



## THE IRS RELEASES FORM 1023-EZ FOR SMALL NONPROFIT ORGANIZATIONS

### Introduction

On July 1, 2014, the Internal Revenue Service (“IRS”) introduced the [Form 1023-EZ](#), a shorter version of the Form 1023 for small charities seeking 501(c)(3) tax-exempt status. Previously, all organizations seeking 501(c)(3) tax-exempt status, regardless of size, had to complete the 26-page Form 1023.

The Form 1023-EZ is three pages long and eliminates the questions on the Form 1023 asking for details about the applicant’s mission and purposes, prior activities, compensation arrangements, fundraising plans, and projected income and expenses.

The IRS hopes that use of the new form will reduce the backlog of pending applications at the IRS by speeding up the approval process for smaller groups and freeing up resources to review applications from larger, more complex organizations.

### Who May File

In order to be eligible to file the Form 1023-EZ, the organization’s gross receipts for each of the three prior years (or, in the case of a new organization, its projected gross receipts for each of the next three years)

cannot exceed \$50,000 and its total assets cannot exceed \$250,000.

In addition, certain organizations are not eligible to use the simplified Form 1023-EZ even if the organization meets the gross receipts and assets test. The organizations not eligible to file the Form 1023-EZ include the following:

- Foreign organizations;
- Limited liability companies;
- Entities that are successor organizations to:
  - for-profit entities, or
  - tax-exempt entities that lost their exempt status for reasons other than failing to file the Form 990 for three consecutive years;
- Churches and associations of churches;
- Hospitals and medical research organizations;
- Schools seeking public charity status;
- Cooperative service organizations of operating educational organizations;
- Supporting organizations operated in connection with one or more publicly supported organizations that qualify under Section 509(a)(3);

- Organizations that have as a substantial purpose providing consumer credit counseling, including budgeting, personal finance, financial literacy, and mortgage foreclosure assistance;
- Health maintenance and accountable care organizations; and
- Organizations seeking retroactive reinstatement of exempt-status under Section 5 or 6 of [Rev. Proc. 2014-11](#), after being automatically revoked.

### How to File

The Form 1023-EZ must be filed online using <http://pay.gov>. There is a \$400 user fee that must be paid at the time of submission. For additional instructions on filing the form, go to <http://www.irs.gov/uac/About-Form-1023EZ>.

### What to File

Form 1023-EZ consists of six parts that must be completed by the organization seeking tax-exempt status. However, as a first step, the IRS asks the organization to state whether it completed the Form 1023-EZ Eligibility Worksheet, which is contained on pages 11-17 in the [instructions for Form 1023-EZ](#).

The worksheet, which does not have to be included with the application, asks a series of questions about the organization, and whether it meets the eligibility requirements for filing a Form 1023-EZ, as described above. If the organization answers yes to any of the eligibility questions, it cannot file a Form 1023-EZ, and must file Form 1023.

Next, if the organization satisfies the eligibility requirements, it must complete

Part I – Identification of the Applicant. In Part I, the IRS asks the organization for:

- Its name, address, email address and website;
- The name and telephone number of the contact person;
- The organization’s employer identification number;
- The tax year; and
- The names and mailing addresses of the organization’s officers, directors and trustees

In Part II – Organizational Structure, the form asks about the organization’s structure and whether it meets the requirements of Section 501(c)(3). Specifically, the organization must state:

- Whether it is a corporation, unincorporated association or trust;
- Whether the organization has adopted an organizational document, such as a trust agreement or articles of incorporation;
- The date that the organization was established;
- The state of incorporation or formation; and
- Whether the organizational document:
  - Limits the purposes of the organization to one or more tax-exempt purposes under Section 501(c)(3);
  - Does not expressly empower the organization to engage, other than in an “insubstantial” way, in activities that are not in furtherance of its exempt purposes; and
  - Contains a provision that upon dissolution of the organization, the organization’s assets will be used for an exempt purpose.

In Part III – Your Specific Activities, the organization is asked to provide a three character NTEE code that best describes its activities. A list of the possible codes is included in the Form 1023-EZ instructions.

Next, the organization is asked a series of questions relating to its activities, and whether those activities are consistent with a tax-exempt organization.

The organization must indicate whether it: is a charitable, religious, scientific, educational, or literary organization; fosters national or international amateur sports competition; tests for public safety; or prevents cruelty to children or animals.

In addition, the organization must certify that it will not engage in activities that violate the IRS rules for exempt organizations. In particular, the organization may not:

- Support or oppose candidates in political campaigns;
- Use any of the organization's assets for the benefit of officers, directors, key management employees and other insiders;
- Engage in non-exempt activities, except in an "insubstantial" way;
- Be organized or operated for the primary purpose of engaging in a trade or business unrelated to the organization's exempt purposes;
- Devote more than an insubstantial part of its activities attempting to influence legislation; and
- Provide commercial type insurance as a substantial part of its activities.

Part III also asks the organization to answer eight yes or no questions. The questions are:

1. Will the organization attempt to influence legislation?
2. Will the organization pay compensation to its officers, directors or trustees?
3. Will the organization donate funds or pay the expenses for individuals?
4. Will the organization operate outside the US or offer assistance to organizations or individuals who do?
5. Will the organization engage in financial transactions (such as loans, payments, rents, etc.) with any officers, directors, trustees or any entities they control?
6. Will the organization have unrelated business gross income of \$1,000 or more in a tax year?
7. Will the organization operate bingo or other gaming activities?
8. Will the organization provide disaster relief?

Based on the answers to these questions, the IRS may ask the organization for additional information before it determines whether or not the organization qualifies as an exempt organization.

Part IV- Foundation Classification asks the organization to state whether it is a:

- Public charity that receives a substantial part of its support from the general public; or
- Private foundation that is typically funded by an individual, family, or business, and derives its income primarily from investments.

Donations to public charities are deductible up to 50% of the donor's adjusted gross income, while donations to private foundations may be limited to 30% of the donor's adjusted gross income.

Part V – Reinstatement After Automatic Revocation asks the organization if it is applying for reinstatement as an exempt organization because it failed to file the Form 990-N for three consecutive years.

Finally, in Part VI - Signature, an authorized representative must sign the application. The application is filed under the penalties of perjury, by which the person signing the form states that, to the best of his or her knowledge, the information in the form is true, correct and complete.

### **Effect of Tax Exempt Status**

If an organization files its application within 27 months of the date it was formed, and was organized and operated in a manner consistent with Section 501(c)(3) during the time its application was pending, the IRS will grant the organization tax-exempt status retroactive to the date it was formed.

In all other cases, the organization's tax-exempt status will be retroactive to the date the application was filed.

### **Organizations with Pending Applications**

If an organization has already filed an application for tax-exempt status using the Form 1023, it can still file a Form 1023-EZ, along with the \$400 application fee, provided the original application has not been assigned for review. The new application will be treated as if the organization had withdrawn the original application and filed the Form 1023-EZ instead.

The organization will not receive a refund of its original application fee. In addition, the date the organization files the Form 1023-EZ will be treated as the filing date, and if it is more than 27 months after the

organization is formed, the organization's tax-exempt status will be retroactive to the date the Form 1023-EZ was filed, and not to the date the original Form 1023 was filed or the date the organization was formed.

### **Don't Go It Alone**

While the Form 1023 poses many challenges to an organization seeking tax-exempt status, it also provides many benefits as well.

First, on the Form 1023 the IRS requests a great deal of detail about the organization's mission, proposed activities, projected income and sources of income, compensation arrangements, etc. As a result, the organization needs to develop a fully thought-out business plan before filing its application.

Additionally, in the instructions to the Form 1023, the IRS provides policies that it requires the organization to adopt, such as a conflict of interest policy, along with sample documents. These documents and policies help ensure that the organization's governance gets off to a good start.

Next, the in-depth review of the application can bring to light compliance issues that are best addressed when the organization is new.

Finally, the complexity of the Form 1023 application process encourages nonprofit organizations to seek legal assistance. The nonprofit's attorney will not only help them with the Form 1023 application, but will also assist them with understanding the compliance requirements for tax-exempt organization under the Internal Revenue Code, federal and state labor laws, nonprofit corporation laws, charitable solicitation laws and other federal and state laws.

Nonprofits that try to go it alone will miss out on many of these benefits, and may find themselves in serious legal trouble later. Therefore, if a nonprofit decides to make use of the Form 1023-EZ, it should still take certain steps to make sure it gets off to a good start. These include:

- ✓ **Develop a business plan for your organization.** It is important to understand what your organization will be doing; how much it will cost; and what sources of funding you can tap.
- ✓ **Find pro bono legal assistance.** Even though the Form 1023-EZ is easier to fill out, you are still taking on a lot of legal responsibilities when you form a tax-exempt organization. The IRS will want to verify that your organization is satisfying the requirements for a tax-exempt organization on an on-going basis. It may conduct compliance checks or audit examinations on an after-the-fact basis.
- ✓ **Get help when drafting your articles of incorporation and bylaws.** You

need to be certain that these important documents comply with the DC Nonprofit Code as well as the IRS's requirements for tax exempt organizations.

- ✓ **Protect your name and logo.** Before you get started, you will need help picking a name for your organization. You want to make sure that another group is not already using the organization's name, and that you can protect your name and logo with the US Patent and Trademark Office.
- ✓ **Get educated.** There is lot for you to learn about, including the rules governing fundraising, acknowledging contributions, hiring employees and risk management and insurance.
- ✓ **Find help recruiting a strong board.**

For further details about Form 1023-EZ, go to the [IRS website](#) or review [IRS Revenue Procedure 2014-40](#).

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