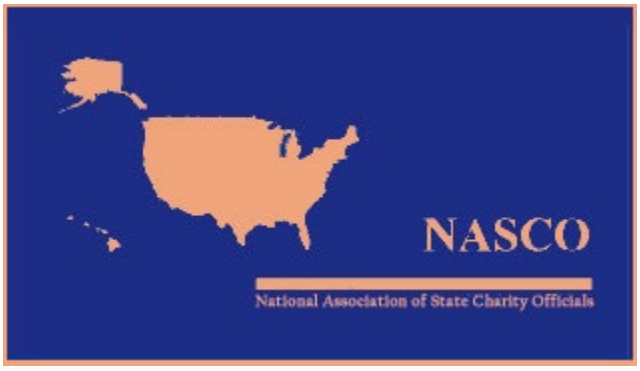

November 27, 2023

Submitted via email **pra.comments@irs.gov**

Andres Garcia
Internal Revenue Service, Room 6526
1111 Constitution Avenue NW
Washington, D.C. 20224

RE: NASCO Comments regarding OMB Control No. 1545-0047

Dear Andres Garcia:

The Board of Directors of the National Association of State Charity Officials ("NASCO") respectfully submits this letter in response to the Internal Revenue Service ("IRS") Notice and Request for Comments on Tax-Exempt Organization Forms.[1] As described more fully below, we recommend that the IRS: (1) revisit the use of the abbreviated Form 1023-EZ; and (2) continue to address the timely availability of Forms 990.

NASCO is an association of state charity officials, including state Attorneys General offices, Secretaries of State offices, and other state offices charged with preventing the misuse of charitable assets, ensuring that trustees of charitable trusts fulfill their fiduciary duties, and enabling donors to make informed choices about which charitable causes to support. State charity regulators have been working together toward shared goals through NASCO for over 40 years. One of those key goals is to uphold the integrity of the charitable sector through ensuring transparency and accountability.

In order to do so, state regulators frequently use and rely on the valuable information contained in the IRS tax-exempt organization forms including, but not limited to, the IRS Forms 990, 990-EZ, 990-PF, and 1023. We know that donors and the public also use and view these forms as educational tools to inform their decision-making.

[1] This letter reflects the views of the NASCO board of directors. It does not necessarily reflect the views of any individual Attorney General, Secretary of State, or other state official.

Based on our experience, we respectfully recommend the following with respect to IRS Tax-Exempt Organization Forms:

(1) Revisit the Use of the Abbreviated Form 1023-EZ

We emphasize here, again, the need for the IRS to revisit the abbreviated Form 1023-EZ.[2] Below we highlight not just the important role of the longer Form 1023 in promoting good governance at newly formed charitable organizations, but also how recent state enforcement actions demonstrate that the use of the 1023-EZ enables fraudulent activity that harms the public.

Especially in light of these recent enforcement actions, the NASCO Board continues to believe that the longer Form 1023 serves important governmental and societal purposes. It effectively operates as both a gate keeper and educational tool for newly formed charitable organizations. In particular, the Form 1023 is often the first exposure a newly formed organization has to the financial, operations, fundraising, and investment responsibilities of newly established charitable nonprofits and their officers and directors.

The longer Form 1023 also provides information that can be useful for state regulators in our compliance and enforcement efforts. For example (and without limitation), representations regarding compensation and other financial arrangements with officers, directors, and key employees are useful when investigating related party transactions, and disclosures regarding prior history can be used to identify repeat bad actors.

We continue to be concerned that the ability to use the Form 1023-EZ in place of the Form 1023 has made it easier for "scam" charities to obtain 501(c)(3) status.[3] For example, because an organization applying for exemption using Form 1023-EZ does not submit a copy of its articles of organization with its application, the IRS does not have access to the governing documents necessary to ensure such organization is, in fact, organized and operated for charitable purposes or that its assets are permanently dedicated to a charitable purpose. We believe it would best serve the public's interest in charities to reinstate the important 1023 requirements that serve as an educational tool for new charities.[4]

Use of the Form 1023-EZ in combination with streamlined retroactive reinstatement procedures under section 4 of Rev. Proc. 2014-11, allows entities to obtain and maintain tax-exempt status as charities for years without disclosing critical information to federal and state regulators and the

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[2] Attached hereto as Exhibit 1 are the following: November 28, 2022 letter from the NASCO Board to the IRS; May 28, 2021 letter from the NASCO Board to the IRS; April 6, 2018 letter from former NASCO President Hugh Jones to The Honorable Lynn Jenkins and The Honorable John Lewis; May 23, 2014 letter from then-NASCO President Alissa Hecht Gardenswartz to the IRS; April 30, 2014 letter from then-NASCO President Alissa Hecht Gardenswartz to the IRS.

[3] *See* Treasury Inspector General for Tax Administration "More Information is Needed to Make Informed Decisions on Streamlined Applications for Tax Exemption," Report No. 2023-10-001, pp.11-14 (October 3, 2022).

[4] *See* May 23, 2014, letter from the then-NASCO President Alissa Hecht Gardenswartz offering several suggested additions to the 1023-EZ, included in Exhibit 1.

public, including information to support their eligibility for tax-exempt status as a charity. For example, an organization using the Form 1023-EZ that falsely attests to the contents of its governing documents such as its charitable purpose as well as its eligibility to file the Form 990-N *e-Postcard* can potentially perpetuate its fraud for six years—three years before automatic revocation under section 6033(j), and three additional years after retroactive reinstatement by following the procedures in Rev. Proc. 2014-11—before it must file a long form annual return that contains any meaningful information about its finances or charitable activities.

Recent public examples highlight how entities can improperly take advantage of the Form 1023-EZ with serious consequences for donors, public funds, and confidence in the charitable sector. In October 2023, the Minnesota Attorney General's Office filed nearly two dozen civil lawsuits against nonprofit corporations that were created or revived by individuals indicted by the federal government for their alleged roles in a $250 million fraud scheme. Of 24 entities, which had a combined revenue of at least $46.5 million, 17 applied for and received recognition of section 501(c)(3) tax-exempt status using the Form 1023-EZ. Many of these entities were formed for the specific purpose of receiving hundreds of thousands of dollars in funds that were the ultimate subject of the federal prosecution, making them ineligible to file the Form 1023-EZ in the first place. Further, because the 1023-EZ process does not require applicants to submit copies of their governing documents, the IRS did not have the opportunity review such documents and ultimately deny exemption to the many entities whose articles of organization did not contain the appropriate purposes, dissolution, and other clauses required of 501(c)(3) tax-exempt entities.[5]

(2) Timely Availability of Forms 990

The NASCO board strongly supports the public availability of information nonprofits report through the Form 990 series and urges the IRS to address delays in the timely availability of these forms.

The Form 990 series is a critical tool for charity regulators, donors, grantors, and the public. For charity regulators, the Form 990 series not only helps ensure transparency and accountability, but also provides vital information for state investigations into potential fraud and misuse of charitable resources. For discerning donors, the Form 990 is an important source of information to support wise giving practices. For responsible grantors, the Form 990 can be an important tool to examine the financial health of potential grantees and ensure they are in compliance with regulatory obligations.

Lags in the availability of the critical data contained in the Form 990 adversely affect regulators, the public, and most importantly, the nonprofit. Because many NASCO member offices rely on the publicly available versions of Forms 990 submitted to the IRS rather than requiring submission of the Forms 990 to their state offices, it is critical that the availability of that data be timely. We

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[5]See October 18, 2023 Press Release from the Minnesota Attorney General's Office, *available at* https://www.ag.state.mn.us/Office/Communications/2023/10/18_FoodFraud.asp#:~:text=October%2018%2C%202023%20(SAINT%20PAUL,as%20fraudulent%20%E2%80%9Csites%E2%80%9D%20tasked%20to

are aware of and have observed significant lags in the amount of time between when charities submit Forms 990 to the IRS and when the IRS posts them. This creates an incomplete picture of a charitable organization when a NASCO office undertakes an investigation of a charity and can lead to confusion for potential charitable donors and others.

While we appreciate improvements to these data lags since the last time we wrote in 2022, we support additional IRS resources in order to meet goals of timely availability of Forms 990.

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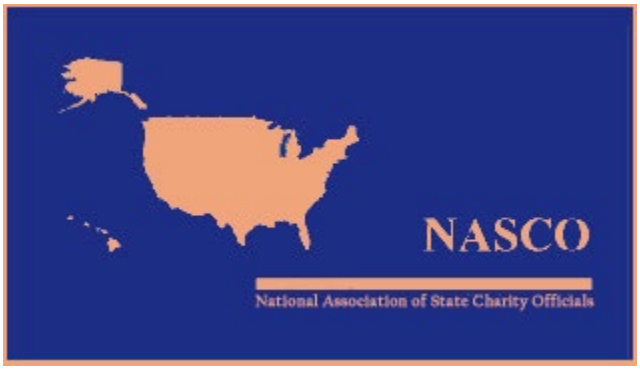
We extend our appreciation to the IRS for this opportunity to convey comments regarding its tax-exempt organization forms. We respectively urge you to consider the issues outlined above and detailed in the attached correspondence. Please feel free to reach out if you would like to discuss these matters.

Sincerely,

/s/ Leslie Friedlander

Leslie Friedlander
President, National Association of State Charities Officials (NASCO) on behalf of the NASCO Board of Directors

Exhibit 1
to November 27, 2023 Letter
from NASCO Board to IRS



November 28, 2022

Submitted via email **pra.comments@irs.gov**

Andres Garcia
Internal Revenue Service, Room 6526
1111 Constitution Avenue NW
Washington, D.C. 20224

RE: NASCO Comments regarding OMB Control No. 1545-0047

Dear Andres Garcia:

The Board of Directors of the National Association of State Charity Officials ("NASCO") respectfully submits this letter in response to the Internal Revenue Service ("IRS") Notice and Request for Comments on Tax-Exempt Organization Forms. As described more fully below, we recommend that the IRS: (1) address the timely availability of Forms 990 and (2) revisit the use of the abbreviated Form 1023-EZ.

NASCO is an association of state charity officials, including state Attorneys General offices, Secretaries of State offices, and other state offices charged with preventing the misuse of charitable assets, ensuring that trustees of charitable trusts fulfill their fiduciary duties, and enabling donors to make informed choices about which charitable causes to support.[1] State charity regulators have been working together toward shared goals through NASCO for over 40 years. One of those key goals is to uphold the integrity of the charitable sector through ensuring transparency and accountability.

In order to do so, state regulators frequently use and rely on the valuable information contained in the IRS tax-exempt organization forms, including but not limited to, the long form IRS Form 990 and 990-EZ, the IRS Form 990-PF, and the long form IRS Form 1023. We know that donors and the public also use and view these forms as educational tools to inform their decision-making.

[1] This letter reflects the views of the NASCO board of directors. It does not necessarily reflect the views of any individual Attorney General, Secretary of State, or other state official.

Based on our experience, we respectfully recommend the following with respect to IRS Tax-Exempt Organization Forms:

(1) Timely Availability of Forms 990

The NASCO board strongly supports the public availability of information nonprofits report through the Form 990 series and urges the IRS to address delays in the timely availability of these forms.

The Form 990 series is a critical tool for charity regulators, donors, grantors, and the public. For charity regulators, the Form 990 series not only helps ensure transparency and accountability, but also provides vital information for state investigations into potential fraud and misuse of charitable resources. For discerning donors, the Form 990 is an important source of information to support wise giving practices. For responsible grantors, the Form 990 can be an important tool to examine the financial health of potential grantees and ensure they are in compliance with regulatory obligations.

Lags in the availability of the critical data contained in the Form 990 adversely affect regulators, the public, and most importantly, the nonprofit. Because many NASCO member offices rely on the publicly available versions of Forms 990 submitted to the IRS rather than requiring submission of the Forms 990 to their state offices, it is critical that the availability of that data be timely. We are aware of and have observed significant lags in the amount of time between when charities submit Forms 990 to the IRS and when the IRS posts them. This creates an incomplete picture of a charitable organization when a NASCO office undertakes an investigation of a charity and can lead to confusion for potential charitable donors and others.

(2) Revisit the Use of the Abbreviated Form 1023-EZ

We reiterate our prior recommendation that the IRS revisit the abbreviated Form 1023-EZ, which certain organizations may file with the IRS to qualify for tax-exempt status under section 501(c)(3).[2] As described in several prior letters from NASCO, we believe that the longer Form 1023 serves important governmental and societal purposes, effectively serving as both a gate keeper and educational tool for newly formed organizations. In particular, the Form 1023 is often the first exposure a newly formed organization has to the financial, operations, fundraising and investment responsibilities of newly established nonprofits and their officers and directors.

The longer Form 1023 also provides information that can be useful for state regulators in our compliance and enforcement efforts. For example (and without limitation), representations regarding compensation and other financial arrangements with officers, directors, and key employees are useful when investigating related party transactions, and disclosures regarding prior

[2] *See* May 26, 2021, letter from NASCO Board to Treasury Department and IRS, attached hereto as Exhibit 1 and enclosing April 6, 2018 letter from former NASCO President Hugh Jones to The Honorable Lynn Jenkins and The Honorable John Lewis, which attached two 2014 letters from then-NASCO President Alissa Hecht Gardenswartz.

history can be used to identify repeat bad actors. We also continue to be concerned that the ability to use the Form 1023-EZ in place of the Form 1023 has made it easier for "scam" charities to obtain 501(c)(3) status.[3] While we understand the desire to simplify 1023 requirements for certain organizations, we believe it would best serve the public's interest in nonprofit organizations to reinstate certain requirements for those organizations that serve as the educational tool that many of those organizations need – whether that reinstatement is accomplished through the elimination or revision of the 1023-EZ.[4]

We extend our appreciation to the IRS for this opportunity to convey comments regarding its tax-exempt organization forms. We respectively urge you to consider the issues outlined above and detailed in the attached correspondence. Please feel free to reach out if you would like to discuss these matters.

Sincerely,

/s/ Leslie Friedlander

Leslie Friedlander
President, National Association of State Charities Officials (NASCO) on behalf of the NASCO Board of Directors

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[3] *See* Treasury Inspector General for Tax Administration "More Information is Needed to Make Informed Decisions on Streamlined Applications for Tax Exemption," Report No. 2023-10-001, pp.11-14 (October 3, 2022).

[4] *See* May 23, 2014 letter from the then-NASCO President Alissa Hecht Gardenswartz offering several suggested additions to the 1023-EZ, included in Exhibit 1.

May 28, 2021

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2021-28) Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

RE: NASCO Recommendations for 2021-2022 Priority Guidance Plan Notice 2021-28

To Whom It May Concern:

The Board of Directors of the National Association of State Charities Officials ("NASCO") respectfully submits this letter in response to the Notice 2021-28 invitation to submit recommendations for items to be included on the 2021-2022 Priority Guidance Plan. As described more fully below, we recommend that the Department of Treasury ("Treasury Department") and the Internal Revenue Service ("IRS") include the following issues in the 2021-2022 Priority Guidance Plan: (1) Revisit the Use of the Abbreviated Form 1023-EZ; (2) Reinstate Schedule B requirements for 501(c)(4) exempt organizations; and (3) Enhance IRS Information Sharing with State Charities Regulators.

NASCO is an association of state charities officials, including state Attorneys General offices, Secretaries of State offices, and other state offices charged with preventing the misuse of charitable assets, ensuring that trustees of charitable trusts fulfill their fiduciary duties, and enabling donors to make informed choices about which charitable causes to support.[1] NASCO regulators work toward the goal of upholding the integrity of the charitable sector through ensuring transparency and accountability. Based on our experience, we recognize the importance of the Treasury Department and the IRS addressing the following:

[1] This letter reflects the views of the NASCO board. It does not necessarily reflect the views of any individual Attorney General, Secretary of State, or other state official.

(1) Revisit the Use of the Abbreviated Form 1023EZ

We recommend revisiting the abbreviated Form 1023EZ, which certain organizations may file with the IRS to qualify for tax exempt status under section 501(c)(3). As described in several prior letters from NASCO,[2] we believe that the longer Form 1023 serves important governmental and societal purposes, effectively serving as both a gate keeper and educational tool for newly formed organizations. In particular, the Form 1023 is often the first exposure a newly formed organization has to the financial, operations, fundraising and investment responsibilities of newly established nonprofits and their officers and directors. Further, the longer Form 1023 provides information that can be useful for state regulators in our compliance and enforcement efforts. For example (and without limitation), representations regarding compensation are useful when investigating related party transactions, and disclosures regarding prior history can be used to identify repeat bad actors. We also continue to be concerned that the ability to use the Form 1023EZ in place of the Form 1023 has made it easier for "scam" charities to obtain 501(c)(3) status. Please see the attached May 23, 2014 letter from the then-NASCO President offering a number of suggested additions to the 1023-EZ, including, among other items, requiring submission of articles and by-laws, provisions for distribution of assets upon dissolution, and detailed information regarding compensation and other financial information with officers, directors and key employees. While we understand the desire to simplify 1023 requirements for certain organizations, we believe it would best serve the public's interest in nonprofit organizations to reinstate certain requirements for those organizations that serve as the educational tool that many of those organizations need – whether that reinstatement is accomplished through the elimination or revision of the 1023-EZ.[3]

(2) Reinstate Schedule B Filing Requirements

We recommend withdrawing the IRS guidance published in 2020 at 85 FR 31959, and reinstating the requirement that 501(c)(4) organizations submit the "names and addresses" of substantial contributors through Form 990, Schedule B, as access to that information is critical to the IRS's enforcement of the Code and state enforcement of complementary state laws regulating certain charitable 501(c)(4) organizations.[4] As we had predicted in our December 5, 2019

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[2] *See* April 6, 2018 Letter from Former NASCO President Hugh Jones to The Honorable Lynn Jenkins and The Honorable John Lewis, which attached two 2014 letters from then-NASCO President Alissa Hecht Gardenswartz, all of which are attached hereto as Attachment A.

[3] In response to prior reviews (e.g., from the Taxpayer Advocate Service) suggesting that a significant percentage of 1023-EZ approved applicants were not in fact eligible for 1023-EZ, the IRS has articulated an intent to conduct audits of approved 1023-EZ applicants, and has discussed its "pre-determination reviews" of a sample of 1023-EZ filers (about 3%). We would appreciate the opportunity to discuss with you the results of these audits and pre-determination reviews.

[4] Many state charities regulators oversee 501(c)(4) organizations, which may be public charities under state law if their primary purpose is not political advocacy. *See* MODEL PROTECTION OF CHARITABLE ASSETS (2011) at 13, *available at* https://www.uniformlaws.org/committees/community-home?CommunityKey=ad5a0384-9d0e-41c0-a00f-4c3794962946 ("Nor does the Act apply to organizations whose primary purpose is political advocacy.

comment letter to the IRS on REG-102508-16, by relieving 501(c)(4) organizations of the obligation to submit Schedule B, the IRS signaled that it abdicated enforcement with respect to those organizations and provided increased opportunity to abuse 501(c)(4) status. We also expect that should the Schedule B requirement not be reinstated promptly, the enforcement burden shouldered by state charities regulators will substantially increase.[5] As a result, the IRS and state charities regulators have been deprived of the important tool we once had to question 501(c)(4) organizations about, among other things, potential undue influence of disqualified persons under 4958. We have also been hindered in investigating illicit "dark money" spent by 501(c)(4) organizations to influence elections, excess benefit transactions, sham charities, and fundraising fraud. For more details regarding why we believe it is vital for the IRS to collect Schedule Bs from 501(c)(4) organizations, please see the attached December 5, 2019 letter NASCO wrote to the IRS.[6]

(3) Enhance IRS Information Sharing with State Charities Regulators

We believe that enhancing the ability of our agencies to share information would support collective goals, which include promoting transparency and accountability in the charitable sector and ensuring against private inurement, waste, fraud, conflicts of interest, excess compensation and other abusive practices. While the Pension Protection Act of 2006 (the "PPA") permitted some level of information sharing, to-date we believe the applicable requirements have largely proven unworkable for state charities regulators. Until the PPA can be amended to ease some burdens, such as subjecting state charity officials to criminal penalty provisions of IRC Sec. 7213, we urge the Treasury Department and IRS to revisit the information sharing procedures, consider how new technologies may facilitate secure sharing of information, and renew IRS attempts to facilitate the states' ability to use shared information. For more information on state charities regulator concerns and challenges with respect to current IRS information sharing policies, please see the attached 2011 letter from 43 Attorneys General[7] and the 2013 Report of Recommendations from the IRS Advisory Committee on Tax Exempt and Government Entities.[8]

Workmen's Circle Educational Center of Springfield v. Board of Assessors, 314 Mass. 616, 619, 51 N.E.2d 313, 316 (1943)").

[5] While California's regulatory compliance requirement that charities confidentially submit Schedule Bs as part of annual filing requirements is before the Supreme Court in *Americans for Prosperity Foundation v. Bonta*, No. 19-251 and *Thomas More Law Center v. Bonta*, No. 19-255, this letter speaks to the separate issue of the IRS's longstanding requirement that 501(c)(4) organizations submit Schedule Bs to the IRS, which was rolled back in 2020.

[6] *See* December 5, 2019 Letter from NASCO to IRS regarding IRS REG-102508-16, attached hereto as Attachment B.

[7] *See* October 28, 2011 Letter from 43 Attorneys General to The Honorable Max Baucus and The Honorable Orrin Hatch, attached hereto as Attachment C.

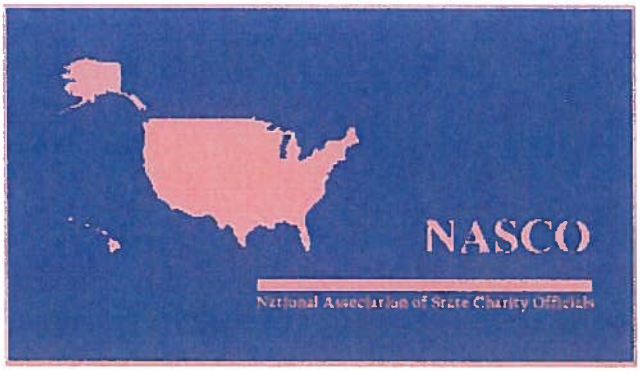
[8] *See* Publication 4344 (Rev. 6-2013), Advisory Committee on Tax Exempt and Government Entities, "Exempt Organizations: Leveraging Limited IRS Resources in the Tax Administration of Small Tax-Exempt Organizations," p. 11-16, available at https://www.irs.gov/pub/irs-tege/tege_act_rpt_12.pdf.

We appreciate the opportunity to convey recommendations for items to be included on the 2021-2022 Priority Guidance Plan. We respectively urge you to consider the issues outlined above and detailed in the attached correspondence for inclusion in the Plan. Please feel free to reach out if you would like to discuss.

Sincerely,

Yael Fuchs /s/

Yael Fuchs
President, National Association of State Charities Officials (NASCO)



April 6, 2018

Via Email
irsreform@mail.house.gov

Chairman Lynn Jenkins
Ranking Member John Lewis
House Ways and Means Oversight Subcommittee
United States House of Representatives
United States Congress
Washington D.C.

Dear Chairman Jenkins and Ranking Member Lewis

Re: Discussion Draft: The Taxpayer First Act, H.R. No. ____ (March 26, 2018)

I am writing on behalf of nine other former presidents[1] of the National Association of State Charity Officials (NASCO). I held the office of president of NASCO during the years 2007-2008 and remain very active in its programs, committees, activities and initiatives. NASCO is an association made up of state Attorneys General and Secretaries of State, and other agencies having state oversight of charitable organizations, and their fundraising and governance practices. These include nonprofit corporations of many kinds, and charitable trusts.

We are writing to strongly suggest that the Taxpayer First Act include provisions that require the Internal Revenue Service (IRS) to revisit the use of the abbreviated Form 1023EZ, which currently allows certain organizations to qualify for tax exempt status under section 501(c)(3) for charitable, educational and religious purposes. We join with the comments submitted separately by the National Council of Nonprofits[2]

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[1] Former NASCO presidents Terry M. Knowles (NH) Chris Cash and Alissa Hecht Gardenswartz (Colo.), Karin Kunstler Goldman (NY), Elizabeth Grant (OR), Belinda Johns (Calif.), Janet Kleinfelter (TN), Mark Pacella (PA), Therese Harris (IL) and others have authorized me to communicate that they join with me, and I am virtually certain that many others would too, time permitting. I am a Senior Deputy Attorney General, with the Tax & Charities Division of the Hawaii Attorney General's office.

[2] The National Council of Nonprofits is an advocate for an effective, robust, ethical and transparent charitable sector and the Council and NASCO frequently collaborate together in our work to promote

which has stood firmly with NASCO on this issue to protect the public trust in the nonprofit sector. I share many of the National Council of Nonprofits' concerns about the Form 1023EZ. I and other former NASCO presidents believe that the IRS should resume using the much more robust Form 1023, although we understand, and in fact support efforts to simplify the prior form, yet make an effective tool for qualifying and educating newly formed charitable organizations.

NASCO is on record in opposition to the use of form 1023EZ and that opposition remains so today. Attached are copies of former NASCO president Alissa Hecht Gardenswartz's April 30 and May 23, 2014 letters that explain in considerable depth, why a longer Form 1023 served important governmental and societal purposes and should not be truncated to the point that it becomes ineffective in performing a gate keeping and educational function for newly formed organizations. The Form 1023 is often the first exposure a newly formed organization has to the myriad of financial, operational, fundraising and investment issues faced by a newly established nonprofit organization. As stated in the 2012 Report of the Tax Advisory Committee (ACT):

> Form 1023 serves an important educational purpose for applying organizations . . .and forces the applying organization to think somewhat deeply about its activities, finances, and management . . . [The Form] also signals to the organization that it is entering into a (probably unfamiliar) comprehensive regulatory scheme, and working through the questions on the form provides the organization with a great deal of information about compliance with this regime.

The concerns of NASCO, the National Council of Nonprofits and the ACT are echoed by those of the Taxpayer Advocate Service. The Taxpayer Advocate Service recently found that exempt status was erroneously granted to up to 42 percent of applicants using the 1023EZ[3]. I, and my colleagues strongly agree with the Taxpayer Advocate Service's statement that Form 1023EZ's "new procedures do not require applicants to submit their articles of incorporation or bylaws to ensure they are properly organized and have adopted the appropriate charitable purpose clause as well as protections against misuse of funds."

Aside from the fact that Form 1023EZ has allowed simply "unqualified" organizations to qualify for tax exempt status, I am concerned that it has been an invitation to possibly "sham" charities to apply for and obtain tax exempt status and use that special tax status as a tool to convince donors to contribute money given the apparent IRS "stamp of approval." In at least one egregious example, a for-profit entity applied for and was granted tax exempt status using Form 1023EZ[4]. There may be others like this example.

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public confidence in the nonprofit sector. Because the Council represents the regulated sector, NASCO listens carefully to the Council's suggestions on a wide range of issues.

[3] https://taxpayeradvocate.irs.gov/reports/2017-annual-report-to-congress/MSP-1023-EZ

[4] Seehttps://www5.sos.state.oh.us/ords/f?p=100:7:::NO:7:P7_CHARTER_NUM:4019295

In Hawaii, nonprofit organizations may use "form" articles of incorporation to simplify the incorporation process, but those "form" articles do not satisfy the section 501(c)(3)'s requirement that a charity's organizational documents limit their activities to one or more exempt purposes, and require that the assets be distributed to other qualifying tax exempt charities. As a result we have seen several Hawaii nonprofit organizations that obtained tax exempt status using Form 1023EZ, representing their organizational documents met stringent IRS requirements, when in fact they did not. I am sure other states that provide "form" articles of incorporation have experienced similar situations. When such organizations' articles of incorporation do not confine the organizations activities to charitable purposes, it invites abuse and makes it very difficult for state charity regulators to protect and safeguard what should be charitable assets.

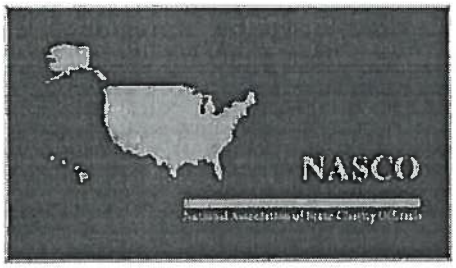
We recommend that this is a suitable time to require the IRS to re-examine use of the truncated IRS Form 1023EZ. The IRS should give full consideration to the suggestions made by the National Council of Nonprofits, and in the 2012 Final Report of the Act. Based on the foregoing, we again recommend that the Taxpayer First Act include provisions which require the IRS to revisit the use of the abbreviated Form 1023EZ to ensure that it performs an effective gate keeping and educational function that it once did.

Thank you for listening to our concerns.

Respectfully submitted,

Hugh R. Jones
NASCO President 2007-2008

Attachments (2)



May 23, 2014

Via Electronic Mail
Ms. Sunita Lough
Commissioner, Tax Exempt and Government Entities Division
Ms. Tamera Ripperda
Director, Exempt Organizations
United States Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

RE: Proposed Internal Revenue Service Form 1023-EZ, OMB Number 1545-0056

Dear Sunita and Tammy:

I am writing to follow up on our May 6 conversation addressing NASCO's concerns about the IRS's implementation of the 1023-EZ. As we mentioned during the call and in our April 30 comments to the OMB and Treasury, NASCO does not oppose the idea of a more streamlined "core form" 1023. We are concerned, however, that the most recent draft of the 1023-EZ fails to obtain the minimum amount of information necessary to identify organizations that should not be approved or should be monitored closely in back-end compliance. Accordingly, we strongly recommend that the following information be requested in the 1023-EZ:

- Provision of articles and by-laws as well as Part III of the current 1023 that requires organizations to state where their purpose is in

organizing documents and greater specifics (beyond mere attestation) on provisions for distribution of assets upon dissolution.

- Detailed information regarding compensation and other financial arrangements with officers, directors, and key employees of the organization. Information provided here could be a source for red flags (for example, the organization will be all volunteer, the executive director's salary will be 70% of total revenue, organization will receive goods/services from an organization associated with an officer or director, etc.) – the vast majority of questions in the current Part V should be required.
- Some financial reporting should be required – at minimum revenues and expenses.
- Part VI is also a source for potential concerns and serves a valuable educational purpose for the many well-meaning organizations that do not realize they cannot form a tax-exempt charity to raise funds for a single individual.
- Organizational history, i.e., whether the organization is a successor organization or has submitted an application more than 27 months after formation.
- Part VIII (specific activities) could be somewhat limited as proposed in the current 1023-EZ, but should also include questions on fundraising activities and contracts, whether the organization is affiliated with a governmental entity, and planned activities with other organizations (joint ventures, loans, etc.).

Other items that could be included on a 1023 application that would be helpful to state regulators and the IRS alike would be questions regarding relationships to previously revoked (c)(3)s, criminal backgrounds of officers and directors, and/or affiliations of the applicant charity with other charities that have been subject to legal action. Even if bad actors are inclined to not answer these questions truthfully, the sheer fact that the questions are asked may deter some people from using tax-exempt status for nefarious purposes, and untruthful responses could provide a basis for state enforcement actions for fraud or impermissible private benefit.

NASCO very much appreciates the opportunity to provide the IRS with feedback regarding its rollout of the 1023-EZ, and we hope that you seriously

consider our suggested modifications to the current form. We look forward to continuing to work with you as you implement these changes.

Sincerely,

Alissa Hecht Gardenswartz
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cc: Ruth Madrigal, Attorney Advisor
Office of Tax Policy, U.S. Dept. of the Treasury (via email)

April 30, 2014

Office of Information and Regulatory Affairs
Office of Management and Budget
Attention: Desk Officer for Treasury
New Executive Office Building, Room 10235
Washington, DC 20503
Via email at OIRA_Submission@OMB.EOP.gov

Treasury PRA Clearance Officer
1750 Pennsylvania Avenue NW, Suite 8140
Washington, DC 20220
Via email at PRA@treasury.gov

RE: Proposed Internal Revenue Service Form 1023-EZ, OMB Number 1545-0056

Thank you for the opportunity to comment on the proposed Form 1023-EZ as drafted on April 23, 2014. I am the current president of the National Association of State Charity Officials (NASCO) and write on behalf of NASCO to reiterate state charity regulator concerns regarding an abbreviated Form 1023 tax exempt application. A survey of state charities regulators conducted prior to the 2012 report of the Internal Revenue Service's Advisory Committee on Taxation (ACT) found that state regulators uniformly believed that collecting less information in the initial application for tax exemption on an assumption that an organization that begins small will remain small invites abuse and results in overall regulatory inefficiency. The ACT recommended against development of a Form 1023-EZ.

NASCO continues to support the ACT's recommendation against a Form 1023-EZ and the Committee's reasoning as stated in the 2012 ACT report:

> a. Rationale for Not Developing a Form 1023-EZ – One of our stated goals for the Form 1023 is that it be simple, and a shorter Form 1023 would almost certainly be simpler for small organizations. But we believe that the value of this increased simplicity would be outweighed by the loss of educational value to the applying organization and the loss of effectiveness to the IRS.
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> Before discussing the rationale for our recommendation regarding the Form 1023-EZ, we first address a consideration that was *not* a basis for our recommendation—that the Form 1023 should deter small organizations that are more likely to be formed without the necessary funding and infrastructure in place to survive long term from applying for recognition of exemption. We do not believe that the Form 1023 should be a barrier to exemption for these organizations and we frankly suspect that the current form, with its complexity, has that effect. We hold this view while fully acknowledging that there are sometimes beneficial effects when the form does act as a barrier. But as a policy matter, we believe that the Form 1023 should address the legal requirements for exemption in an effective, consistent, simple, and educational manner—nothing more, nothing less.
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> The primary reason we do not recommend the development of a Form 1023-EZ is because the Form 1023 serves an important educational purpose for applying organizations. Through its questions, the form forces the applying organization to think somewhat deeply about its activities, finances, and management. The form also signals to the organization that it is entering into a (probably unfamiliar) comprehensive regulatory regime, and working through the questions on the form provides the organization with a great deal of information about compliance with this regime. We agree with the many practitioners we spoke with who believe that the educational benefits of the Form 1023 are especially important for small organizations. And we do not believe that a significantly shorter Form 1023 could provide a comparable level of these benefits.
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> In addition, we think that it would be difficult to design a significantly shorter Form 1023-EZ that would still be effective from the IRS's perspective, i.e., that it would still provide the IRS with all the essential information it needs to a make a determination on a small organization's exempt status. While the current Form 1023 clearly

needs to be redesigned and streamlined, in the end many of the questions on the current form will still need to be asked (in some form or another) of all organizations, both large and small, although reformatting will reduce the need for smaller organizations to respond to certain questions. It should also be noted that many small exempt organizations will be Form 990-N (e-Postcard) filers. Hence, the Form 1023 will be the only opportunity for the IRS to receive any substantive information about such organizations. Thus, it is even more important that the Forms 1023 filed by small organizations request all the information the IRS needs because there will not be a "second chance" to obtain this information later from a (full) Form 990 or 990-EZ.

While there is certainly abuse in both large and small charities, some practitioners and state charity regulators we spoke with noted that some types of small charities are particularly susceptible to abuse. In their view, some small charities seemingly do little more than pay salaries to their founders and insiders. It may also be easier to embezzle from a small charity because it has few or no staff and financial controls are perhaps not as strong as they should be. Moreover, small organizations often lack sufficient reserves to withstand such losses of resources. All these considerations are relevant to the application process for small organizations. The information an organization provides on its Form 1023 can sometimes signal to the IRS a potential for possible abuse, and the IRS can then "flag" that organization for later follow-up. Our concern is that a shorter Form 1023-EZ may be less capable of providing these warning signals.

State charity regulators uniformly oppose a Form 1023-EZ, noting that such a form would make it easier for "scam" charities to obtain Section 501(c)(3) status. They also believe that there is no way at the outset to justify a rationale of exempting small charities from the Form 1023 filing burden, because all applicants, other than perhaps private foundations, begin their existence as small organizations. As one state charity regulator noted: "The application process should be the same for everyone -- no one knows how large and successful a particular organization or cause may be at its earliest beginnings, even if they pledge to 'stay small.'"

Another objection to a Form 1023-EZ for small organizations is the difficulty in determining an appropriate standard for what "small" should mean for this purpose. If, for example, annual gross receipts are used as the threshold requirement for using the shorter Form 1023-EZ,

> this could frustrate the rationale for having the shorter form. An organization's projected gross receipts on the Form 1023 could be substantially smaller than what it actually receives in its first few years. But because its projections were small, the organization would qualify to file the shorter Form 1023-EZ, and thus avoid providing the IRS, on a (full) Form 1023, with a more comprehensive view of this now "un-small" organization. More generally, if projected annual gross receipts were used as the threshold for the Form 1023-EZ, there would be a natural inclination for organizations to understate those projections.

2012 ACT Report of Recommendations. "Exempt Organizations: Form 1023-Updating It for the Future," pages 31-33, located at http://www.irs.gov/pub/irs-tege/tege_act_rpt11.pdf.

State charities regulators use the same vital information collected on Forms 1023 to ensure compliance with federal tax regulations to carry out our respective state regulatory duties to protect charitable assets from fraud and abuse, and to ensure that charitable assets are used for the purposes represented to the public. We believe that the Form 1023-EZ will increase opportunity for fraud and heighten the burden on state regulators to compensate for the reduced standards that will be required of the organization to meet federal tax exemption requirements. While we appreciate that the IRS will be committing more resources to back-end compliance examinations to address the potential for malfeasance, our concern is that the current 17% of all applicants for which the Form 1023-EZ would apply could grow exponentially if the process for obtaining tax-exempt status was significantly simplified. Both IRS and state charities regulator enforcement capabilities are already stretched thin. While use of the Form 1023-EZ may result in somewhat of a short-term reduced burden in processing applications, the long-term effect certainly will be a greatly increased burden on already overburdened state and federal regulators.

We submit that there are alternate and more effective ways to foster "accountability, transparency, and openness in Government and society" consistent with the spirit and purpose of the Paperwork Reduction Act. NASCO is taking a leadership role in trying to create substantive efficiencies for charitable organizations in meeting state and federal regulatory requirements. We are working with the Multistate Registration and Filing Project ("MFRP, Inc.") to develop a unified multistate charities registration website that will enable tax-exempt organizations to meet state regulatory registration requirements for every

state and, at the same time, file their annual Forms 990 at one convenient, easy to use website, without duplication of data entry. Making electronic filing uniform and convenient will result in significant cost savings for charities. It will significantly decrease processing time for the IRS and state regulators, making government more efficient. It will heighten transparency by enabling effective data sharing among federal and state regulators, legislators, and the general public. We believe that working together to achieve these efficiencies will ultimately alleviate burdens on charitable organizations and government more effectively than reducing the standard for acquiring tax exempt status by enabling some organizations to obtain tax exemption with an abbreviated Form 1023-EZ.

In conclusion, NASCO agrees that a reconsideration of the Form 1023 is appropriate in the context of reducing the burden on charities and the government, but believes the discussion should involve input from all stakeholders with an eye towards reduced burden overall and not just in the application process.

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