

RETHINK: Applying for Non Profit Exempt Status

The question from my client was: What if you are trying to apply for exempt status and the second question on Form 1023-EZ Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code

ANSWER: If you answer "Yes" to any of the worksheet questions, you are not eligible to apply for exemption under section 501(c)(3) using Form 1023-EZ. You must apply for exempt status with IRS on Form 1023. Question number 2 asks if your gross receipts are more than \$50,000 in any of the three preceding years and you are stating that your answer would be yes; therefore, you must file Form 1023 or the long form. You just are not eligible to file the short form or Form 1023-EZ.

You can find the form and instructions at this link www.irs.gov then go to the Forms & Pubs tab. I have listed a few of the publications below that might be of interest to you. You may also want to download or read "Life Cycle of an Exempt Organization" at the following section of the IRS website at this link <http://www.irs.gov/Charities-&-Non-Profits> to help you understand which type of organization that you may also be able to qualify for. Not all donations are 100% deductible to the person giving the deduction and it depends on the type of not-for-profit you want to apply for. You will also have to apply for California status and fill out tax returns for both Federal and State. Tax preparation is not cheap.

The most important things to know about a not-for-profit organization are:

1. That you have to comply with IRS rules
2. That bookkeeping is done differently than a for profit organization
3. All records must be made available for public inspection

You must publish a notice annually (in a newspaper) when the books and records are complete stating an address where they are available for public inspection.

Note: There are not very many people that are qualified to do not-for-profit bookkeeping.

The biggest problem is thinking that YOU will be paid out of the not-for-profit organization because in actuality the principal organizers and board of directors are prohibited from being paid. The term for it is self-dealing and it is illegal. You must also remember that when you close down a not-for-profit organization the only way to get rid of any and all assets is to give them to another not-for-profit organization and your plan must be stated when you apply for the exempt status. You will have no say in the organization because it must be run by a board of directors. Remember, IRS will hold the board of directors personally responsible for any and all problems or activities connected with the organization.

Most people think that they will get money from grants. Reality is that it is very difficult to get a grant. You usually have to hire a CPA to perform an audit before and after you receive the grant and it is very costly. Most audits start at \$5,000. In order to remain exempt, you must pass a "public support" test, which is reported for an ongoing 5 year periods at a time.

You will not be granted a not-for-profit status unless your organization's purpose is clearly defined and you will lose that status if your money does not go for the intended purpose you stated on your application.

IRS provides educational workshops and seminars for exempt organizations. There are also online courses and webcasts available. Not-for-profit organizations are very time consuming and you really need to be sure you want to undertake such a project before you begin. You will need lots of support to make sure you are complying with the rules and regulations.

The following publications are available to you for further information.

Publication 517, Social Security and Other Information for Members of the Clergy and Religious Workers
Publication 526, Charitable Contributions

Publication 557, Tax-Exempt Status for Your Organization

Publication 598, Tax on Unrelated Business Income of Exempt Organizations

Publication 1771, Charitable Contributions—Substantiation and Disclosure Requirements

Publication 1828, Tax Guide for Churches and Religious Organizations

Publication 3079, Tax-Exempt Organizations and Gaming

Publication 3833, Disaster Relief: Providing Assistance Through Charitable Organizations

Publication 4220, Applying for 501(c)(3) Tax-Exempt Status

Publication 4221, Compliance Guide for 501(c)(3) Tax Exempt Organizations

For help in completing Form 1023 or general questions relating to an exempt organization, call Exempt Organization Customer Account Services toll free at 1-877-829-5500. Submitting an application does not guarantee exemption status will be granted by IRS.

I hope that my information has helped you make an informed decision. Form 1023 is 31 pages long and can require up to an additional 8 schedules. It requires that you provide the articles of organization, profit and loss statements for current and the three prior years, establish a budget for two years beyond the current tax year and there are plenty of questions about how you are currently doing business. The fee is \$850 to send in your application and it would help if you had knowledge of bookkeeping.

Many times clients have answered enough questions to prove to themselves that it would be least costly to be a for profit company, first starting as a self-employed person choosing a fictitious name to do business under, ie a DBA you would register with the county. It would be written as your name, DBA fictitious name. An example would be Caran Ebert, dba Holistic Tax Advice. As you grow, there is a certain amount of liability that would warrant changing into an LLC (limited liability company) but I always advise my client to start off small with the least amount of cost so that you have little to lose when you are learning how to be in business for yourself.

By
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