. Part XI, Public Charity Status.

1. Title and Description.

Both the title to this Part and the description before its items should be altered to describe this Part as addressing not just public charity status, but also classification as a private operating foundation. We suggest the title be altered to: “Public Charity or Private Operating Foundation Status.” The description should have an additional sentence that states: “If the organization is a private foundation, this Part is also used to seek classification as a private operating foundation.”

2. Item 5e.

Item 5, line e should include a reference to operating in support of an organization that is qualified under Section 501(c)(4), (5), or (6) and which would be considered a public charity under the public support test referenced below at Part XI, Item 5i. The text should be changed so that a reader does not infer that the supported organization must be qualified under Section 501(c)(3).

3. Item 5h and i.

As we noted earlier in comments to the Instructions, it would be extremely useful if the Form 1023 Overview and Instructions would provide more specific information regarding the three public support tests that are encompassed with Item 5 lines h and i. Each of these two lines should close with a reference to the specific location in the Instructions where such material will be found.

4. Item 5i.

Item 5, line i is technically inaccurate. The language should be revised to read:

509(a)(2) – an organization that receives more than one-third of its financial support from membership fees or gross receipts from admissions, sales, or performance of services that are either related to its exempt function or otherwise not an unrelated trade or business, or donations, and not more than one-third of its financial support from investment income.
5. Item 6.

Item 6 provides an extremely helpful change from the current form. We believe that the incorporation of Form 872-C into the Form 1023 is a very good improvement.

a. In reviewing Part XI, Item 6(a), we note, however, that applicants may not be aware that the box that appears under the text of this Item is to be signed by the IRS rather than by the applicant. Specifically, in the draft Form 1032, a shaded area appears with the words “For IRS use only” in small type. Therefore, it might be helpful to emphasize, either through larger type, bold type, or different colored type, that this box is supposed to be signed by the IRS, and not by the applicant.

b. We suggest that the IRS include a copy of page 7 showing the IRS signatures along with the determination letter package.

c. Item 6 –Ib and –IIb should be annotated with a note that the supplemental lists of major donors are not open to public inspection with the rest of the Form 1023’s information.


Item 7, concerning receipt of any unusual grants, should be augmented by two points:

a. As was the case with Item 6, this Item should have a note that the names of contributors will not be open to public inspection. Furthermore, as we noted in our comments on the Instructions, it is not only the contributors’ name, but the date and amount of the grant, and a description of the grant, that may impermissibly disclose the donor’s identity, and the applicant should be advised that any such identifying information will need to be redacted from public disclosure. The Service has already adopted procedures along these lines for Form 990.1

b. The text here should specifically refer the applicant back to the Instructions for the definition of an unusual grant. This is a common area of misunderstanding.

O. Signature block.

We urge the IRS to protect from public disclosure the signature executed on this Form (as well as on any Form 2848 submitted with the application, and/or check remittance for the User Fee).

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1 See letter from Steven T. Miller, Exempt Organizations Division Director, to Gregory L. Colvin, dated October 28, 2002, as reported in Tax Notes on November 18, 2002 (p. 888).
V. COMMENTS ON SCHEDULES AND INSTRUCTIONS TO SCHEDULES

A. Schedule A – Churches.

1. General Comments.

   a. The draft Schedule A is commendable for departing from a mechanical tracking of the fourteen factors used to evaluate whether a religious organization qualifies as a “church” under Section 170(b)(1)(A)(vi). In particular, we are pleased that the draft has removed questions relating to the less inclusive characteristics found in those factors, particularly through deletion of the current Form’s questions 3 (“does the organization require prospective members to renounce other religious beliefs or their membership in other churches or religious orders to become members”) and 12 (“describe the organization's religious hierarchy or ecclesiastical government”).

   b. It is helpful that the draft Schedule is shorter than the current Form 1023 Schedule, and that there are Instructions tied to each question. These changes will make it easier for applicants to complete the Schedule.

2. Specific Comments.

   a. Questions 2 and 7.

   Question 2, “are you part of a group of churches with similar beliefs and structure?” and question 7, “do you have an established congregation or other regular membership group?” are helpful additions to the Form that will aid in distinguishing so-called “mail order” churches from bona fide houses of worship.

   b. Question 5.

   We suggest that this question concerning whether an applicant has a “school for the religious instruction of youth” is not needed. Among the fourteen factors used in determining whether an organization is a church, having such a program is by no means dispositive. As noted above, in our view the Schedule properly omits other factors, and we recommend that this one be omitted as well.

   c. Question 10.

   The Instructions should explain that the term “pastor/minister” as used in Items 10-12 includes not only pastors and ministers, but also rabbis, shamans, and other leaders of worship services or congregants. This explanation could follow the sentence in the Instructions that states: “church’ includes mosques, temples, synagogues, and other places where religious organizations described under section 501(c)(3) conduct regular worship services.”

   d. Question 11.

   Question 11 (“is your pastor/minister also one of your officers, directors, or trustees”) should be deleted; most if not all houses of worship will answer yes, and the information is likely
to be available, at least for pastors/ministers who are remunerated, through an applicant’s response at Part III, item 3.

e. Question 14.

We appreciate that applicants will be allowed to provide additional “information to establish that you are a church” at question 14.


Two questions retained from the current Schedule can be strengthened to help identify abusive churches. Question 12 (in the current Schedule’s question 14) states: “do you license or ordain pastors/ministers or issue church charter?” We believe that this question’s phrasing is overbroad because most churches license or ordain pastors/ministers. We suggest that it be restated: “do or will you license or ordain pastors/ministers who are not regular participants in the majority of your organization's religious services, or in a number each year that represents more than 5% of the regular participants in your organization’s religious services?”

Similarly, question 13 continues an inquiry from the present Schedule: “did you pay a fee for a church charter.” This question is likely to elicit “yes” answers from virtually all incorporated churches that were subject to a State filing fee upon their incorporation. We suggest the question instead read: “did you pay a fee for a church charter other than any payment required by your State’s administrative offices such as the Secretary of State or Franchise Tax Board?”

g. Add Question.

One additional area we suggest the Schedule explore is how many hours of service the pastor/minister provides the organization, and at what rate of compensation. To this end, we suggest that a portion of the current Schedule’s question 16 be rewritten as follows: “show how many hours a week each pastor/minister devotes to church work and the amount of compensation he/she receives from you.”

B. Schedule B – Schools, Colleges and Universities.

1. Definition of “Educational Organization”: Section I, Line 1.

The draft is better tailored to elicit the information required to make a determination of an organization’s tax-exempt status than the current application. The instructions do not accurately state the definition of an educational organization contained in Treasury Regulation § 1.170A-9(b)(1), however. The test set forth in the regulations states:

An educational organization is described in section 170(b)(1)(A)(ii) if its primary function is the presentation of formal instruction and it normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.
This can be broken down into a five-part test under which a school, college or university may qualify as an educational organization within the meaning of Section 170(b)(1)(A)(ii) if it:

a. Has the presentation of formal instruction as its primary function;

b. Normally maintains a regular curriculum;

c. Normally maintains a regular faculty;

d. Normally has a regularly enrolled body of students; and

e. Has a place where its educational activities are regularly carried on.

Schedule B should be revised to require a specific explanation of how the organization meets the test. Specifically, with regard to Schedule B, Section I, Line 1, we suggest that this question could read as follows:

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Is your primary function the presentation of formal instruction?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If yes, provide an explanation of how you satisfy this requirement.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Do you normally maintain a regular curriculum?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If yes, provide an explanation of how you satisfy this requirement.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>c. Do you normally maintain a regular faculty?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If yes, provide an explanation of how you satisfy this requirement.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>d. Do you normally have a regularly enrolled body of students?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If yes, provide an explanation of how you satisfy this requirement.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>e. Do you have facilities where your educational activities are regularly carried on?</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

We recommend that the Instructions for Schedule B, Part I, Line 1 be revised to state all five requirements of the Treasury Regulation § 1.170A-9(b)(1) test as discussed above.

2. **Non-Traditional Schools.**

The Instructions for the General Information portion of Schedule B should be expanded to state that schools under Section 170(b)(1)(A)(ii) of the Code can include other less traditional types of schools such as an outdoor survival school, a yoga school and a field school in the social

3. Section II, Item 3.

The Instructions do not accurately reflect the requirements of IRS Revenue Procedure 75-50, 1975-2 C.B. 587. The Instructions state: “Rev. Proc. 75-50 requires that you publish your nondiscriminatory policy as to students on an annual basis.” It goes on to request that applicant submit the page in the newspaper on which the notice appears.

Revenue Procedure 75-50 does not, in fact, require an organization to publish its nondiscriminatory policy annually. Rather, it states at Section 4.03:

Publicity. The school must make its racially nondiscriminatory policy known to all segments of the general community served by the school.

1. The school must use one of the following two methods to satisfy this requirement:

   a. The school may publish a notice of its racial nondiscriminatory policy in a newspaper of general circulation that serves all racial segments of the community….

   b. The school may use the broadcast media to publicize its racially nondiscriminatory policy if this use makes such nondiscriminatory policy known to all segments of the general community the school serves. (Emphasis added.)

The Revenue Procedure goes on to provide that the publicity requirements in subsection 1 will not apply under one of the following circumstances: (1) where an organization is a parochial or other church-related school that for the preceding three years has consisted of students at least 75% of whom are members of the sponsoring religious denomination or unit, the school may make its racially nondiscriminatory policy known in newspapers or circulars that the religious denomination or unit utilizes in the communities from which the students are drawn; or (2) if the school “customarily draws a substantial percentage of its students nationwide or worldwide from a large geographic section or sections of the United States and follows a racially nondiscriminatory policy as to students,” the publicity requirement may be demonstrated by the school showing that it “currently enrolls students of racial minority groups in meaningful numbers or, when minority students are not enrolled in meaningful numbers, that its promotional activities and recruiting efforts in each geographic area were reasonably designed to inform students of all racial segments in the general communities within the area of the availability of the school.”

We recommend revising the Instructions to state as follows:

You must demonstrate that you have made your nondiscriminatory policy known to all segments of the general community served by
the school. One way of meeting this requirement is to publish the school’s nondiscriminatory policy annually. For information on other ways of satisfying this requirement, see Revenue Procedure 75-50.

C. Schedule C – Hospitals and Medical Research Organizations.

1. Part I, Item 5b.

The Instructions ask the applicant to submit past records that detail “the number of times and the types of services provided” to charity care patients. We believe that it is impractical and unnecessary for large health care organizations to provide the information in the level of detail requested. In addition, applicants that are new organizations simply will not have the requested data. Applicants should instead be asked to provide a summary of their charity care experience in a format similar to that typically reported on a Form 990. We also think it would be helpful if the time period for this information were specified and limited to the time period of information reported in Part X (Financial Data) of the draft Form 1023.

We further note that the “community benefit” standard of Revenue Ruling 69-545, 1962-2 C.B. 117, does not require a hospital to provide charity care in order for it to qualify for exemption. While the provision of charity care may be relevant to the determination of qualification for exemption, we believe that the level of detail requested is unnecessary. If the IRS believes that the information requested is in fact necessary, then the Schedule should articulate the standard that will be applied in evaluating the information.


This question should clarify that it refers to office space rented to physicians, not to office space provided to physicians who are employed by the applicant.


The question asks whether the organization has a “community board of directors.” First, the Instructions to the Schedule should define this term so that applicants may respond appropriately. Second, as with the question concerning charity care, Revenue Ruling 69-545 does not require that a hospital have a community board as a prerequisite to exemption. Board composition is only one factor in the analysis. The Instructions to the Schedule should explain the analysis that will be applied in evaluating the information.

As currently drafted, the question asks an applicant to explain its board composition only if it answers “Yes” to the question, “Do you have a community board of directors?” Oddly, if an applicant answers “No,” there is no follow-up question. The question should be revised to ask an applicant to provide an explanation if it answers “No.” We suggest the following additional follow-up questions:

a. Does an organization described in section 170(b)(1)(A)(iii) exercise any rights or powers over the applicant (e.g., right to appoint members to the applicant’s board or right to approve certain transactions)? If so, please explain.
b. Does the law of the state in which you are incorporated require your governing body to be composed solely of physicians licensed to practice medicine in the state?

c. If the law of the state in which you are incorporated requires your governing body to be composed solely of physicians, does a section 170(b)(1)(A)(iii) organization that exercises rights and powers over you have a community board? If yes, please attach a description of the organization and its community board.

d. Please describe in detail any services you provide to a section 170(b)(1)(A)(iii) organization that exercises rights or powers over you.


In our experience the IRS generally asks in the course of the determination process whether medical services are provided by employed physicians and, if so, how physician compensation is determined and who determines it. If the IRS expects to ask this question of all organizations that employ physicians, we suggest that the question appear in the application. We note, however, that if the IRS does ask this question in the determination process, the instructions to the Schedule should explain the analysis that will be applied in evaluating the information.

5. Non-Acute Care Hospitals.

The questions in the draft Schedule C Part I are designed for acute care hospitals. We suggest that the IRS consider including in the Form 1023 a new category of questions that would be applicable to “hospitals” that are not acute care in-patient facilities or medical research organizations, but which may qualify under Section 170(b)(1)(A)(iii). The questions would be directed toward organizations such as outpatient clinics or physician practices owned by hospitals. Items 1 and 4 are not generally relevant for such entities.

D. Schedule D – Section 509(a)(3) Supporting Organizations.

The addition of specific questions that correspond with the tests for each of the three types of supporting organizations is a wonderful improvement.

1. Item 1. Instructions.

The Instructions to Item 1 provide that an applicant should answer “Yes” to the question if the applicant’s governing document, bylaws or other internal rules and regulations show that the majority of the applicant’s governing board or officers are elected or appointed by the supported organization(s). It might be helpful to specify in the Instructions that the supported organization(s) can elect or appoint a majority of the applicant’s governing board or officers through action of (i) the governing body of the supported organization(s), (ii) officers of the supported organization(s) acting in their official capacities, or (iii) the membership, if any, of the supported organization(s). See Treas. Reg. § 1.509(a)-4(a)(1)(i).
2. Section II, Item 3. Instructions.

The “Note” in the Instructions recommends that an applicant that is a charitable trust seeking to be a Type III supporting organization contact its “state official” if the applicant is unsure whether its beneficiary organization has the power to enforce the trust and compel an accounting under state law. It might be helpful if an example is provided of the title of the state official or the name of the state governmental agency that should be contacted for additional guidance (e.g., the state attorney general or the state attorney general’s office).

3. Section II, Item 4a.

Item 4a asks whether the officers, directors or trustees of the supported organization(s) appoint one or more of the officers, directors or trustees of the applicant. Pursuant to Treasury Regulation § 1.509(a)-4(i)(2)(ii)(a), the membership, if any, of the supported organization(s) may also appoint the officers, directors or trustees of the applicant to satisfy the alternative “operated in connection with” responsiveness test. It might be helpful to revise both the question in Item 4a and the accompanying Instructions to include the membership of the supported organization(s) as an additional group that may appoint the officers, directors or trustees of the applicant.

4. Section II, Items 6b/6c.

It might be helpful to add lines on which an applicant can answer the questions in Items 6b and 6c.

5. Section IV, Item 2.

If an applicant answers “No” to the question in Item 2, the Instructions require the applicant to attach an explanation describing the circumstances under which the applicant supports or benefits an organization not specified in Sections I, II or III of Schedule D. An applicant will not know to attach such an explanation, however, unless the Instructions are read together with the question in Item 2. Therefore, it might be helpful to add the following language after the question in Item 2: “If “No,” refer to the Instructions.”

6. Section IV, Item 5.

The third bullet point has a typo: “The complexity of the your filing …. ” Delete “the.”

E. Schedule E – Organizations Not Filing Form 1023 with 27 Months of Formation.

1. Comments Regarding Instructions.

a. We are pleased that the draft Form 1023 takes the Technical Questions from the current Form’s Part III, lines 1-6, and moves them into a Schedule format where they will need to be addressed only by applicants whose ability to qualify for Section 501(c)(3) status retroactively is at issue. We note a technical inaccuracy in the Form itself, however, which incorrectly drives an applicant to this Schedule if more than 27
months have passed since the applicant was formed. Part VII, Item 5 should be corrected to provide that only applicants who have had 27 months pass *after the end of the month* in which they were formed need to complete this Schedule.

b. The Instructions do not indicate the Schedule’s purpose and effect. We suggest that a preamble be included with the Schedule E instructions to explain to the reader the nature of the Schedule, as follows:

Most organizations are required to give notice to the IRS of their desire and ability to be recognized as exempt under section 501(c)(3) by filing an exemption application. When an organization files an application within 27 months from the end of the month in which it was formed, the IRS must recognize the organization as exempt back to the date the organization was formed. In that case, donors to the organization may deduct their donations to the organization as charitable contributions back to the date the organization was formed. The questions in this Schedule are designed to allow the IRS to determine the effective date of your section 501(c)(3) status if this application is approved. The questions here first relate to possible exceptions from having to file an application. For applicants who are late in filing and meet no automatic exception, the questions go on to evaluate the ability of the applicant to qualify, prior to the date of filing this application, as tax-exempt under section 501(c)(3), or, alternatively, under section 501(c)(4).

c. The instruction for Item 2 does not explain how to test whether the organization’s “annual gross receipts exceed $5,000.”

d. For ease of understanding, we suggest that the italicized text after the Item 3 Instruction be augmented by a conclusion. We suggest that the text be modified as follows (shown in italics): “If you indicated “Yes” to any of the above items, do not complete the rest of this Schedule. Your section 501(c)(3) status will be in effect as of the date of formation of the organization.”

e. Similarly, the text after the Item 4 instruction relating to those who answer “Yes” needs an explanatory conclusion. We suggest the addition of the following after the directive not to complete the rest of the schedule: “If you indicated ‘Yes’ to any of the above items, do not complete the rest of this Schedule. Your section 501(c)(3) status will be in effect as of the date of formation of the organization.”

f. We are intrigued by the instruction at Item 6. It appears that even if an applicant does not request extension of time to file Form 1023 under Treasury Regulations § 301.9100, the IRS is inviting requests for partial period retroactive status under section 501(c)(3). The draft Instruction states: “Answer “No” if you filed the Form 1023 late, did not request an extension under … item 5, but still wish to pursue exemption under section 501(c)(3) prior to the received date of the Form 1023.”
The instruction goes on to request an explanation from the applicant as to why it believes qualification “prior to the received date of the Form 1023” should be allowed, and mentions appeal rights in the event of an unfavorable ruling. If it is the case that late filing organizations can request a time-specific retroactive ruling, we suggest this be stated more explicitly in the Instructions. The factors by which the IRS will evaluate such requests also be stated.

2. Comments Regarding Draft Schedule E Form.

a. The text of Items 1-3 should direct applicants to the instructions (e.g., Item 1: “Are you a church, association of churches, or integrated auxiliary of a church? See instructions”)

b. The text in Item 4 for those who answer “Yes” needs an explanatory conclusion. We suggest the following addition (shown in italics): “If “Yes,” stop here. Your Section 501(c)(3) status will be in effect as of the date of formation of the organization.”

c. We suggest that an important note be added to Item 7, as follows:

Note: If you check “Yes” and file the completed page 1 of Form 1024, you are asking for a determination letter that will first allow exemption under section 501(c)(4) from date of formation until the filing date of this application, and then allow section 501(c)(3) status forward from that date. If you check “No”, you are asking for a determination letter that will grant section 501(c)(3) status only from the date this application was received; for the period(s) before that date you will be treated as taxable (i.e., not tax-exempt). For more information about tax deductions for charitable contributions and returns due for any periods prior to recognition of section 501(c)(3) status, see the instructions to this Item.

d. We understand that Item 8 is intended to capture two projected years budgets for organizations that file later than the 27th full month following the end of the month in which they were formed (without being granted automatic or relief exception from the notice deadline). The format of the revenue presentation here should tie to that in Part X-A, and our earlier comments about lines 1-14 of Part X-A should be read here as well. In addition, we do not see why applicants are required to total the two years shown, and suggest that the third column be deleted.

F. Schedule G – Successors to “For-Profit” Organizations.

Overall the draft Schedule G improves on the existing Schedule I. The Instructions, in particular, provide helpful background. The second paragraph, however, states “You should complete this schedule if you took over the assets of a for-profit organization….” As noted above concerning the Instructions at Part VII regarding “successor” organizations, the language “took over” is vague and over-inclusive. Please see our comments above to the Instructions at Part VII regarding suggested descriptions of “successor” organizations.
G. Schedule H – Organizations Providing Scholarship Benefits, Student Aid, Etc. to Individuals.

The draft Schedule H is a significant improvement over the existing form. It is generally much clearer and easier for the applicant to understand. We have only a few suggestions for changes.

1. Question 2.

The only acceptable answer to Question 2 as written is “yes.” The last sentence should be revised to read, “If “No,” attach a statement explaining how you will demonstrate that your educational grants are being used for charitable purposes.”

2. Question 7.

The references in Question 7 to grants under Sections 4945(g)(2) and (g)(3) indicate that Schedule H is required not only for scholarships, fellowships, and other forms of educational assistance to individuals, but also for prizes and awards in recognition of past achievement (Section 4945(g)(2)) and specific project grants to individuals (Section 4945(g)(3)). If this is the case, Schedule H should be renamed to make this clear, and references in Form 1023 to Schedule H should include the larger purpose. (Currently some private foundation applicants complete Schedule H for all three types of Section 4945(g) grants when the applicant anticipates such activities. The reviewing agents find it very difficult to issue a determination letter referring to Section 4945(g)(2) or (3) grant procedures, however, which tends to result in much correspondence to obtain a proper determination letter.) Also, the questions in Schedule H should be revised to include the information the Service may require in order to approve grant procedures under Sections 4945(g)(2) and (3) as well. If Schedule H is appropriate only for scholarships, applicants should be so informed, and applicants should be instructed to provide the necessary information under Sections 4945(g)(2) and (3) elsewhere.

3. Instructions, Item 1d.

“Verbally” should be “orally.”