

THE PPC NONPROFIT UPDATE

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Updated Exempt Organization Procedural Guidance



The IRS has updated guidance regarding the application process for tax-exempt status. Revenue Procedure 2020-8 (2020-8 IRB 447) modifies certain previous guidance as highlighted in this article.

Mandatory Electronic Filing for Form 1023

Applications for tax-exempt status under IRC Sec. 501(c)(3) filed after April 30, 2020, on Form 1023 must be submitted electronically. The electronic filing requirement also applies to organizations seeking a determination described in Section 501(e), (f), (k), (n), (q), or (r). Previously, a Form 1023 could be filed on paper. The revenue procedure, effective January 31, 2020, provides a 90-day grace period (e.g., through April 30) for paper applications already in progress before having to comply with the new electronic filing requirement.

Expedited handling requests. A request for expedited handling must be indicated

on the form and a supporting written statement must be submitted as an attachment with the completed application. This replaces the separate letter requesting expedited handling that was sent to the IRS with or soon after filing a paper Form 1023.

User fee. The Form 1023 user fee is currently \$600 and must be paid through **www.pay.gov**. Because fees are subject to change, applicants are advised to check the IRS website at **www.irs.gov** (and search “exempt organization user fee”). An exemption application will not be processed without payment of the proper user fee. Payment can be made directly from a bank account or by a credit or debit card.

Note: Form 1023-EZ, filed by eligible organizations, was already required to be filed electronically. The user fee for an applicant submitting Form 1023-EZ is currently \$275.

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Applications Filed after the 27-month Period

If an organization files an exemption application within the 27-month period following formation, and the IRS determines they qualify as a Section 501(c)(3) entity, their exempt status is effective from the date of formation. If an exemption application is not filed within this 27-month period, the organization qualifies as a Section 501(c)(3) entity from the date a subsequently approved application is postmarked or submitted (as applicable) with the IRS, rather than from the date of formation.

If the organization has been in existence for more than 27 months, it may qualify for an earlier effective date than the submission date. The earlier effective date may only be requested by completing Form 1023 in its entirety instead of completing Form 1023-EZ. Organizations can no longer file Form 1023-EZ and then submit a correspondence to request an earlier effective date.

Practical Consideration:

The IRS expects the benefits of electronic filing Form 1023 to mirror those realized when Form 1023-EZ went online in 2014, reflecting improved application processing time for both the Form 1023 and 1023-EZ while maintaining similar approval and rejection rates between the two forms.



Political Campaign Intervention Review

As this election year progresses, it's a good time to review the prohibitions against political campaign intervention. An organization that directly or indirectly participates or intervenes in a political campaign on behalf of, or in opposition to, a political candidate is an action organization and cannot be an exempt organization under IRC Sec. 501(c)(3) or (c)(29). Section 501(c)(4) organizations are not discussed in this article.

Caution: In addition to a possible loss of exemption, certain organizations are subject to an excise tax on amounts paid or incurred in participating or intervening in a political campaign (i.e., political expenditures). If

not corrected within a certain period, an additional excise tax applies. An organization's manager can also be subject to an excise tax if certain conditions apply.

Candidate for Public Office

To violate the prohibition against participating in political campaigns, a public charity must participate or intervene on behalf of or in opposition to a candidate for public office. A candidate for public office is one who offers himself, or is proposed by others, as a contestant for an elective public office, whether such office is national, state, or local [Reg. 1.501(c)(3)-1(c)(3)(iii)].

Whether an individual is actually a candidate is not always clear. Once an individual has declared his candidacy for public office, his status as a candidate is evident. Less obvious is the status of an individual rumored as a likely candidate for a particular office or an incumbent who has not announced an intention to run for reelection. A person does not become a candidate simply because there is public speculation about the person's possible candidacy. However, an individual who has not announced may nevertheless be deemed a candidate. The determination of when an individual has taken sufficient steps prior to announcing an intention to run for office to be considered to have offered himself or herself as a candidate is based on all the facts and circumstances. Ironically, an organization may be deemed to have intervened in a political campaign even though a particular person never becomes an actual candidate [Reg. 1.527-2(c)(1)].

Direct and Indirect Participation

Activities that are direct participation or intervention in a political campaign include: (1) giving a candidate or political party cash, property, the free use of facilities, and/or free services; (2) publishing or distributing written statements, or making oral statements on behalf of or in opposition to candidates; and (3) analyzing candidates' qualifications and publishing the names of those deemed most qualified [*Association of the Bar of the City of New York*, 62 AFTR 2d 88-5625 (2nd Cir. 1988)]. Several types of other activities may or may not result in prohibited participation or intervention, depending on subjective issues and subtle differences in the facts.

Indirect participation may occur when funds transferred to a non-Section 501(c)(3) exempt organization are used by the transferee for political purposes. Earmarking such funds to be used only for administrative expenses could help prevent indirect campaign activity.

Personal Views or Organization's Position?

The prohibition against campaign activity does not prevent an organization's officers or directors from expressing their views as individuals on a candidate, a political party, or a campaign. However, they cannot use the organization's financial assets, facilities, or personnel in any way and should clearly indicate that their actions or statements are entirely their own and not the organization's. Also, their views cannot be expressed in official organization publications or at official organization functions. The organization must not explicitly or implicitly ratify the actions of any individual to avoid having those actions attributable to it.

Education and Registration

Voter education, registration, and get-out-the-vote drives conducted by a Section 501(c)(3) or (c)(29) organization are not deemed political activities if conducted in a nonpartisan manner. However, participation or intervention conducted with a bias that (1) favors one candidate over another, (2) opposes a candidate in some way, or (3) favors a candidate or group of candidates, is prohibited. A facts and circumstances test must be applied in each of these situations.

Issue Advocacy

Section 501(c)(3) organizations can conduct public advocacy on significant moral, social, or economic issues even when a candidate has become closely identified with that issue during a campaign. However, certain precautions must be observed.

Campaign intervention occurs when an organization is commenting on a candidate rather than addressing an issue. Words such as "conservative," "liberal," "pro-life," or "pro-choice" cannot be used in lieu of a candidate's name to subliminally support or oppose a candidate. Advocacy communication must not reflect an organization's position on a candidate or slate of candidates even though names are not mentioned. The IRS applies factors to determine whether issue communications are deemed campaign intervention.

Voter Guides

Section 501(c)(3) organizations sometimes prepare and distribute voter guides that contain voting records, questionnaire responses, and other information. A voter guide will not be regarded as campaign intervention if it is unbiased in form, content, and distribution. Bias may be blatant or subtle, and a determination depends on the facts and circumstances in each case.

Newsletters

Publishing a candidate's views on a narrow range of issues important to the organization can be considered campaign intervention. However, an organization may publish a newsletter of incumbents' voting records on selected issues if certain parameters are met.

Business Activity

An organization cannot show political campaign bias in any aspects of its business activities, including the selling or renting of mailing lists, the leasing of office space, or the acceptance of paid political advertising.

Administration of a payroll deduction plan that allows employees to contribute to a political action committee (PAC) endorsed by the employer is considered participation or intervention in a political campaign. However, administration of a payroll deduction plan is apparently permissible if the employees can select the recipient PACs.

Websites

Section 501(c)(3) organizations often use their websites to disseminate statements and information. They also routinely link their websites to those maintained by other organizations as a way of providing additional information that the organizations believe is useful or relevant to the public. An organization that posts something on its website favoring or opposing a candidate for public office will be treated the same as if it distributed printed material, oral statements, or broadcasts that favored or opposed the candidate.

When an organization establishes a link to another website, the organization is responsible for the consequences of establishing and maintaining that link, even if it does not have control over the content of the linked site. Because the linked content may change over time, an organization should reduce the risk of political campaign intervention by monitoring the linked content and adjusting the links accordingly.

Practical Consideration:

Because the situations involving the question of prohibited campaign intervention depend on the particular facts involved and/or on subjective determination, Section 501(c)(3) and (c)(29) organizations must monitor any politically-tinged activities to avoid prohibited conduct.



Increased Transparency on Gifts-in-kind Coming

Nonprofit organizations of all sizes rely on gifts of nonfinancial assets for their operations. From the local food bank that receives donated food to the medical center that receives contributed medical services, the start-up nonprofit that receives free use of office space, and the women's shelter that receives business attire to help women reenter the workforce, these entities all use contributions other than cash to help achieve their missions. Users of financial statements want information about such contributions of nonfinancial assets, more commonly referred to as gifts-in-kind.

In February 2020, the FASB issued an exposure draft of a proposed Accounting Standards Update, *Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets*.

Proposed Changes

The exposure draft doesn't change how gifts of nonfinancial assets are recognized and measured. The intent of the exposure draft is to enhance the existing presentation and disclosure requirements to better address financial statement users' desire for transparency about gifts-in-kind. Currently, the disclosure requirements only address contributed services.

Presentation Requirements. The exposure draft proposes that nonprofit organizations present the gifts-in-kind they receive separately from contributions of cash or other financial assets.

Disclosure Requirements. The current disclosure requirements related to contributed services (FASB ASC 958-605-50-1) wouldn't change but would be moved to a new paragraph in the FASB ASC. New disclosures related to gifts-in-kind would include a breakdown of gifts-in-kind by type. Then for each type of gifts-in-kind, disclosures would include:

- Information about whether the nonprofit organization had or planned to either monetize the gift-in-kind or use it during the reporting period or a future period. If the nonprofit organization had or planned to use the gift-in-kind, the disclosure would describe the program or activity for the use.
- A description of any donor-imposed restrictions on the gifts-in-kind.

- How the organization valued the gifts-in-kind, including the principal market or most advantageous market, as those terms are used in FASB ASC 820, *Fair Value Measurement*.

Effective Date. As with other recent proposed ASUs, the FASB requests feedback on the appropriate effective date.

Practical Consideration:

The FASB welcomes comments on the exposure draft by April 10, 2020. See www.fasb.org for more information.



ARSC Issues SSARS 25

In February 2020, the AICPA Accounting and Review Services Committee (ARSC) issued Statement on Standards for Accounting and Review Services (SSARS) 25, *Materiality in a Review of Financial Statements and Adverse Conclusions*. These amendments to the SSARS are a result of ARSC's project to converge AR-C 90, *Review of Financial Statements*, with International Standard on Review Engagements (ISRE) 2400, *Engagements to Review Historical Financial Statements (Revised)* and remove inconsistencies between the SSARS and the auditing standards with respect to concepts that should apply to all service levels.

General Provisions

In general, SSARS 25 provides for the following:

- Makes explicit the requirement that the accountant should determine materiality for the financial statements as a whole and apply this benchmark when designing procedures and evaluating results. Such a requirement is already inherent in the extant standards because the accountant's review report concludes on whether the accountant is aware of any material modifications that would need to be made to the financial statements to comply with the applicable financial reporting framework.
- Provides for an adverse conclusion in a review report when there is evidence of pervasive and material misstatement of the financial statements. Under the extant standards, the accountant's only recourse is to withdraw from the engagement.
- Revises the accountant's review report to state that the accountant is required to be independent with

respect to the entity and also to comply with ethical responsibilities under the relevant professional standards.

- Provides language clarifying existing requirements and expands application guidance.

Effective Date. SSARS 25 is effective for engagements performed in accordance with SSARS for periods ending on or after December 15, 2021, with early implementation permitted.

Specific Amendments

Specific amendments to AR-C 60, *General Principles for Engagements Performed in Accordance With Statements on Standards for Accounting and Review Services*; AR-C 70, *Preparation of Financial Statements*; AR-C 80, *Compilation Engagements*; and AR-C 90, *Review of Financial Statements*, are as follows:

AR-C 60 Changes. SSARS 25 amends AR-C 60 as follows:

- Aligns the definition of *financial statements* to be consistent with the definition of that term in the auditing standards.
- Adds definitions deleted and moved from other SSARS standards to AR-C 60.07: *applicable financial reporting framework*, *designated accounting standard setter*, and *special purpose framework*.
- Adds definitions of *general purpose financial statements* and *general purpose framework* consistent with the definitions of those terms in the auditing standards.

AR-C 70 Changes. SSARS 25 amends AR-C 70 as follows:

- Deletes and moves the definitions of *applicable financial reporting framework* and *special purpose framework* to AR-C 60.07.
- Requires the accountant to disclose a material misstatement(s) in the financial statements when management does not provide additional or corrected information when the accountant becomes aware that the records, documents, explanations, or other information, including significant judgments, used in the preparation of financial statements are incomplete, inaccurate, or otherwise unsatisfactory.
- Requires the accountant to inform management of the reasons for withdrawing when the accountant intends to withdraw from the engagement because—
 - the accountant is unable to include a statement on each page of the financial statements indicating, at a minimum, that “no assurance is provided” on the financial statements; or

- management does not provide additional or corrected information when the accountant becomes aware that the records, documents, explanations, or other information, including significant judgments, used in the preparation of financial statements are incomplete, inaccurate, or otherwise unsatisfactory.

AR-C 80 Changes. SSARS 25 amends AR-C 80 as follows:

- Deletes and moves the definitions of *applicable financial reporting framework* and *special purpose framework* to AR-C 60.07.
- Eliminates the requirement that the accountant’s report on special purpose financial statements prepared in accordance with the regulatory or contractual basis of accounting disclose the purpose for which the financial statements are prepared. (AR-C 80.21b already requires the accountant’s compilation report to refer to the note in the financial statements that describes the framework.)
- Expands disclosures for the accountant’s report on special purpose financial statements prepared in accordance with the provisions of a contract to add a statement that the financial statements may not be suitable for another purpose.

AR-C 90 Changes. SSARS 25 amends AR-C 90 as follows:

- Deletes and moves the definitions of *applicable financial reporting framework*, *designated accounting standard setter*, and *special purpose framework* to AR-C 60.07.
- Adds the definitions of *inquiry*, *limited assurance*, *modified conclusion*, *pervasive*, and *professional skepticism*.
- Revises the definition of *review evidence*.
- Adds an explicit requirement for the accountant to plan and perform the review with professional skepticism.
- Adds required procedures if, after the engagement is accepted, the accountant is not satisfied that preconditions at AR-C 60.26 or AR-C 90.13 have been met.
- Makes explicit that the requirement to agree on the terms of the engagement is satisfied prior to commencement of the engagement.
- Adds a requirement that the agreement of the terms of the engagement should include a statement that a review is substantially less in scope than an audit and that the accountant will not express an opinion on the financial statements.
- Adds an explicit requirement for the accountant to determine materiality for the financial statements as a whole and apply materiality in designing procedures

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- and evaluating the results of the procedures performed. Further, the accountant is required to revise materiality if the accountant becomes aware of information that would have resulted in a different initial materiality amount.
- Significantly revises the list of inquiries the accountant is required to make of members of management who have responsibility for financial and accounting matters, and others as appropriate, concerning the financial statements.
- Adds a requirement for the accountant to remain alert for evidence of related-party relationships or transactions not previously identified.
- Adds inquiries the accountant should make of management if, in the course of performing review procedures, the accountant becomes aware of significant transactions outside the entity's normal course of business.
- Adds a requirement when using the work of others to ensure the work performed is adequate for the accountant's purposes.
- Eliminates the requirement that the accountant's report on special purpose financial statements prepared in accordance with the regulatory or contractual basis of accounting disclose the purpose for which the financial statements are prepared.
- Expands disclosures for the accountant's report on special purpose financial statements prepared in accordance with the provisions of a contract to add a statement that the financial statements may not be suitable for another purpose.
- Limits the requirement for a use restriction for the accountant's report to special purpose financial statements prepared in accordance with the contractual basis of accounting.
- Allows the accountant to express an adverse conclusion when the financial statements are materially and pervasively misstated and provides illustrative language.
- Requires the accountant to document communications with management, those charged with governance, and others about significant matters arising during the engagement, including the nature of such matters.
- Requires the accountant to document information that is inconsistent with the accountant's findings regarding significant matters that affect the financial statements and how those inconsistencies were addressed.
- Requires the accountant to document (1) who performed procedures and the date procedures were completed; and (2) who performed the technical review necessary to assure engagement quality control, the extent of such review, and the date the review was performed.

Practical Consideration:

SSARS 25 is available on the AICPA website at www.aicpa.org and on Checkpoint at checkpoint.riag.com/.

