

# Contents

About the Author	xxvii
Preface	xxix
About the Online Resources	xxxiii
Book Citations	xxxv

## **PART ONE: INTRODUCTION TO THE LAW OF TAX-EXEMPT ORGANIZATIONS**

<b>1</b>	<b>Definition of and Rationales for Tax-Exempt Organizations</b>	<b>3</b>
§ 1.1	Definition of <i>Nonprofit</i> Organization	3
	(a) <i>Nonprofit Organization</i> Defined	4
	(b) Nonprofit Sector	5
§ 1.2	Definition of <i>Tax-Exempt</i> Organization	7
§ 1.3	Tax-Exempt Organizations Law Philosophy	9
§ 1.4	Political Philosophy Rationale	11
§ 1.5	Inherent Tax Rationale	17
§ 1.6	Other Rationales and Reasons for Exempt Organizations	18
§ 1.7	Freedom of Association Doctrine	19
<b>2</b>	<b>Overview of Nonprofit Sector and Tax-Exempt Organizations</b>	<b>23</b>
§ 2.1	Profile of Nonprofit Sector	24
§ 2.2	Organization of IRS	28
	(a) IRS in General	29
	(b) Tax Exempt and Government Entities Division	30
§ 2.3	Charitable Contribution Deduction Rules	32
§ 2.4	Evolution of Statutory Regime	35

## **PART TWO: FUNDAMENTALS OF THE LAW OF TAX-EXEMPT ORGANIZATIONS**

<b>3</b>	<b>Source, Advantages, and Disadvantages of Tax Exemption</b>	<b>43</b>
§ 3.1	Source of Tax Exemption	43
§ 3.2	<i>Recognition</i> of Tax Exemption	45
§ 3.3	Recognition of Public Charity, Private Foundation Status	48
§ 3.4	Advantages of Tax-Exempt Status	48
	(a) Tax Exemption	48
	(b) Deductibility of Contributions	49
	(c) Grants	50
	(d) Preferential Postal Rates	50
	(e) Employee Benefits	50

## CONTENTS

	(f) Antitrust Laws	50
	(g) Securities Laws	51
	(h) Other Advantages	53
§ 3.5	Disadvantages of Tax-Exempt Status	56
§ 3.6	Alternatives to Tax-Exempt Status	57
<b>4</b>	<b>Organizational, Operational, and Related Tests and Doctrines</b>	<b>61</b>
§ 4.1	Forms of Tax-Exempt Organizations	62
	(a) General Rules	62
	(b) Check-the-Box Regulations	64
	(i) Basic Rules	64
	(ii) Exempt Organization Rules	65
§ 4.2	Governing Instruments	66
§ 4.3	Organizational Test	67
	(a) Statement of Purposes	68
	(b) Dissolution Requirements	71
	(c) Mission Statements	73
	(d) Board Composition	73
	(e) Rules for Limited Liability Companies	74
	(f) What Test Does Not Encompass	75
	(i) Banking Law	75
	(ii) IRS Ruling Policy	76
§ 4.4	Primary Purpose Test	77
§ 4.5	Operational Test	82
	(a) Basic Rules	82
	(b) Activities Tests	86
	(c) Quantification of Activities	87
	(d) Action Organizations	88
	(e) Aggregate Principle	89
§ 4.6	Exclusively Standard	90
§ 4.7	Commensurate Test	93
§ 4.8	Consideration of Organizations' Names	95
§ 4.9	State Action Doctrine	96
	(a) Doctrine in General	97
	(b) Doctrine as Applied to Social Clubs	103
	(c) Doctrine and Other Exempt Organizations	104
	(d) Statutory Law	106
§ 4.10	Operations for Profit	106
§ 4.11	Commerciality Doctrine	112
	(a) Summary of Doctrine	112
	(b) Rationale Underlying Doctrine	112
	(c) Origin of Doctrine	113
	(i) Internal Revenue Code	114
	(ii) Tax Regulations	116
	(iii) Beginnings of Doctrine	117
	(iv) Focus on Publishing	118
	(d) Contemporary Application of Doctrine	123
	(e) Contemporary Perspective on Doctrine	127

## CONTENTS

§ 4.12	Social Enterprise Developments	128
	(a) Concept of <i>Social Enterprise</i>	129
	(b) Program-Related Investments	130
	(c) Low-Profit Limited Liability Companies	130
	(d) B Corporations	130
	(e) Benefit Corporations	131
	(f) Flexible Purpose Corporations	131
<b>5</b>	<b>Nonprofit Governance</b>	<b>133</b>
§ 5.1	Boards of Directors Basics	134
§ 5.2	Board Composition and Tax Law	134
§ 5.3	Duties and Responsibilities	135
§ 5.4	Board Member Liability	136
§ 5.5	Sarbanes-Oxley Act	136
§ 5.6	Nonprofit Governance Principles	137
	(a) Governance Philosophy in General	137
	(b) Senate Finance Committee Staff Paper	137
	(c) Treasury Department's Voluntary Best Practices	138
	(d) Committee for Purchase Proposed Best Practices	140
	(e) American National Red Cross Governance Modernization Act	141
	(f) Independent Sector's Governance Principles	142
	(i) Legal Compliance and Public Disclosure	142
	(ii) Effective Governance	143
	(iii) Strong Financial Oversight	144
	(iv) Responsible Fundraising	145
	(g) Redesigned Form 990	145
	(h) Boards of Credit Counseling Organizations	147
	(i) Other Developments	147
§ 5.7	IRS and Governance	148
	(a) Matter of Agency Jurisdiction	148
	(b) IRS Officials' Speeches	150
	(c) IRS Ruling Policy	152
	(d) IRS Training Materials	154
	(e) IRS Governance Check Sheet	155
	(i) Governing Body and Management	155
	(ii) Compensation	156
	(iii) Organizational Control	156
	(iv) Conflicts of Interest	156
	(v) Financial Oversight	156
	(vi) Document Retention	156

## PART THREE: TAX-EXEMPT CHARITABLE ORGANIZATIONS

<b>6</b>	<b>Concept of <i>Charitable</i></b>	<b>159</b>
§ 6.1	Federal Tax Law Definition of <i>Charitable</i>	160
	(a) Popular and Ordinary Definition	160
	(b) Common Law Definition	160
	(c) Federal Tax Law Definition	162

## CONTENTS

§ 6.2	Public Policy Doctrine	166
	(a) General Principles	166
	(b) Race-Based Discrimination	168
	(i) Supreme Court Pronouncement	168
	(ii) IRS Policy	169
	(iii) Broader Policy Impact	171
	(c) Gender-Based Discrimination	172
	(d) Other Forms of Discrimination	173
	(e) Affirmative Action Principles	174
§ 6.3	Collateral Concepts	176
	(a) Requirement of <i>Charitable Class</i>	176
	(b) Means-to-End/Instrumentality Rule	179
	(c) <i>Charity</i> as Evolutionary Concept	181
	(d) Motive	181
	(e) Private Use	182
	(f) <i>Cy Pres</i> Doctrine	183
	(g) Fluid Recovery Principles	184
	(h) Charging of Fees	186
	(i) Illegal Activities	186
	(j) Tax Exemption Does Not Create Contract	188
	(k) Tax Exemption Does Not Create Third-Party Beneficiaries	189
	(l) Tax Exemption Does Not Create Private Right of Action	189
	(m) Tax Exemption Does Not Create Charitable Trust	190
<b>7</b>	<b>Charitable Organizations</b>	<b>191</b>
§ 7.1	Relief of Poor	192
§ 7.2	Relief of Distressed	194
	(a) General Principles	194
	(b) Disaster Relief Programs	194
§ 7.3	Credit Counseling	197
	(a) Initial Evolution of Exemption Law	197
	(b) IRS Enforcement Program	198
	(c) Contemporary IRS Policy	199
	(d) Statutory Criteria for Exemption	200
§ 7.4	Provision of Housing	202
§ 7.5	Down Payment Assistance	203
§ 7.6	Promotion of Health	205
	(a) Hospital Law in General	205
	(b) Additional Statutory Requirements for Hospitals	208
	(i) Hospitals Subject to Requirements	208
	(ii) Community Health Needs Assessments	208
	(iii) Financial Assistance Policy	209
	(iv) Emergency Medical Care Policy	210
	(v) Limitation on Charges	210
	(vi) Billing and Collection	210
	(vii) Mandatory IRS Review of Tax Exemption	210
	(viii) Effective Dates	210

## CONTENTS

- (c) Hospital Clinical Departments and Funds 210
- (d) Medical Research Organizations 211
- (e) Homes for Aged 212
- (f) Health Maintenance Organizations 212
- (g) Integrated Delivery Systems 214
- (h) Peer Review Organizations 215
- (i) Fitness Centers 218
- (j) Other Health Care Organizations 219
- (k) Regional Health Information Organizations 221
- (l) Health Insurance Exchanges 222
- (m) Accountable Care Organizations 223
  - (i) ACOs in General 224
  - (ii) CMS Regulations 224
  - (iii) Tax-Exempt Organizations Issues 225
- § 7.7 Lessening Burdens of Government 228
- § 7.8 Advancement of Education 232
- § 7.9 Advancement of Science 235
- § 7.10 Advancement of Religion 235
- § 7.11 Promotion of Social Welfare 237
- § 7.12 Promotion of Arts 240
- § 7.13 Consortia 242
  - (a) General Principles 242
  - (b) Adjunct Theory 245
  - (c) Cooperative Arrangements 246
- § 7.14 Fundraising Organizations 247
  - (a) General Principles 248
  - (b) Application of Commensurate Test 249
  - (c) Other Exemption Issues 251
- § 7.15 Instrumentalities of Government 252
- § 7.16 Other Categories of Charity 256
  - (a) Environmental Protection 256
  - (b) Promotion of Patriotism 257
  - (c) Promotion of Sports 257
  - (d) Public Interest Law 258
  - (e) Local Economic Development 260
  - (f) Other Charitable Organizations 261

## 8 Educational Organizations

263

- § 8.1 Federal Tax Law Definition of *Educational* 263
- § 8.2 *Education* Contrasted with *Propaganda* 264
- § 8.3 Educational Institutions 267
  - (a) Schools, Colleges, and Universities 267
    - (i) General Criteria 268
    - (ii) IRS Inquiry 270
  - (b) Museums and Similar Organizations 270
  - (c) Other Educational Organizations 272

## CONTENTS

§ 8.4	Instruction of Individuals	272
§ 8.5	Instruction of Public	276
§ 8.6	Educational Activity as Commercial Business	280
§ 8.7	Educational Activity as Private Benefit Function	284
§ 8.8	Child Care Organizations	284
<b>9</b>	<b>Scientific Organizations</b>	<b>287</b>
§ 9.1	Federal Tax Law Definition of <i>Science</i>	287
§ 9.2	Concept of <i>Research</i>	288
§ 9.3	Requirement of <i>Public Interest</i>	291
§ 9.4	<i>Scientific</i> as <i>Charitable</i> or <i>Educational</i>	292
§ 9.5	Technology Transfer	292
<b>10</b>	<b>Religious Organizations</b>	<b>295</b>
§ 10.1	Constitutional Law Framework	295
	(a) General Constitutional Law Principles	296
	(i) Free Exercise Clause	296
	(ii) Establishment Clause	297
	(iii) Religious Freedom Restoration Act	300
	(iv) Free Speech Considerations	301
	(b) Constitutional Law and Tax Exemption	301
	(c) Internal Revenue Code Provisions	303
§ 10.2	Federal Tax Law Definition of <i>Religion</i>	305
	(a) <i>Religion</i> Defined	305
	(b) Bases for Denial of Tax Exemption	309
	(c) Abuse of Tax Exemption	310
§ 10.3	Churches and Similar Institutions	312
	(a) General Principles	312
	(b) Associational Test	316
§ 10.4	Conventions or Associations of Churches	319
§ 10.5	Integrated Auxiliaries of Churches	320
§ 10.6	Mission Societies	322
§ 10.7	Religious Orders	322
§ 10.8	Apostolic Organizations	323
§ 10.9	Communal Groups	325
§ 10.10	Retreat Facilities	326
<b>11</b>	<b>Other Charitable Organizations</b>	<b>329</b>
§ 11.1	Cruelty Prevention Organizations	329
§ 11.2	Amateur Sports Organizations	329
§ 11.3	Public Safety Testing Organizations	331
§ 11.4	Cooperative Hospital Service Organizations	332
§ 11.5	Cooperative Educational Service Organizations	335
§ 11.6	Charitable Risk Pools	335
§ 11.7	Literary Organizations	336

## CONTENTS

- § 11.8 Donor-Advised Funds 336
  - (a) Donor-Advised Fund Basics 337
  - (b) Statutory Criteria 338
- § 11.9 Endowment Funds 340
  - (a) Definition of *Endowment Fund* 340
  - (b) College and University Endowments 340
  - (c) Form 990 Reporting 342

## 12 Public Charities and Private Foundations

343

- § 12.1 Federal Tax Law Definition of *Private Foundation* 344
  - (a) *Private Foundation* Defined 344
  - (b) Private Operating Foundations 344
  - (c) Exempt Operating Foundations 346
  - (d) Conduit Foundations 347
  - (e) Common Fund Foundations 348
  - (f) Other Types of Foundations 348
  - (g) Organizational Test 349
- § 12.2 Disqualified Persons 350
  - (a) Substantial Contributors 350
  - (b) Foundation Managers 352
  - (c) Twenty Percent Owners 352
  - (d) Family Members 353
  - (e) Corporations 354
  - (f) Partnerships 354
  - (g) Trusts or Estates 354
  - (h) Private Foundations 354
  - (i) Governmental Officials 355
- § 12.3 Categories of Public Charities 356
  - (a) Institutions 356
  - (b) Publicly Supported Charities 356
    - (i) Donative Publicly Supported Charities in General 356
    - (ii) Facts-and-Circumstances Test 359
    - (iii) Community Foundations 360
    - (iv) Service Provider Publicly Supported Organizations 361
    - (v) Public Colleges and Universities Support Foundations 363
  - (c) Supporting Organizations 364
  - (d) Public Safety Testing Organizations 369
- § 12.4 Private Foundation Rules 369
  - (a) Self-Dealing 370
  - (b) Mandatory Distributions 372
  - (c) Excess Business Holdings 374
  - (d) Jeopardizing Investments 375
  - (e) Taxable Expenditures 377
  - (f) Other Provisions 380
- § 12.5 Consequences of Private Foundation Status 381

## CONTENTS

### PART FOUR: OTHER TAX-EXEMPT ORGANIZATIONS

<b>13 Social Welfare Organizations</b>	<b>385</b>
§ 13.1 Concept of <i>Social Welfare</i>	385
(a) General Rules	385
(b) Benefits to Members	388
§ 13.2 Requirement of <i>Community</i>	391
(a) Community and Condominium Associations	391
(b) Broader Requirement of <i>Community</i>	395
§ 13.3 Conduct of Business	396
§ 13.4 Advocacy Organizations	397
(a) Legislative Activities	397
(b) Political Campaign Activities	397
§ 13.5 Comparison with Charitable Organizations	397
<b>14 Business Leagues and Like Organizations</b>	<b>401</b>
§ 14.1 Concept of <i>Business League</i>	401
(a) General Principles	402
(i) Tax Law Characteristics	402
(ii) Members	403
(iii) Dues	404
(b) Meaning of <i>Business</i>	404
(c) Line-of-Business Requirement	405
(i) Concept of <i>Line of Business</i>	405
(ii) Supreme Court Pronouncement	405
(iii) Other Developments	406
(d) Membership Services	408
(e) Professional Organizations	410
(f) Business Leagues in General	411
(g) Certification Programs	413
§ 14.2 Disqualifying Activities	414
(a) Line-of-Business Requirement	414
(b) For-Profit Business Activities	415
(i) General Rule	415
(ii) Incidental Business Activity	416
(c) Performance of Particular Services	417
(i) Particular Services	417
(ii) General Rule	418
(iii) Particular Services outside Membership	423
(iv) Unrelated Business Activities	423
(d) Private Inurement	424
(e) Commerciality	424
§ 14.3 Chambers of Commerce	425
§ 14.4 Boards of Trade	426
§ 14.5 Real Estate Boards	427



## CONTENTS

<b>15 Social Clubs</b>	<b>429</b>
§ 15.1 Social Clubs in General	429
(a) Rationale for Tax Exemption	429
(b) Club Functions	430
(c) Other Tax Law Matters	433
§ 15.2 Public Use Limitation	433
§ 15.3 Investment Income Limitation	435
§ 15.4 Exceptions to Limitations	437
§ 15.5 Taxation of Social Clubs	438
§ 15.6 Sale of Club Assets	443
<b>16 Labor, Agricultural, and Horticultural Organizations</b>	<b>445</b>
§ 16.1 Labor Organizations	445
§ 16.2 Agricultural Organizations	450
§ 16.3 Horticultural Organizations	454
<b>17 Political Organizations</b>	<b>455</b>
§ 17.1 Political Organizations in General	456
(a) <i>Political Organizations</i> Defined	457
(b) Principal Campaign Committees and Newsletter Funds	459
§ 17.2 Organizational Test	460
§ 17.3 Operational Test	460
§ 17.4 Public Policy Advocacy Activities	461
§ 17.5 Taxation of Political Organizations	462
§ 17.6 Taxation of Other Exempt Organizations	464
§ 17.7 Avoiding Political Organizations Tax	466
§ 17.8 Independent Political Action Committees	468
<b>18 Employee Benefit Funds</b>	<b>469</b>
§ 18.1 Overview of Employee Benefits Law	470
(a) Compensation in General	470
(b) Fringe Benefits	471
(c) Deferred Compensation	472
(d) Qualified Plans	472
(i) Defined Benefit Plans	472
(ii) Defined Contribution Plans	472
(iii) Funding Mechanism	474
(e) 403(b) Plans	475
(f) Nonqualified Plans	476
(i) 457(b) Plans	477
(ii) 457(e)(11) Plans	477
(iii) 457(f) Plans	477
(iv) Rabbi Trusts	478
(g) Options for Tax-Exempt Employers	478
(h) Perspective	479

## CONTENTS

§ 18.2	Special Rules for Welfare Benefit Funds	479
	(a) Nondiscrimination Requirements	479
	(b) Tax-Exempt Status	480
§ 18.3	Voluntary Employees' Beneficiary Associations	480
§ 18.4	Supplemental Unemployment Benefit Trusts	485
§ 18.5	Black Lung Benefits Trusts	486
§ 18.6	Retirement Plan Trust Funds	488
§ 18.7	Other Benefit Funds	489
<b>19</b>	<b>Other Categories of Tax-Exempt Organizations</b>	<b>491</b>
§ 19.1	Instrumentalities of United States	492
§ 19.2	Title-Holding Corporations	493
	(a) Single-Parent Organizations	493
	(b) Multiple-Parent Organizations	497
§ 19.3	Local Associations of Employees	498
§ 19.4	Fraternal Organizations	500
	(a) Fraternal Beneficiary Societies	500
	(b) Domestic Fraternal Societies	502
§ 19.5	Benevolent or Mutual Organizations	504
	(a) Local Life Insurance Associations	504
	(b) Mutual Organizations	505
§ 19.6	Cemetery Companies	509
§ 19.7	Credit Unions	512
§ 19.8	Mutual Reserve Funds	513
§ 19.9	Insurance Companies and Associations	514
§ 19.10	Crop Operations Finance Corporations	515
§ 19.11	Veterans' Organizations	516
	(a) General Rules	516
	(b) Pre-1880 Organizations	517
§ 19.12	Farmers' Cooperatives	517
§ 19.13	Shipowners' Protection and Indemnity Associations	524
§ 19.14	Homeowners' Associations	524
§ 19.15	High-Risk Individuals' Health Care Coverage Organizations	527
§ 19.16	Workers' Compensation Reinsurance Organizations	527
	(a) State-Sponsored Organizations	528
	(b) Certain Insurance Companies	528
§ 19.17	Railroad Retirement Investment Trust	528
§ 19.18	Qualified Health Insurance Issuers	528
§ 19.19	Qualified Tuition Programs	529
	(a) State-Sponsored Programs	530
	(b) Educational Institution-Sponsored Programs	531
	(c) Other Rules	531
§ 19.20	ABLE Programs	532
§ 19.21	Professional Sports Leagues	533
§ 19.22	Governmental and Quasi-Governmental Entities	534
	(a) Intergovernmental Immunity	534
	(b) Income Exclusion Rule	535

## CONTENTS

- (c) Integral Parts of States 537
- (d) State Instrumentalities 539
- (e) Related Considerations 540
- § 19.23 Native American Tribes 540
- § 19.24 Other Tax-Exempt Organizations 541
- § 19.25 Nonexempt Membership Organizations 542

### PART FIVE: PRINCIPAL EXEMPT ORGANIZATION LAWS

#### 20 Private Inurement and Private Benefit

547

- § 20.1 Concept of *Private Inurement* 549
- § 20.2 Definition of *Net Earnings* 551
- § 20.3 Definition of *Insider* 552
- § 20.4 Compensation Issues 556
  - (a) Meaning of *Compensation* 556
  - (b) Determining Reasonableness of Compensation 557
  - (c) Percentage-Based Compensation 561
  - (d) Multiple Payors 562
  - (e) Role of Board 562
  - (f) Board Member Compensation 562
  - (g) Actuality of Services Rendered 563
  - (h) Illegal Payments 563
- § 20.5 Other Forms of Private Inurement 564
  - (a) Rental Arrangements 564
  - (b) Lending Arrangements 565
  - (c) Sales of Assets 565
  - (d) Capital Improvements 566
  - (e) Equity Distributions 566
  - (f) Assumptions of Liability 567
  - (g) Employee Benefits 567
  - (h) Tax Avoidance Schemes 568
  - (i) Services Rendered 569
  - (j) Business Referral Operations 572
  - (k) Provision of Goods or Refreshments 572
  - (l) Retained Interests 573
  - (m) Embezzlements 573
- § 20.6 *Per Se* Private Inurement 574
- § 20.7 Incidental Private Inurement 575
- § 20.8 Private Inurement and Social Welfare Organizations 577
- § 20.9 Private Inurement and Business Leagues 578
- § 20.10 Private Inurement and Social Clubs 580
- § 20.11 Private Inurement and Other Categories of Exempt Organizations 581
- § 20.12 Private Benefit Doctrine 582
  - (a) General Rules 582
  - (b) Incidental Private Benefit 584
  - (c) Joint Venture Law 587
  - (d) Perspective 591

<b>21</b>	<b>Intermediate Sanctions</b>	<b>595</b>
§ 21.1	Concept of <i>Intermediate Sanctions</i>	596
§ 21.2	Tax-Exempt Organizations Involved	596
§ 21.3	Disqualified Persons	597
§ 21.4	Transactions Involved	600
	(a) General Rules	600
	(b) Revenue-Sharing Arrangements	602
	(c) Automatic Excess Benefit Transactions in General	602
	(d) Automatic Excess Benefit Transactions and Supporting Organizations	603
	(e) Automatic Excess Benefit Transactions and Donor-Advised Funds	604
	(f) Scholarships and Similar Grants	604
§ 21.5	Controlled Entities	605
§ 21.6	Intermediaries	606
§ 21.7	<i>For the Use of</i> Transactions	606
§ 21.8	Initial Contract Exception	610
§ 21.9	Rebuttable Presumption of Reasonableness	610
	(a) Independent Body	611
	(b) Appropriate Data	611
	(c) Adequate Documentation	612
§ 21.10	Excise Tax Regime	613
§ 21.11	Correction Requirement	614
§ 21.12	Definitions	616
	(a) Participation	616
	(b) Knowing	616
	(c) Reliance on Professional Advice	617
	(d) Willful	618
	(e) Occurrence	618
§ 21.13	Indemnification and Insurance	619
§ 21.14	Return for Payment of Excise Taxes	619
§ 21.15	Statute of Limitations	619
§ 21.16	Interrelationship with Private Inurement Doctrine	620
<b>22</b>	<b>Legislative Activities by Tax-Exempt Organizations</b>	<b>625</b>
§ 22.1	Legislative Activities Law for Exempt Organizations— Introduction	626
§ 22.2	Meaning of <i>Legislation</i>	626
	(a) Substantial Part Test	626
	(b) Expenditure Test	627
	(c) Associations' Dues Deductibility Test	627
§ 22.3	Lobbying by Charitable Organizations	628
	(a) Legislative History	628
	(b) Concept of <i>Lobbying</i>	629
	(c) Substantial Part Test	629
	(i) Action Organizations	629
	(ii) Allowable Lobbying	630

## CONTENTS

	(iii) Exceptions	631
	(iv) Reporting Rules	632
(d)	Expenditure Test	633
	(i) Influencing Legislation	633
	(ii) Allocation Rules	635
	(iii) Allowable Lobbying	635
	(iv) Non-Earmarked Grants	638
	(v) Exceptions	638
	(vi) Election of Test	639
	(vii) Evaluating Election	639
	(viii) Affiliated Organizations	640
	(ix) Record-Keeping Requirements	641
	(x) Reporting Rules	642
§ 22.4	Lobbying Expenditures and Tax Sanctions	642
§ 22.5	Legislative Activities of Social Welfare Organizations	642
§ 22.6	Legislative Activities of Business Leagues	643
	(a) Business Expense Deduction Disallowance Rules	644
	(b) Flow-Through Rules	647
	(c) Proxy Tax Rules	647
§ 22.7	Legislative Activities of Other Tax-Exempt Organizations	649
§ 22.8	Internet Communications	649
§ 22.9	Constitutional Law Framework	651
<b>23</b>	<b>Political Campaign Activities by Tax-Exempt Organizations</b>	<b>657</b>
§ 23.1	Political Campaign Activities by Charitable Organizations—Introduction	658
§ 23.2	Prohibition on Charitable Organizations	658
	(a) Scope of the Proscription	658
	(b) <i>Participation or Intervention</i>	659
	(i) Terminology	660
	(ii) Political Campaign Intervention	660
	(iii) Ascertaining Intervention	660
	(iv) Summary of Law	661
	(v) Candidate Appearances	664
	(vi) Individual Participation	665
	(c) Voter Education Activities	666
	(d) Requirement of <i>Candidate</i>	669
	(e) Requirement of <i>Campaign</i>	669
	(f) Requirement of <i>Public Office</i>	669
	(g) Activist Organizations	670
§ 23.3	Political Campaign Expenditures and Tax Sanctions	674
§ 23.4	Taxation of Political Expenditures	676
§ 23.5	Political Activities of Social Welfare Organizations	677
	(a) Allowable Campaign Activity	678
	(b) Political Campaign Activities	679
	(c) Political Activities	680
§ 23.6	Political Activities by Labor Organizations	680
§ 23.7	Political Activities by Business Leagues	680

## CONTENTS

- § 23.8 Political Activities by Other Exempt Organizations 681
- § 23.9 Advocacy Communications 681
- § 23.10 Internet Communications 682

### **24 Unrelated Business: Basic Rules**

**685**

- § 24.1 Introduction to Unrelated Business Rules 686
- § 24.2 Definition of *Trade or Business* 689
  - (a) General Principles 689
  - (b) Requirement of Profit Motive 690
  - (c) Competition 692
  - (d) Commerciality 693
  - (e) Charging of Fees 693
  - (f) Fragmentation Rule 695
  - (g) Nonbusiness Activities 696
  - (h) Real Estate Development Activities 698
  - (i) Occasional Sales 700
  - (j) Concept of *Investment Plus* 700
- § 24.3 Definition of *Regularly Carried On* 702
  - (a) General Principles 702
  - (b) Determining Regularity 703
  - (c) Fundraising and Similar Activities 704
  - (d) Preparatory Time 704
- § 24.4 Definition of *Substantially Related* 705
  - (a) General Principles 706
  - (b) Size and Extent Test 707
  - (c) Same State Rule 708
  - (d) Dual Use Rule 709
  - (e) Exploitation Rule 711
  - (f) Related Business Activities 711
  - (g) Unrelated Business Activities 713
- § 24.5 Contemporary Applications of Unrelated Business Rules 715
  - (a) Educational Institutions 715
  - (b) Health Care Organizations 718
    - (i) Various Related Businesses 719
    - (ii) Sales of Pharmaceuticals 719
    - (iii) Testing Services 720
    - (iv) Fitness Centers 721
    - (v) Physical Rehabilitation Programs 722
    - (vi) Administrative Services 723
    - (vii) Other Health Care Activities 723
  - (c) Museums 724
  - (d) Social Welfare Organizations 726
  - (e) Business Leagues 726
    - (i) Services to Members 726
    - (ii) Insurance Programs 728
    - (iii) Associate Member Dues 729
    - (iv) Other Association Business Activities 730

## CONTENTS

- (f) Labor and Agricultural Organizations 731
- (g) Credit Unions 732
- (h) Advertising 732
  - (i) Concept of *Advertising* 733
  - (ii) General Rules 733
  - (iii) Concept of Related Advertising 736
- (i) Fundraising 737
  - (i) Fundraising as Unrelated Business 738
  - (ii) Affinity Card Programs 739
  - (iii) Sales of Mailing Lists 739
  - (iv) Application of Exceptions 740
  - (v) Tax Planning Consulting 741
- (j) Travel Tour Activities 742
- (k) Provision of Services 743
- (l) Sales of Merchandise 746
- (m) Share-Crop Leasing 747
- (n) Retirement Plan Reversions 748
- (o) Internet Communications 749
- (p) Debt Management Plan Services 751
- (q) Other Organizations' Exempt Functions 751
- § 24.6 Corporate Sponsorships 752
- § 24.7 Partnership Rules 755
- § 24.8 Commercial-Type Insurance 756
- § 24.9 Unrelated Debt-Financed Income 757
  - (a) General Principles 757
  - (b) Debt-Financed Property 757
  - (c) Acquisition Indebtedness 759
  - (d) Exempt Function borrowing 762
- § 24.10 Tax Structure 763
- § 24.11 Deduction Rules 763

## **25 Unrelated Business: Modifications, Exceptions, and Special Rules**

767

- § 25.1 Modifications 767
  - (a) Passive Income in General 768
  - (b) Dividends 768
  - (c) Interest 769
  - (d) Securities Lending Income 769
  - (e) Certain Consideration 769
  - (f) Annuities 769
  - (g) Royalties 770
  - (h) Rent 771
    - (i) General Rules 771
    - (ii) Passive Rent Test 772
    - (iii) Related Rental Activities 773
  - (i) Other Investment Income 773

## CONTENTS

- (j) Capital Gains 774
- (k) Loan Commitment Fees 775
- (l) Research Income 775
- (m) Electric Companies' Member Income 776
- (n) Foreign Source Income 776
- (o) Brownfield Sites Gain 777
- (p) Religious Order Rule 777
- (q) Charitable Deduction 778
- (r) Specific Deduction 778
- (s) Net Operating Losses 779
- § 25.2 Exceptions 779
  - (a) Volunteer-Conducted Businesses 780
  - (b) Convenience Businesses 781
  - (c) Sales of Gift Items 782
  - (d) Businesses of Employees' Associations 782
  - (e) Entertainment Activities 783
  - (f) Trade Shows 783
  - (g) Hospital Services 786
  - (h) Gambling 786
  - (i) Pole Rentals 787
  - (j) Low-Cost Articles 787
  - (k) Mailing Lists 787
  - (l) Associate Member Dues 788
  - (m) Small Business Corporation's Rules 788
- § 25.3 Special Rules 789

## PART SIX: ACQUISITION AND MAINTENANCE OF TAX EXEMPTION

### 26 Exemption Recognition and Notice Processes

795

- § 26.1 Recognition Application Procedure 796
  - (a) General Procedures 798
    - (i) Required Information 798
    - (ii) Other Procedural Elements 801
    - (iii) Preparation of Application 802
  - (b) *Substantially Completed* Application 802
  - (c) Issuance of Determinations and Rulings 804
  - (d) User Fees 805
  - (e) General Application Form 805
  - (f) Penalties for Perjury 810
  - (g) Interactive Form 1023 810
  - (h) Streamlined Application 811
    - (i) Overview 811
    - (ii) Exceptions 811
  - (i) Impact of Tax Refunds 812
  - (j) Applications Processing Controversy 813



## CONTENTS

§ 26.2	Requirements for Charitable Organizations	815
	(a) General Rules	815
	(b) Exceptions	816
	(c) Limited Liability Companies	817
§ 26.3	Nonprivate Foundation Status	818
	(a) Notice Requirement	818
	(b) Rules for New Publicly Supported Charities	819
§ 26.4	Requirements for Certain Credit Counseling Organizations	819
§ 26.5	Requirements for Certain Employee Benefit Organizations	820
§ 26.6	Requirements for Certain Prepaid Tuition Plans	820
§ 26.7	Requirements for Certain Health Insurance Issuers	820
§ 26.8	Requirement for ABLE Programs	821
§ 26.9	Rules for Other Organizations	821
§ 26.10	Group Exemption Rules	822
§ 26.11	Suspension of Tax Exemption	826
§ 26.12	Notice Requirements for Political Organizations	827
§ 26.13	Integral Part Doctrine	828
	(a) Affiliated Organizations	828
	(b) Divisions	831
§ 26.14	Forfeiture of Tax Exemption	832
§ 26.15	Constitutional Law Aspects of Process	834
<b>27</b>	<b>Administrative and Litigation Procedures</b>	<b>835</b>
§ 27.1	Administrative Procedures Where Recognition Denied	835
§ 27.2	Revocation or Modification of Tax-Exempt Status: Administrative Procedures	837
§ 27.3	Retroactive Revocation of Tax-Exempt Status	838
§ 27.4	Tax Consequences of Retroactive Revocation of Exempt Status of Public Charities	841
	(a) Tax Treatments: Corporations	842
	(b) Tax Treatments: Individuals	845
§ 27.5	Statute of Limitations Matters	846
§ 27.6	Revocation of Tax-Exempt Status: Litigation Procedures	847
	(a) General Rules	848
	(b) Declaratory Judgment Rules	851
	(i) General Requirements	852
	(ii) Exhaustion of Administrative Remedies	856
	(iii) Deductibility of Contributions	857
	(iv) Administrative Record	858
	(c) Other Approaches	860
§ 27.7	IRS Examination Procedures and Practices	861
	(a) General IRS Exempt Organizations Audit Procedures and Practices	861
	(i) General Procedures	862
	(ii) Types of Examinations	863
	(iii) Controversy	865
	(iv) Coping with Examination	865

## CONTENTS

- (b) IRS Exempt Organizations Examination Guidelines 866
- (c) Church Audits 867
- § 27.8 Compliance Checks 872
- § 27.9 Fast-Track Case Settlement Program 873
- § 27.10 IRS Disclosure to State Officials 874

### **28 Operational Requirements**

877

- § 28.1 Changes in Operations or Form 878
  - (a) Changes in Operations 879
  - (b) Changes in Form 879
- § 28.2 Annual Reporting Rules 881
  - (a) Overview of Annual Information Returns 882
    - (i) Form 990 882
    - (ii) Form 990-EZ 883
    - (iii) Form 990-PF 883
    - (iv) Filing Dates 884
    - (v) Penalties 885
    - (vi) Assessments 886
    - (vii) Miscellaneous 887
  - (b) Exceptions to Reporting Requirements 887
    - (i) Churches and Other Religious Organizations 888
    - (ii) Small Organizations 888
    - (iii) Other Exempted Organizations 889
  - (c) Limited Liability Companies 891
  - (d) Group Returns 891
- § 28.3 Annual Information Return 892
  - (a) Part I (Summary) 892
  - (b) Part III 892
  - (c) Part IV 892
  - (d) Part V 892
  - (e) Part VI 893
  - (f) Part VII 893
  - (g) Parts VIII–XI 893
  - (h) Schedule A 893
  - (i) Schedule B 894
  - (j) Schedule C 894
  - (k) Schedule D 894
  - (l) Schedule E 894
  - (m) Schedule F 894
  - (n) Schedule G 895
  - (o) Schedule H 895
  - (p) Schedule I 895
  - (q) Schedule J 896
  - (r) Schedule K 896
  - (s) Schedule L 896
  - (t) Schedule M 896
  - (u) Schedule N 897
  - (v) Schedule O 897

## CONTENTS

- (w) Schedule R 897
- (x) Uncertain Tax Positions 897
- (y) Preparer Tax Identification Numbers 899
- § 28.4 Notification Requirement 900
- § 28.5 ABLE Program Reports 901
- § 28.6 Filing Requirements and Tax-Exempt Status 901
- § 28.7 Charitable Organizations Listing Reliance Rules 902
- § 28.8 Reporting by Political Organizations 904
  - (a) General Rules 904
  - (b) Filing Dates 905
- § 28.9 Electronic Filing Rules 906
  - (a) Modernized e-File System 906
  - (b) Mandatory Electronic Filing 906
  - (c) Waivers 907
- § 28.10 Unrelated Business Income Tax Returns 908
- § 28.11 IRS Document Disclosure Rules 909
  - (a) Federal Tax Law Disclosure Requirements 909
    - (i) General Rules 909
    - (ii) Exempt Organizations Documents 911
  - (b) Freedom of Information Act 913
- § 28.12 Document Disclosure Obligations of Exempt Organizations 914
  - (a) General Rules 914
  - (b) Rules as to Inspection 915
  - (c) Rules as to Copies 915
  - (d) Failure to Comply 916
  - (e) Widely Available Exception 917
  - (f) Harassment Campaign Exception 917
  - (g) Penalties 918
  - (h) Political Organizations 918
- § 28.13 Information or Services Disclosure 919
- § 28.14 Fundraising Disclosure 919
- § 28.15 Insurance Activities 921
  - (a) General Rules 921
  - (b) Commercial-Type Insurance Rules 922
  - (c) Charitable Split-Dollar Insurance Plans 925
- § 28.16 Feeder Organizations 926
- § 28.17 Tax-Exempt Entity Leasing Rules 930
  - (a) Introduction 930
  - (b) Summary of Rules 931
  - (c) Definition of *Tax-Exempt Entity* 931
  - (d) Definition of *Related Entity* 932
  - (e) Recovery Periods 932
  - (f) Definition of *Tax-Exempt Use Property* 932
  - (g) Partnership Arrangements 934
  - (h) Interrelationship with Certain Tax Shelter Rules 936
- § 28.18 Tax-Exempt Organizations and Tax Shelters 936
  - (a) General Concept of *Tax Shelter* 937
  - (b) Judicial Doctrines Used to Combat Tax Shelters 938

## CONTENTS

- (c) Tax Shelter Tax Penalties 938
- (d) Reportable Transactions 938
- (e) Tax Shelters in Exempt Organizations Context 939
- (f) Excise Tax Penalties 939
- § 28.19 International Grantmaking Requirements 942
  - (a) Charitable Organizations Generally 942
  - (b) Private Foundations 943
  - (c) Treasury Anti-Terrorist Financing Guidelines 943
- § 28.20 Record-Keeping Requirements 945

## PART SEVEN: INTERORGANIZATIONAL STRUCTURES AND OPERATIONAL FORMS

### **29 Tax-Exempt Organizations and Exempt Subsidiaries 949**

- § 29.1 Subsidiaries Basics 949
- § 29.2 Charitable Organizations as Subsidiaries 951
  - (a) Subsidiaries of Social Welfare Organizations 952
  - (b) Subsidiaries of Business Leagues 952
  - (c) Subsidiaries of Other Noncharitable Exempt Organizations 954
  - (d) Subsidiaries of Domestic Charitable Organizations 955
  - (e) Subsidiaries of Foreign Charitable Organizations 956
- § 29.3 Tax-Exempt Subsidiaries of Charitable Organizations 959
- § 29.4 Other Combinations of Tax-Exempt Organizations 960
- § 29.5 Contributions and Other Payments 961
- § 29.6 Revenue from Tax-Exempt Subsidiary 963

### **30 Tax-Exempt Organizations and For-Profit Subsidiaries 965**

- § 30.1 For-Profit Subsidiaries in General 966
  - (a) Establishing For-Profit Subsidiary 966
  - (b) Choice of Form 967
  - (c) Control Element 968
- § 30.2 Potential of Attribution to Parent 969
- § 30.3 Financial Considerations 974
  - (a) Capitalization 974
  - (b) Compensation 975
  - (c) Sharing of Resources 975
- § 30.4 Asset Accumulations 976
- § 30.5 Subsidiaries in Partnerships 977
- § 30.6 Effect of For-Profit Subsidiaries on Public Charity Status 978
  - (a) Publicly Supported Organizations 978
  - (b) Supporting Organizations 978
- § 30.7 Revenue from For-Profit Subsidiary 979
  - (a) Income Flows to Parent 979
  - (b) Tax Treatment of Income from Subsidiary 980
  - (c) Tax Treatment of Revenue Received by Taxable Subsidiary 982
  - (d) Temporary Rule 982
- § 30.8 Liquidations 983

## CONTENTS

<b>31 Tax-Exempt Organizations and Joint Ventures</b>	<b>987</b>
§ 31.1 Partnerships and Joint Ventures Basics 987	
(a) Partnerships 988	
(b) Joint Ventures 991	
(c) Law-Imposed Joint Ventures 993	
§ 31.2 Public Charities as General Partners 994	
(a) Evolution of Law 995	
(b) Current State of Law 998	
(i) General Rules 998	
(ii) Health Care Institutions 1000	
§ 31.3 Whole-Entity Joint Ventures 1002	
(a) Overview of Law 1002	
(b) IRS Guidance 1003	
(i) Fact Situation 1 1003	
(ii) Fact Situation 2 1004	
(iii) Summary of Guidance 1005	
(iv) Subsequent Case Law 1007	
§ 31.4 Ancillary Joint Ventures 1009	
§ 31.5 Low-Income Housing Ventures 1011	
§ 31.6 Information Reporting 1014	
§ 31.7 Alternatives to Partnerships 1015	
<b>32 Tax-Exempt Organizations: Other Operations and Restructuring</b>	<b>1017</b>
§ 32.1 Organizational Considerations 1017	
(a) Form 1017	
(b) Governing Boards 1018	
(c) Control 1021	
(d) Attribution Considerations 1022	
§ 32.2 Operational Considerations 1023	
(a) Expenses 1023	
(b) Gifts and Grants 1025	
§ 32.3 Mergers 1025	
§ 32.4 Reorganizations 1027	
§ 32.5 Limited Liability Company Law Basics 1029	
§ 32.6 Multiple-Member Limited Liability Companies 1029	
§ 32.7 Single-Member Limited Liability Companies 1031	
§ 32.8 Choice of Entity Considerations 1035	
§ 32.9 Conversion from Exempt to Nonexempt Status 1035	
(a) State Law 1036	
(b) Federal Tax Law 1037	
§ 32.10 Conversion from Nonexempt to Exempt Status 1043	
(a) State Law 1043	
(b) Federal Tax Law 1043	
(c) Gain or Loss Recognition 1046	

CONTENTS

**PART EIGHT: APPENDIXES**

- A. Sources of Tax-Exempt Organizations Law 1051
- B. Internal Revenue Code Sections 1067
- C. 75 Categories of Tax-Exempt Organizations 1081

**Index**

**1085**

<http://www.pbookshop.com>