

Federal Tax Update February 12, 2013

EO FY 2012 Workplan: Some Highlights

Legislative Implementation:

- Auto-Revocation for Non-Filers
- Requirements for Tax-Exempt Hospitals
- Section 501(c)(29) Organizations
 - Proposed and Temporary Regulations
 - Revenue Procedure 2012-11
- Accountable Care Organizations
- Notice 2011-20

Compliance: Using the Form 990

- Section 501(c)(4), (5), and (6) organizations self-declaring exemption
 - Questionnaires to be sent to these organizations to assess compliance
- Political activity
 - Enforcement of rules relating to political campaigns and campaign expenditures
 - Compliance with Section 527(f)
- 990-T and UBIT
 - Comparison of Form 990 UBI revenue but no Form 990-T filed
- Governance
 - Use Form 990 as a tool to compare governance practices and tax compliance

EO will support four IRS focus areas:

- Impact of recent legislation
- EO is developing new publications describing the special rules that apply to foreign charities and domestic charities that conduct activities abroad
- Medical resident FICA processing of refund claims
- National Research Program – study of employment tax returns

Collaboration with external stakeholders:

- Academic Institutions Initiative
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FY 2012 Projects:

- Colleges and Universities
- Disaster Relief Communications
- Group Rulings
- Mortgage Foreclosure Assistance
- State-Sponsored Workers Compensation Organizations (501(c)(27))
- Private Foundations
- EO Services and Assistance

IRS Initiatives

Treasury-IRS 2011-2012 Priority Guidance

Exempt Organizations:

- Final regulations to implement Form 990 revisions and to modify the public support test (issued September 2011)
- Guidance updating grantor and contributor reliance criteria under Sec. 170b and 509
- Guidance under Sec. 501(c)(29) relating to tax exemption for certain qualified nonprofit health insurance issuers
 - Proposed and Temporary Regulations and Rev. Proc. 2012-11 issued 2/7/12
- Guidance under Sec. 501(r) and 6033 on additional requirements for charitable hospitals as added by the ACA
 - Notice 2011-52 released 7/7/11
 - Proposed Regulations 1.501(r) issued 6/22/12
- Final supporting organizations regulations – proposed regulations were published 9/24/09
- Additional guidance on Sec. 509(a)(3) supporting organizations
- Update to Rev. Proc. 92-94 (equivalency determinations for grants by private foundations to foreign grantees)
- Proposed Regulations under Sec. 4944 providing additional examples of program related investments published on 4/19/09
- Guidance on the PPA amendments to Sec 4943 regarding excess business holdings rules
- Guidance under Sec. 4944 on program-related investments
- Regulations regarding Sec. 4966 excise taxes on donor advised funds and fund management.
- Regulations under Sec. 6033 regarding group returns
- Final Regulations under Sec. 7611 relating to church tax inquiries and examinations – proposed regulations published 8/5/09

Colleges & Universities Compliance Initiative

- September 2008, 400 questionnaires were sent to public and private four-year colleges and universities inquiring about
 - Unrelated business income
 - Endowments
 - Executive compensation
- Interim report was published May 2010
 - Scope included 344 institutions, 177 private and 167 public
 - 159 small, 94 medium, and 91 large
- Final report issued ??? focusing on:
 - UBI
 - Trade or Business
 - Cost Allocation

IRS Compliance Project: IRS Section 402(b) Plans

- 300 higher education institutions will be selected Purpose is to determine if organizations are complying with the 403(b) universal availability (UA) nondiscrimination rules and the new written plan document requirements
- The UA rule provides that if any employee is permitted to make elective salary deferrals to a 403(b) plan, then all employees, with limited exceptions, must be provided the same opportunity
- IRS will audit every automatically revoked 403(b) plan

Other IRS Activities

- Governance
 - Lois Lerner, Director Exempt Organizations, provides comments on the continued importance of governance in charitable organizations
 - Research on the intersection between good governance and tax compliance
 - http://www.irs.gov/pub/irs-tege/georgetown_04192011.pdf
- Form 990, Schedule H desk audits
 - Affordable Care Act included a provision for IRS to audit community benefit activities of hospitals once every three years
 - Began in March of 2011
- IRS audits large private foundations
- Medical Resident FICA
 - In January 2012, the IRS began sending Letter 4878 which provides taxpayers additional information regarding the IRS' processing of Medical Resident FICA refund claims
 - Claims allowance/disallowance report
 - Information regarding interest payments
- IRS updates procedures for issuing new Individual Taxpayer Identification Numbers
 - IRS will only issue ITINs when the W-7 submitted includes original or certified documents
- IRC Sec. 512(b)(13)
 - Pension Protection Act provided for an exclusion from UBI for interest, annuities, rents and royalties received from a controlled entity if:
 - The payments received were less than FMV
 - There was a written, binding contract in place as of August 17, 2006
 - This exception had been extended through 12/31/2011 but was not renewed

FBAR

- Offshore voluntary disclosure program was reopened on January 9, 2012
 - Participants must file all original and amended tax returns and include payment for back-taxes and interest for up to 8 years as well as pay any penalties (up to 27.5% of the highest aggregate balance in foreign bank accounts/entities)

- New procedures effective 9/1/12 categorizes filers into low and high compliance risk
- FBAR due date for individuals eligible for the extensions for reporting signature authority extended to June 30, 2013

Revocation of Tax-Exempt Status

- Section 6033(j) of the IRC automatically revokes exemption of any organizations that does not satisfy its filing requirement for three consecutive years
- IRS will notify organizations that failed to file an annual information return for three years and will publish a list of revoked organizations
 - Notice 2011-44 provides for reinstatement of tax-exempt status for organizations that have lost tax-exempt status (not retroactive unless IRS receives evidence of reasonable cause)

Revocation of Tax-Exempt Status: Small Filers

- Filing Relief Program
 - Requires small tax-exempt organizations with gross receipts of \$25,000 or less to file Form 990-N once every three years (\$50,000 for tax years ending on or after December 31, 2010)
 - IRS will notify organizations that failed to file an annual information return for three years and will publish a list of revoked organizations
 - Notice 2011-43 provides for automatic retroactive reinstatement of tax-exempt status for certain small organizations that have lost tax-exempt status
 - Application for reinstatement of tax-exempt status must be filed by December 31, 2012

New Form 8940 for Miscellaneous Determination Requests

- IRS released Form 8940 in August 2011 for tax-exempt organizations to use to request certain determinations, other than initial exemption) including the following:
 - Exemption from Form 990 filing requirements
 - Advance determination that a potential grant or contribution is an unusual grant, excluded from the calculation of public support
 - Change in (or initial determination of) Type of a IRC Section 509(a)(3) supporting organization
 - A user fee must accompany most requests (see Revenue Procedure 2012-8)

Treasury Issues Report on Supporting Organizations and Donor Advised Funds

- Treasury considered and Report Found:
 - Whether the existing deduction rules for contributions to DAFs and SOs are appropriate
 - Report found that because contributions to DAF sponsoring organizations and SOs, like contributions to other public

charities, are generally to organizations the donor doesn't control, the deduction rules are appropriate

- Whether DAFs should be subject to a distribution requirement
 - Report found that when compared to private foundations, the mean payout for Aggregate DAFs in 2006 appears to be high; therefore Treasury is not recommending a distribution requirement for DAFs
- Whether an advisory role in the investment or distribution of donated funds is consistent with a completed gift
 - Report found that high approval rates for grant recommendations are not in itself indicative of donors' exerting excessive control over donated assets
- Whether the issues described in questions 1-3 are also issues with respect to other forms of charities or charitable donations
 - Report did not note any issues

Voluntary Worker Classification Program

- Voluntary Classification Settlement Program (Ann. 2011-64)
 - Applies to taxpayers who are currently treating workers as independent contractors or other nonemployees
 - Taxpayers must agree to prospectively treat workers as employees
 - Must have consistently treated workers as nonemployees and filed Forms 1099 for the previous three years
 - Does not apply to taxpayers who are under IRS exam
 - Partial relief from federal employment taxes
 - FAQs posted on IRS website: [http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Voluntary-Classification-Settlement-Program-\(VCSP\)-Frequently-Asked-Questions](http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Voluntary-Classification-Settlement-Program-(VCSP)-Frequently-Asked-Questions)

Legislative Update

- Patient Protection and Affordable Care Act includes many provisions impacting tax-exempt organizations
 - Medicare tax increase of 0.9% on employee wages in excess of \$200,000 effective January 1, 2013
 - Beginning in 2011, W-2 statements issued must include the aggregate cost of employer sponsored health benefits
- Originally included expanded Form 1099 reporting requirements are expanded to include payments made to corporations. However, this provision was repealed in April 2011
- Individual mandate upheld as a tax by the Supreme Court
- Veterans Work Opportunity Tax Credit Available

- Incentives for employers that hire unemployed veterans as a credit against payroll taxes
- Applies to qualified veterans who began work after November 21, 2011 and before January 1, 2013
- Payroll Tax Holiday
 - 2% reduction effective for 2011 is extended through 2012

Regulatory Update

- Final Regulations on 3% withholding requirement released May 6, 2011
 - After 12/31/2012, federal, state, and other units of government with annual payments for goods and services of \$100MM or more must withhold income tax of 3% of the total payment for goods and services, with limited exceptions.
 - Repealed November 16, 2011
- Proposed Regulations Section 48.4191 address Medical Device Excise Tax
 - 2.3% excise tax on sales of certain medical devices by the manufacturer, producer, or importer of the device
 - Certain retail and other exemptions are clarified
 - Leverages the existing manufacturing excise tax regulations
- Tangible Property Temporary Regulations address a broad range of capitalization and deduction issues for expenditures related to tangible property:
 - Acquiring tangible personal property
 - Producing tangible personal property
 - Improving tangible personal property
 - Disposing of tangible personal property
 - Consuming materials and supplies in operations
- Proposed Regulations under Section 501(r) provides guidance to hospitals exempt under IRC Section 501(c)(3) and operate state licensed hospital facilities:
 - Information that a hospital facility must include in its financial assistance policy and emergency medical care policy, including publicizing the policies
 - How a hospital facility determines the maximum amounts it can charge FAP-eligible individuals for emergency and other medically necessary care (IRC Section 501(r)(5))
 - Describes the actions that are considered "extraordinary collection actions" and the "reasonable efforts" a hospital facility must make to determine FAP-eligibility before engaging in such actions (IRC Section 501(r)(6))

Employer Provided Cell Phones: Notice 2011-72

- Notice 2011-72 provides that when an employer provides an employee with a cell phone primarily for noncompensatory business purposes, the business and personal use of the cell phone is not taxable to the employee.
- IRS will not require recordkeeping of business use in order to receive this tax-free treatment.

- Because cell phones are no longer listed property, the notice states that the heightened substantiation requirements that apply to listed property no longer apply to cell phones for taxable years beginning after December 31, 2009.

Contributions to SMLLC

- Notice 2012-52
 - Provided long-awaited guidance that contributions of assets to a SMLLC owned by a charitable organization would be treated as a charitable contribution
 - Applies to assets such as real estate and other property commonly housed in a SMLLC
 - Contribution treated as if it was made directly to the charity itself

Other Rulings of Note

- PLR 201123045
 - Health club operated by an exempt hospital offered memberships to employees and the public on sliding scale membership rate was found to constitute a charitable activity
- Program Manager Technical Assistance memorandum 2011-004
 - IRS cautions that payments made by booster club member to a booster club in excess of the benefits received could be considered a private benefit; revocation of exempt status
- CCA 2011447001
 - Loan repayments made to participants in a state program designed to attract health care professionals to underserved areas of the state are excludable from gross income under IRC Sec. 108(f)(4)
- PLR 201147035
 - Rental income derived from recreational facility furthered the organization's exempt purpose and was not considered debt-financed since the unrelated rentals constituted less than 15% of the total use of the facility
- PLR 2012203019
 - IRS revoked an organization's tax-exempt status because it dissolved in one state and subsequently reincorporated in another (see also Revenue Ruling 67-390)
- PLR 201219026
 - Fraternity foundation loses its tax-exempt status prospectively on the grounds that the foundation had correctly described its activities to the IRS as part of its application for tax-exempt status and the IRS incorrectly granted the foundation tax-exempt status under IRC Sec. 501(c)(3)
- Program Manager Technical Assistance memorandum 2012-01
 - State program to reimburse tuition (or other incentive compensation) of health care professionals does not qualify under IRC Sec. 108(f)(4) student loan exclusion because the payments are neither loan repayments nor forgiveness programs

- PLR 201220005
 - Organization that provides support to public schools found to be an instrumentality of the state
 - IRS applied the six-factor test (Rev. Rul. 57-128)
- PLR 201228029
 - Management agreement between a governmental entity and third party did not meet the safe harbors of Rev Proc 97-13 but did not result in private business use

Certain Cases of Note

- *Ocean Pines Association, Inc v. Comm.* (Tax Ct. 2010)
 - Income generated by a beach club and parking lots held to be UB I to an exempt homeowner's association
 - 4th Circuit US Court of Appeals affirmed this decision on March 2, 2012
- *Asmark Institute, Inc. v. Comm.* (TC Ct. 2012)
 - Entity did not qualify for exemption due to the commerciality doctrine (provided consulting services for a fee), and engaged in the same activities as its for-profit predecessor organization.

2011 Form 990: Significant Changes

- Core Form Appendix F: Disregarded Entities and Joint Ventures
 - Updated to require and organization to use Schedule K-1 information from joint ventures when reporting income, expense, and balance sheet items
 - Optional for 2011
- Schedule J, Compensation
 - Part I, Line 3 regarding methods of determining compensation of CEO or executive director may not be checked if used by a related organization
- Schedule H, Hospitals
 - Revised to include information required by health care reform