

Frequently Asked Questions on Tax Exempt Status

How do we get a tax ID number?

Use IRS Form SS-4 to obtain an EIN (Employer Identification Number), an identifying number for all Federal tax purposes, whether you plan to have employees or not. You can apply for an EIN separately if you need one immediately, for banking, for instance, or attach a completed Form SS-4 to your application for tax exempt status. NOTE: This number does not, in any way, indicate whether or not your organization is exempt from tax!

What form do we file to get our tax exempt status?

Organizations seeking 501(c)(3) status (generally, charitable, educational, scientific and religious organizations) file IRS Form 1023. Other groups, such as social welfare organizations, labor unions, professional associations, or social clubs use form 1024.

How much will it cost to get our tax exempt status?

The IRS has charged a non-refundable processing fee for exemption applications since 1987. There is currently a two tier fee schedule. Organizations whose gross receipts have averaged, or will average, not more than \$10,000 per year pay \$150. Larger organizations pay \$500. A new IRS Revenue Procedure announcing the fees comes out each January; if you are submitting your application late in the year, there may be some benefit to getting it in before January 1st.

[Other costs you might incur when setting up a new non-profit organization include incorporation, charitable solicitation and other registration fees to state and local authorities, and fees to have your articles of incorporation, bylaws and exemption application professionally prepared.]

How long will it take to get our tax exempt status?

The IRS is currently (3/99) saying that it takes an average of 120 days to process an application. Roughly a quarter to a third of the applications they receive do not require further development, and are processed in six to ten weeks. The balance of the applications they receive take closer to five or six months - hence the "average" 120 days.

What is the deadline for applying for tax exempt status?

A new charitable, educational, scientific or religious organization must submit its application to the IRS by the end of the 27th month after the end of the month in which the organization was created. There is no similar deadline for non 501(c)(3) groups.

Can we ask for donations before we get our tax exempt status?

If your charitable, educational, scientific or religious organization submits its application to the IRS by the deadline described above and is approved, the "effective date" of your group's tax exempt status will be the day it was originally created. This means that contributions that your organization received after incorporation, but before the IRS issued your exemption letter will be deductible.

Because there is, of course, a chance that your application for tax exempt status will be turned down, it is only fair to let your potential donors know that you do not actually have IRS approval yet. "501(c)(3) application pending."

What are the chances of having our exemption application approved?

Recent statistics show the IRS approving tax exempt status for a little more than 70% of the applications they receive, and denying tax exempt status for less than 1% of the applications they receive. The other 29% or so are mostly organizations who become discouraged by the numerous questions the IRS asks, and give up before they actually get a ruling.

Does a small organization really need to apply?

Tax law does not require a 501(c)(3) application when an organization normally has gross receipts less than \$5,000 per year. A small organization may want to apply anyway to save donors possible inconvenience in an audit, to be able to apply for grants, or to obtain a bulk mailing permit. An organization which no longer qualifies for this low gross receipts exception must submit its application to the IRS within 90 days of the end of the year in which average gross receipts exceed \$5,000.

Can we pay salaries to our board members? Can we rent a building owned by a board member, or purchase equipment from a board member?

Tax law always permits the payment of reasonable compensation for goods or services actually rendered. If the IRS finds that amounts received by insiders are unreasonably high, however, they can fine both the insider who received the payment, and the board members who approved the payment. In extreme cases, they can take away the organization's tax exempt status.

It is a good idea, therefore, to fully document the board's decision-making process when any kind of payment will be made to an insider. Place copies of all relevant information (salary surveys, job description, resumés, prior salary history, real estate appraisals, rent "comparables") in the minutes, and never let a board member vote on his or her own compensation, or on the compensation of anyone related to him or her.