

November 10, 2024

Andres Garcia
Internal Revenue Service, Room 6526,
1111 Constitution Avenue NW
Washington, DC 20224

RE: Comments regarding Tax- Exempt Organization Forms
OMB Control No. 1545-0047

Dear Mr. Garcia:

On behalf of the networks of the National Council of Nonprofits (NCN), we submit the following comments in response to the invitation for public comment on proposed and/or continuing information collections concerning IRS forms and schedules used by tax-exempt organizations (OMB Control No. 1545-0047). NCN is the nation's largest network of nonprofits, with more than 25,000 organizational members. Our membership reflects the wide spectrum of nonprofit missions. Like the vast majority of charitable organizations, most are small to mid-sized entities. Ninety-seven percent of America's nonprofits have budgets under \$5 million; 92 percent have budgets less than \$1 million. In formulating these comments, we have relied on extensive communication with this network and feedback from multiple organizations representing subsector groups across the nonprofit sector.

Our comments will address four specific topics: (1) a renewed request to extend the review and comment process on the forms and schedules used by tax-exempt organizations for at least an additional 60 days; (2) improvements in the timeliness of public accessibility of Forms 990; (3) the need for revisions to specific provisions in Form 990 to better reflect the reporting of government revenue received by charitable organizations and to provide a clearer definition of the term "gross receipts;" and (4) a renewed call on the IRS to revoke the current Form 1023-EZ and seek stakeholder input for establishing a more appropriate process for determining the tax-exempt status of certain charitable entities.

1. IRS Regulatory Review of Exempt Organization Forms

On September 4, 2024, the IRS published the above-referenced request for comments on over 130 tax forms and schedules, as well as more than 140 other notices, revenue procedures, and Treasury Decisions impacting the financial and regulatory reporting requirements of tax-exempt

organizations. The request for comments asks whether the collection of information in these myriad forms, schedules, and other regulatory requirements is necessary for the proper performance of the functions of the IRS and whether the information has practical utility. It also seeks input on how to enhance the quality, utility, and clarity of the information needed to be collected and ways to minimize the burden of the collection of information on respondents. This annual review is of enormous interest to charitable organizations both due to the amount of the paperwork and reporting burden that this information imposes as well as because the charitable sector is virtually unanimous in its commitment to transparency and public awareness regarding all phases of its operations.

The National Council of Nonprofits remains concerned regarding the time constraints imposed by the comment period deadline. It is our belief that the regulated community has not been provided sufficient time to consider adequately and thoroughly the vast majority of the forms and other reporting requirements listed in Appendices A and B.

NCN recommends that the IRS reopen the regulatory review of exempt organization forms and extend the period of public comment for at least an additional 60 days.

2. More Timely Public Accessibility of Forms 990

The National Council of Nonprofits strongly believes in the importance of accessibility to the information available on Forms 990 in order to bolster public confidence in the operation of the charitable sector. We join with other national organizations, including the National Association of State Charity Officials (NASCO), in urging the IRS to address ways to minimize delays in the timely availability of these forms. Delay in the release of Forms 990 undermines public confidence in nonprofits. Delays also adversely impact governance, management, and fundraising operations, as well as overall compliance.

The Form 990 is a fundamental source of information for donors, grantors, regulators, and the general public. As NASCO has stated in prior submissions to the IRS on tax-exempt organization forms, “(f)or 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 to ensure they are in compliance with regulatory obligations... 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.”

NCN notes that the official IRS Advisory Council expressed concern in its 2022 report about the “lack of timely, consistent and complete Form 990 data provided by the IRS.” The report recommended that the IRS “identify operational improvements to ensure all available data is uploaded and available on the website in a timely and consistent manner and information posted is a complete representation of filed documents.”

NCN recommends that the IRS continue to take steps to improve release of Form 990 information. We support the calls on Congress to provide additional resources to the IRS in order to meet the overall goal of timely public accessibility.

3. Form 990: Reporting of Revenues Earned from Government Grants and Contract

The current Form 990 reporting of revenues earned from governments provides that government grants are reported at Part VIII, Line 1e – “Government grants (contributions).” Revenues earned pursuant to government contracts are reported under Line 2 – “(Program Service Revenue),” a category that can include Medicare and Medicaid reimbursements and payments for many other forms of receipts. We agree with the views expressed by the Aspen Institute and others (Comments to the Internal Revenue Service Taxpayer First Act Office, July 3, 2020) that Form 990 Part VIII “lacks sufficient clarity with respect to the reporting of government revenue, confusing users of the form, and likely resulting in inaccurate reporting.” As an interim step, we agree with their recommendations that Part VIII be modified to include a dedicated line for government reimbursements as part of line 2 and that the instructions to Form 990 clarify the distinction between revenue for “grants” that benefit the public versus payments under “contracts” that serve the needs of a governmental unit.

However, the concerns of the nonprofit community regarding reporting of revenues earned from governments go beyond administrative burdens and data collection addressed by others. The Form 990 and instructions seek to impose on nonprofits an other-worldly perspective on how nonprofits and governments actually operate in the real world.

Stated succinctly, nonprofits provide services on behalf of governments at all levels pursuant to written agreements. Governments rely on charitable nonprofits to provide vital services and pay the nonprofits for those services (although rarely at amounts that cover full costs). The government may view the agreements as grants or contracts but impose wildly disparate regulatory schemes to govern every aspect of their operations and documentation. As for nonprofits and the people and

communities they serve, it is a false and harmful distinction that undermines public confidence and promotes confusion rather than certainty. .

The problem with the current version of Form 990, Part VIII is that the line items 1e and 2 create and perpetuate the flawed narrative about nonprofit dependence on government funding. In reality, many of the government programs that are critical to the lives of the real people being served are performed by charitable nonprofits pursuant to government grants. The declaration of the payments as “contributions” trivializes the payments for the performance of essential services as mere gifts, as if they were voluntary and discretionary by government officials, or to use the outdated term, “alms.” The IRS must alter Form 990, Part VIII to delete “(contributions)” to remove this inaccurate qualifier.

Further, the distinction between grants and contracts may make sense to governments and accountants who deal with the differences on a daily basis. But the distinction is neither self-evident nor logical to nonprofits operating in the real world. At the federal level, government “grants” are governed by the [OMB Uniform Guidance](#); “contracts” are controlled by the [Federal Acquisition Regulations](#) (FAR). However, at the state and local levels, the written agreements pursuant to which nonprofits perform may be called “grants” or “contracts” or “grants contracts” (in at least one state). The simplistic breakdown of revenues earned from governments on the Form 990 breeds confusion and inconsistency. Even worse, the lack of greater clarity on the Form 990 promotes a damaging narrative that undermines public understanding, appreciation, and support. A more thorough review process is needed than contemplated in the present regulatory review process.

We note that many organizations in the nonprofit sector, even ones with years of experience, have difficulty distinguishing between grants and contracts that benefit the public versus those payments that serve the needs of a governmental unit. As far back as 2015, the [Advisory Committee on Tax Exempt and Government Entities \(ACT\) report](#) highlighted this problem, stating that it can result in “inconsistent reporting among seemingly comparable organizations,” as well as result in errors in the computation of some organizations’ public support test on Form 990 Schedule A. Given the significance of government revenue to the nonprofit sector, it is important that the IRS take steps to address this.

NCN recommends that the IRS commit to a more thorough analysis of Form 990, Part VIII with the goal of eliciting stakeholder input on how nonprofits can best report revenues earned pursuant to written agreements with governments at all levels. We reiterate that the networks of NCN will participate in such a review that promotes clarity, administrative ease, and public support.

4. Form 1023-EZ: Revoke and revise the current Form 1023-EZ

The IRS's primary obligation in reviewing applications for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code is to prevent ineligible organizations from attaining tax-exempt status and deterring bad actors from receiving and exploiting such status for personal gain. In 2014, the IRS radically streamlined its application and approval process for certain organizations seeking tax-exempt status under Section 501(c)(3). Generally, organizations with total assets up to \$250,000 and those expecting annual gross receipts up to \$50,000 are eligible to use Form 1023-EZ to apply for recognition of exempt status. As has been seen consistently in the ensuing decade, the result of this form and review procedure has been a disaster.

Numerous studies by unbiased government entities continue to find that the Form 1023-EZ as currently constituted fails to provide sufficient information to make informed decisions regarding the tax-exempt status of the applicant. For instance, a recent report from the [Treasury Inspector General for Tax Administration](#) (TIGTA) concludes, "(it) does not educate applicants about eligibility requirements for tax exemption." The IRS Taxpayer Advocate (TAS) has consistently found that virtually every entity that applies using the Form 1023-EZ receives tax-exempt status regardless of eligibility. The Taxpayer Advocate found erroneous approvals at rates of 37, 26, and 42 percent during 2015, 2016, and 2017, respectively. In a more recent report, TAS found that the rate increased to 46 percent despite revisions to the Form 1023-EZ that required additional information to assist the IRS in the review process. To bolster that conclusion, the TIGTA tested the form and process by submitting five fictitious organizations for tax-exempt status (including one with an "ineligible mission") for review. The IRS approved four of the applications and assigned the ineligible mission entity "for further review."

The TIGTA report notes that the TAS, NASCO, NCN, and the Advisory Committee on Tax Exempt and Government Entities all agree that a more streamlined process is needed for smaller organizations to apply for tax-exempt status; however, they also believe that the information currently required on Form 1023-EZ is insufficient to make such a determination. And as NASCO has noted, "(u)se 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 public, including information to support their eligibility for tax-exempt status as a charity."

The recommendations for improvements by the TAS and TIGTA address specific problems with the IRS processing of the form, yet do not get to the root cause of the problem – a form that fails to provide adequate information to ensure that only eligible organizations receive tax-exempt status

and the privilege of receiving tax-deductible donations. Such information should include, among other items, organizing documents, such as articles of incorporations and by-laws, provision for distribution of assets upon dissolution, and information regarding compensation of officers, board of directors, and key employees, and conflicts of interest.

NCN recommends that the IRS withdraw the current Form 1023-EZ and engage stakeholders – charitable regulators, nonprofit infrastructure organizations, funders, and tax-law practitioners – to develop a workable replacement for the form and process that will respect the IRS’s primary obligation of preventing ineligible organizations from attaining tax-exempt status and perhaps bad actors from receiving and exploiting such status for personal gain. Although we continue to respect the initial recommendation made by the National Taxpayer Advocate in 2011 on the need to develop a simplified method of applying for tax-exempt status, especially for smaller nonprofit organizations, we also believe the current Form 1023-EZ fails to provide the IRS with sufficient information to make an informed decision regarding qualification and fails to provide applicants with the necessary education regarding the requirements to apply for and maintain tax-exempt status.

We thank the IRS for conducting this regulatory review process and offer to assist in convening stakeholders and other interested parties to improve the regulatory reporting process in order to achieve greater transparency in the nonprofit sector.

Respectfully submitted,

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