

Tax Guide for Nonprofits

4th Edition

Stephen Fishman, J.D.

Table of Contents

Chapter 1 – Nonprofits and the IRS	1
Learning Objectives	1
Introduction.....	1
What Do We Mean When We Say “Nonprofit”?	1
Tax-Exempt Nonprofits	1
Section 501(c)(3) Charitable Organizations	2
Private Foundations and Public Charities	3
The Life Cycle of a Nonprofit.....	3
Creating Your Legal Entity	4
Obtaining Tax-Exempt Status	4
Ongoing Compliance	5
Limitations on Your Nonprofit’s Activities	6
Documenting and Disclosing Contributions	7
Annual Tax Filings	7
Record Keeping.....	8
Ending Your Nonprofit.....	8
IRS Audits	8
What Is an Audit?	8
Who Gets Audited.....	9
Types of Audits.....	9
Audit Outcomes	13
Appealing an IRS Audit.....	14
Review Questions.....	16
Review Answers	18
Chapter 2 – Annual IRS Filings – The Form 990.....	21
Learning Objectives	21
Introduction.....	21
The Nuts and Bolts of the Filing Process	21
Why an Information Return?	21
Who Is Exempt?	22
Which Form Should You File?.....	23
When to File Your Return.....	24
When to File Your Return	24
How to File Your Return.....	25
What If You Don’t File?	25
The 990-N Postcard Filing—As Simple as It Gets.....	26
How to Complete and File Form 990-N	27
Form 990-EZ: The E-Z Way Out	28
General Background Information.....	29
Parts I and II: Financial Information.....	30
Part III: Program Accomplishments	39
Part IV: ODTKE Disclosure and Compensation	41
Parts V and VI: Additional Information.....	42
Part VI: Payments to Key Employees or Contractors.....	44
Signature Block	44
Schedules.....	45
Form 990: Just Hold Your Nose and File It.....	46
Do You Really Have to File Form 990?	46
Who Should Prepare Form 990?.....	47
An Overview of the Form 990.....	48
Getting Ready for Form 990.....	49
Are Your Management Practices Up to Snuff?	51
Identify and Disclose Family and Business Relationships	52

Table of Contents

Letting the Public See Your Report Card: Disclosure of Form 990.....	54
Public Inspection of Returns.....	55
Furnishing Copies of Returns.....	55
What If Someone Harasses You?	56
Penalties for Failure to Comply	56
Notifying the IRS If You Terminate, Merge, or Contract Your Nonprofit.....	56
Which Form to File.....	57
When the Return Is Due.....	57
Information You Must Disclose.....	57
Significant Contraction of Your Nonprofit.....	58
What to Do If the IRS Has Revoked Your Nonprofit's Tax-Exempt Status.....	58
Reinstating Tax-Exempt Status.....	59
If Your Nonprofit Was Previously Reinstated (Not Retroactively)	61
Review Questions.....	63
Review Answers	65
Chapter 3 – Record Keeping and Accounting.....	67
Learning Objectives	67
Introduction.....	67
Why Keep Financial Records?	67
Preparing Annual IRS Information Returns.....	67
Showing You're Fulfilling Your Nonprofit Mission.....	68
Showing You Qualify as a Public Charity.....	68
UBIT	68
Preparing Financial Statements	68
Monitoring Your Budget	68
What Does the IRS Require?	69
A Tax Year	69
An Accounting Method.....	70
A Record of Income and Expenses	71
A Paper Trail.....	77
Asset and Liability Records	79
Employment Tax Records	79
How Long Should Records Be Kept?	80
Do You Need an Independent Audit?	81
Minding the GAAP	82
Required Financial Statements	83
Accounting for Restricted Funds	83
Recording Pledges and Donations	83
Review Questions.....	85
Review Answers	87
Chapter 4 – Volunteers, Employees, and Independent Contractors	89
Learning Objectives	89
Introduction.....	89
Volunteers—The Backbone Workforce of Nonprofits.....	89
What Is a Volunteer?	90
Volunteer Work—From Director to Intern	90
Reimbursing Your Volunteers—Know the Rules.....	90
Accountable Plans—The Key to Success With the IRS	91
Local Transportation Costs	95
Travel and Entertainment Expenses.....	95
Unreimbursed Volunteer Expenses	96
Requirements for Deducting Unreimbursed Expenses.....	96
Substantiation of Volunteer Expenses.....	98
Benefits and Freebies—How to Show Your Appreciation Tax Free.....	99
Working Condition Fringe Benefits	99

Table of Contents

De Minimis Benefits—Those Token Freebies.....	100
Tax-Free Benefits for Volunteer-Employees	101
Paid Help: Employees and Independent Contractors.....	102
What's the Big Deal?	103
How to Tell the Difference.....	104
The Safe Harbor Rule for Independent Contractor Status.....	108
Getting an IRS Advance Determination	108
Classifying Corporate Officers and Directors	109
Hiring Independent Contractors.....	109
Procedures for Hiring Contractors	109
Your Tax Reporting Obligations	112
Filling Out Form 1099-MISC.....	113
Filing Paper Form 1099s.....	113
Hiring Employees.....	114
The Tax Collector Role	114
Reimbursing Your Employees.....	116
Obamacare (Affordable Care Act) and Nonprofit Employers.....	118
Is Your Nonprofit a “Large Employer”?	118
Independent Contractors Not Covered by Employer Mandate	118
Penalties Under the ACA	119
Small Business Health Care Tax Credit.....	119
Review Questions.....	120
Review Answers	122
Chapter 5 – Charitable Giving – The Basics and Cash Donations	125
Learning Objectives	125
Introduction.....	125
Your Role as a Nonprofit.....	125
Threshold Requirements for Deducting Donations.....	126
The Donee Side—It Must Be a Qualified Organization	127
The Donor Side—Only Those Who Itemize Can Deduct.....	128
Annual Limits on Charitable Deductions	130
Pease Limitation on Itemized Deductions.....	130
What Can a Donor Contribute?	130
When Is a Contribution Made for Tax Purposes?	131
Special Gifts—Earmarked, Restricted, and Conditional	132
Earmarked Gifts.....	132
Restricted Gifts	133
Conditional Gifts	133
If Your Nonprofit Provides Goods or Services.....	134
Cash Contributions	135
Contributions of \$250 and Less.....	135
Contributions of \$250 and More	136
Cash Gifts From IRAs	137
Interest-Free Loans	138
Quid Pro Quo Contributions	138
Disclosure Statements	139
Exceptions to the Quid Pro Quo Rules	141
Charity Auctions.....	144
Review Questions.....	145
Review Answers	147
Chapter 6 – Property Donations	149
Learning Objectives	149
Introduction.....	149
Annual Deduction Limit for Property Donations	149
Long-Term Capital Gain Property.....	150

Table of Contents

Ordinary Income and Short-Term Capital Gain Property.....	150
Valuing Property Donations—An Art, Not a Science.....	151
Your Nonprofit's Role in Determining Value.....	151
Basic Valuation Rule: Fair Market Value	151
Different Types of Property Donations.....	152
Clothing and Household Items	152
Vehicles—Used Cars, Boats, and Aircraft	153
Stock and Other Securities	155
Real Estate	157
Art, Antiques, Collectibles, and Unusual Gifts.....	158
Conservation Easements.....	160
Food Inventory.....	161
Business Inventory	161
Corporate Inventory and Equipment.....	161
Documenting Property Donations.....	162
Deadline for Providing Documentation	162
Property Worth Less Than \$250.....	163
Property Valued at \$250 to \$500.....	163
Property Valued at \$500 to \$5,000	164
Property Valued at \$5,000 or More.....	165
When a Nonprofit Sells Donated Property—IRS Form 8282	167
Documentation Rules for Cars, Boats, and Airplanes	172
Review Questions.....	176
Review Answers	177
Chapter 7 – Excessive Compensation, Sweetheart Deals, and Other Ways to Get in Trouble With the IRS.....	179
Learning Objectives	179
Introduction.....	179
A Nonprofit Is Not a Personal Piggy-Bank	179
The IRS Intermediate Sanctions Minefield.....	180
Disqualified Person + Excess Benefit = IRS Sanctions	181
Automatic Excess Benefits.....	182
Loans With Insiders	182
Transactions With Disqualified Persons—How to Avoid Problems With the IRS	183
Identify Your Nonprofit's Disqualified Persons	183
Follow IRS-Approved Procedures	185
Have a Conflict of Interest Policy.....	187
Excessive Compensation for Services: The Most Common Excess Benefit	188
Preapproval of Compensation.....	188
What Is Reasonable Compensation?	189
What Is Included in Compensation?	190
Using Comparable Compensation Data	191
Document All Taxable Compensation Paid to DPs	193
Reimburse Employee DP Expenses Under an Accountable Plan	195
Correcting and Reporting Excess Benefit Transactions	196
The IRS's Sentence of Death: Revocation of Tax-Exempt Status	197
Private Inurement	197
Private Benefit	198
Review Questions.....	201
Review Answers	203
Chapter 8 – Nonprofits That Make Money and UBIT.....	205
Learning Objectives	205
Introduction.....	205
What Is UBIT?	205
Is the Activity Related to Your Mission?.....	206

Table of Contents

Is the Activity a Business	208
Is the Activity “Regularly Carried On”?.....	209
Activities Exempt From UBIT	210
When Your Volunteers Do the Work.....	210
Thrift Shops and Donated Merchandise	210
Donor Lists	211
Convenience Activities.....	211
Business Sponsorships.....	211
Rental Income, Capital Gains, and Investment Income.....	212
Low-Cost Giveaways	213
Research Income.....	213
Bingo Games.....	214
Periodical Advertising Income	214
Do You Owe UBIT?	215
Filing UBIT Tax Returns.....	216
Deadline for Filing.....	217
Failure to File Form 990T.....	217
Contents of Form	217
Paying UBIT	217
Review Questions.....	219
Review Answers	220
Chapter 9 – Lobbying and Political Campaign Activities	221
Learning Objectives	221
Introduction.....	221
Lobbying by Nonprofits—What’s Allowed and What’s Not	221
What Is Lobbying?	222
Not All Advocacy Is Lobbying	223
Nonpartisan Education Is Not Lobbying.....	224
How Much Lobbying Is Too Much?	225
Reporting Your Lobbying Time and Expenses.....	227
Lobbying via the Internet.....	228
If You Receive Federal Grants	228
Political Campaign Activities—An Absolute Ban	229
What Activities Are Prohibited	229
Voter Education, Voter Registration, and Get-Out-the-Vote Drives	229
Candidate Appearances.....	230
Voter Guides.....	231
Individual Activity by Directors, Officers, and Employees	231
Issue Advocacy Versus Political Campaign Activity	232
Business Activity as Political Campaign Activity	233
Websites.....	233
Consequences of Violating the Rules.....	235
Getting Around the Restrictions.....	235
Forming a Social Welfare Organization	235
Forming a PAC	236
Review Questions.....	237
Review Answers	239
Chapter 10 – Help Beyond This Book.....	241
Learning Objectives	241
Introduction.....	241
Help From the IRS	241
Other Helpful Publications and Websites.....	243
Researching the Tax Law	244
Review Questions.....	249
Review Answers	250

Table of Contents

Appendix – Forms	251
IRS Form 990-EZ.....	251
Sample Conflict of Interest Policy.....	251
Rebuttable Presumption Checklist	251
Family and Business Relationship Questionnaire	251
Expense Report.....	251
Glossary.....	265
Index	271