

An hourglass graphic with a globe in the top bulb and another globe in the bottom bulb. The top bulb is dark blue, and the bottom bulb is light blue. The hourglass is light gray. The globe in the top bulb is dark blue, and the globe in the bottom bulb is light blue. The hourglass is centered on the page.

# WikiLeaks Document Release

<http://wikileaks.org/wiki/CRS-RS21892>

February 2, 2009

Congressional Research Service

Report RS21892

*Application Process for Seeking Section 501(c)(3) Tax  
Exempt Status*

Erika Lunder, American Law Division

December 12, 2007

**Abstract.** Charities and other entities seeking tax-exempt status as 501(c)(3) organizations generally must apply to the Internal Revenue Service. This report provides an overview of the application process.

WikiLeaks



## CRS Report for Congress

# Application Process for Seeking Section 501(c)(3) Tax-Exempt Status

Erika Lunder  
Legislative Attorney  
American Law Division

## Summary

Charities and other entities seeking tax-exempt status as § 501(c)(3) organizations generally must apply to the Internal Revenue Service. This report provides an overview of the application process.<sup>1</sup>

## Organizations Eligible for § 501(c)(3) Status

Nonprofit organizations that meet the criteria in Internal Revenue Code § 501(c)(3) qualify to be exempt from the federal income tax. The organization may be formed as a corporation, trust, or unincorporated association. Organizations are formed under state law, and the specific requirements vary by state. In general, a state's secretary of state will be able to provide information on how to form an organization.

In order to be eligible for tax-exempt status, the organization must meet the requirements in IRC § 501(c)(3). Section 501(c)(3) reads:

Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise

---

<sup>1</sup> Further information and the forms referenced in this report are available on the IRS website at [<http://www.irs.gov/charities/charitable/index.html>]. IRS Publication 557, *Tax-Exempt Status for Your Organization*, may be particularly useful. For general information on tax-exempt organizations, see CRS Report 96-264, *Frequently Asked Questions About Tax-Exempt Organizations*, by Erika Lunder.

attempting, to influence legislation (except as otherwise provided in subsection (h))<sup>2</sup>, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Thus, there are basically four requirements:

- The organization must be operated and organized for at least one of the listed exempt purposes. This means that no more than an insubstantial amount of the organization's activities may be for nonexempt purposes, and the organization must serve a public, as opposed to private, interest.<sup>3</sup>
- The organization's earnings may not be used to benefit any person having a personal and private interest in the organization's activities.
- No more than an insubstantial amount of the organization's activities may be lobbying.
- The organization may not participate in any political campaign activity.

Organizations that meet these qualifications must generally apply to the Internal Revenue Service (IRS) for recognition of their § 501(c)(3) status. Some religious organizations, such as churches, do not have to seek recognition from the IRS of their tax-exempt status. Additionally, organizations, other than private foundations, with normally no more than \$5,000 in annual gross receipts do not have to apply for recognition.

## When to File

An organization should try to file the application soon after its formation. If the application is filed within 27 months of the organization's formation, the exemption will generally be effective back to the date of formation. The IRS may grant an extension depending on the circumstances. If the organization does not file its application in a timely manner, it will generally not be treated as an exempt organization for the period between its formation and the postmark date on the application.

## Filing Requirements

An organization seeking § 501(c)(3) status must file an application (Form 1023) that shows it meets the organizational and operational requirements.<sup>4</sup> The application asks questions concerning a variety of areas related to the organization's activities. The organization's operations must be described and organizing documents, such as articles of incorporation or association, must be included. There are detailed questions about the compensation of and dealings with directors and highly-compensated employees, and the organization must complete financial statements. Additionally, the application must include the organization's Employer Identification Number (EIN), which may be obtained

---

<sup>2</sup> IRC § 501(h) allows § 501(c)(3) organizations to elect to have their lobbying activities measured by a numerical limit, as opposed to the indefinite "no substantial part" test. Some organizations, including churches, are not allowed to make this election.

<sup>3</sup> See Treas. Reg. §§ 1.501(c)(3)-1(b)(1), 1.501(c)(3)-1(c)(1) and 1.501(c)(3)-1(d)(1)(ii).

<sup>4</sup> Organizations seeking a group exemption letter do not apply using Form 1023. For more information, see IRS Publication 557, *Tax-Exempt Status for Your Organization*.

online or by telephone, and, if applicable, a power of attorney authorization, among other documents. The IRS may require additional information.

**User Fee.** As part of the application, organizations must pay a user fee. The fee is \$300 for organizations with average annual gross receipts of not more than \$10,000 and \$750 for all other organizations.<sup>5</sup> A new organization should use its expected average receipts to determine which fee is appropriate.

## Public Charity v. Private Foundation

On the application, the organization will need to tell the IRS that it is either a public charity or a private foundation. In general, private foundations receive contributions from limited sources and do not directly provide charitable services. Due to fear of abuse, private foundations are subject to stricter regulation than public charities. An organization is a private foundation unless it shows the IRS that it meets the requirements to be a public charity. Some organizations, such as churches, schools, and hospitals, automatically qualify to be public charities. Other organizations will be classified as public charities if they can show the IRS that they receive substantial public support.

**Advance Rulings.** An advance ruling allows a new organization to be treated as a public charity even though it is unable to show the IRS that it receives sufficient public support. The intent is to allow an organization to have five years in which to develop operations to obtain the necessary level of support. An organization can request an advance ruling on Form 1023. The organization should be able to show that it reasonably expects to be publicly supported during the advance ruling period. If the IRS grants the request, the organization will be treated as a public charity for five years and then must prove to the IRS that it receives substantial public support for the treatment to continue.

## IRS Determination of § 501(c)(3) Status

Applications are sent to IRS Exempt Organization (EO) Determinations. EO Determinations determines whether the organization meets the exemption requirements by looking at the statutory language, IRS regulations, and such sources as IRS revenue rulings. EO Determinations may ask an organization for further information. Difficult cases, e.g., where there is no precedent or technical advice is needed, are referred to IRS Headquarters. An organization may request a referral to this office for an issue requiring technical advice.

If the IRS approves the application, a favorable determination letter is sent to the organization. As discussed above, if the application for § 501(c)(3) status was filed in a timely manner, the exemption will generally be effective back to the date of the organization's formation. The exemption will not be effective back to formation if the IRS requires the organization to make changes in its structure or operations in order to receive the exemption or if the application was not timely filed. In both cases, the effective date of the exemption will be provided in the determination letter.

---

<sup>5</sup> Rev. Proc. 2007-8, 2007-1 I.R.B. 230.

Once the exemption has been approved, the organization may generally continue to rely on its § 501(c)(3) status unless there is a material change in the organization's purpose or activities that is inconsistent with the exemption requirements. Additionally, events outside of the organization's control may affect its status, including new laws, treaties, court decisions, or regulations.

**Adverse Determinations.** If the IRS issues an adverse determination, then the organization may protest the decision to the IRS Appeals Office or, if appropriate, IRS Headquarters. Once the organization has exhausted its administrative appeals, it may, subject to numerous requirements, file an appeal in the federal courts.

## Length of Determination Process

The IRS expects to respond to an exemption application within four months of the application's receipt. In 2002, the IRS estimated the average review was 91 days.<sup>6</sup> A common reason for delays is that the organization's application has incomplete information.

**Expedited Review.** The IRS has internal procedures that allow for expedited review of an application when:

- an organization has a pending grant and the failure to secure the grant may have an adverse impact on the organization's ability to continue operations,
- an organization is intended to provide relief to disaster victims,
- the determination process was delayed due to the fault of the IRS, or
- EO Determinations management determines that expedited review is warranted for a situation not listed above.<sup>7</sup>

An organization must request expedited review in its application. The management at EO Determinations decides whether the application will be given priority treatment.

An example of the IRS using an expedited review procedure occurred after September 11, 2001. On September 18, 2001, the IRS announced it would give priority treatment to applications of charities formed to respond to the events of September 11.<sup>8</sup> The IRS estimated that the average review of these applications was seven days.<sup>9</sup> The IRS also used the expedited review procedure after Hurricane Katrina for organizations seeking § 501(c)(3) status to provide relief to the victims.<sup>10</sup>

---

<sup>6</sup> See GAO, *Tax-Exempt Organizations: Improvements Possible in Public, IRS, and State Oversight of Charities*, GAO Report 02-526, at 60 (April 2002).

<sup>7</sup> Internal Revenue Manual 7.21.3.4.1 (01-01-2003).

<sup>8</sup> See IRS News Release IR-2001-82 (Sept. 18, 2001).

<sup>9</sup> See GAO Report 02-526, *supra* note 6, at 60 (April 2002).

<sup>10</sup> See IRS News Release IR-2005-93 (Sept. 6, 2005).