

IRS Releases Streamlined Application for Tax-Exempt Status

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The Internal Revenue Service (the “IRS”) has significantly streamlined the application process for small nonprofits seeking recognition as tax-exempt 501(c)(3) organizations through the release of a new application form on July 1.

The IRS’s Exempt Organizations division currently has more than one year’s worth of backlogged applications for tax-exempt status. Resource constraints at the IRS have made it challenging to reduce this backlog. Streamlining the application process for smaller nonprofit organizations may help address this long-standing issue.

The new Form 1023-EZ, which must be filed online at www.pay.gov with a \$400 filing fee, is only three pages in length as compared to the current 26-page Form 1023 and is designed to take significantly less time to complete. IRS review of applications using the new form is anticipated to be correspondingly faster.

To be eligible to use the Form 1023-EZ, an organization must qualify as a public charity or private foundation, have current or projected gross annual receipts of no more than \$50,000, have total assets of no more than \$250,000 and meet certain other criteria. Larger charitable organizations with income or assets above these thresholds, foreign organizations, churches, schools and hospitals are not eligible to use the Form 1023-EZ. The instructions to the Form 1023-EZ include an eligibility checklist that organizations must complete before filing the form. The IRS estimates that as many as 70% of all applicants for tax-exempt status may be eligible to use the new form.

The Form 1023-EZ, which hews closely to the draft form released by the IRS in April 2014, requests summary representations from applicants. Further, in contrast to the full Form 1023, the Form 1023-EZ does not require the applicant to provide budgeting and financial projections, detailed information regarding its activities or disclosure of the details of its compensation arrangements.

In this way, the Form 1023-EZ shifts a fair amount of the compliance burden for smaller organizations back onto the organizations themselves. The written narratives, financial information and governance disclosures that are required as part of the full Form 1023 offer a general roadmap for applicants to organize themselves in accordance with applicable laws and regulations. Organizations completing Form 1023-EZ will not have this roadmap and, therefore, will bear greater responsibility for educating themselves and working with their legal and financial advisors to ensure organizational and operational compliance with the rules applicable to tax-exempt organizations.

With the IRS exercising a much more cursory review of organizations before issuing determination letters, potential donors may also need to be more careful in vetting organizations that have received tax-exempt status using the Form 1023-EZ.

Organizations that have a Form 1023 pending with the IRS that has not yet been assigned for review may submit a Form 1023-EZ (along with the \$400 filing fee). The IRS will treat this as a withdrawal of the originally filed Form 1023, and the effective date of the organization’s application will be the date that the Form 1023-EZ was submitted to the IRS.

If an organization is applying for exemption as a 501(c)(3) organization, and submits its Form 1023-EZ within 27 months of the end of the month in which it was formed, it may be exempt as a 501(c)(3) organization from its date of formation. If the organization does not submit its Form 1023-EZ in this time period, its exemption as a 501(c)(3) organization may commence no earlier than the date that the Form 1023-EZ was submitted. Thus, an organization whose Form 1023 continues to be pending beyond that 27-month deadline may not want to withdraw its Form 1023 by submitting a Form 1023-EZ, since that would forfeit its opportunity to be recognized as a 501(c)(3) organization from the date of its formation.

In addition, an organization whose tax-exempt status was revoked due to a failure to annually file the required Form 990 may be eligible, in certain circumstances, to use Form 1023-EZ to reapply for tax-exempt status if otherwise qualified.

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