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Raising the Curtain: Notification Requirements for Social Welfare Organizations

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New rules require section 501(c)(4)¹ social welfare organizations to notify the IRS of their existence on or before September 6, 2016, unless the organizations applied for recognition of tax-exempt status on Form 1024, *Application for Recognition of Exemption under Section 501(a)* or submitted at least one Form 990-series return or notice on or before July 8, 2016. Organizations formed after that date have 60 days from the date of formation to provide notice. This article explains how the new notification requirements have materially changed the compliance procedures for social welfare organizations.

Background

Section 501(c)(4) describes civic leagues or organizations operated exclusively for the promotion of social welfare and certain local associations of employees. Unlike section 501(c)(3) organizations, which generally must apply for and obtain recognition of tax-exempt status from the IRS, section 501(c)(4) social welfare organizations do not have such a requirement and may “self-declare” their tax-favored status. Therefore, aside from receiving the information required by annual information returns

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¹ Unless otherwise indicated, section references are to the Internal Revenue Code of 1986, as amended (the “Code”) or the applicable regulations promulgated pursuant to the Code (the “regulations”).

(i.e., Form 990-series), the IRS typically would have no knowledge of the existence of these organizations.

The Protecting Americans from Tax Hikes Act of 2015 (“PATH Act”) changed the status quo by adding new section 506, which requires a section 501(c)(4) organization to provide notice to the IRS of its intent to operate as such within 60 days of its date of legal formation.² Organizations that fail to timely provide the notice may be subject to penalties.³

This new requirement does not otherwise change the option to “self-declare” section 501(c)(4) status or the option to apply for and obtain recognition of tax-exempt status under section 501(c)(4). Applying for tax-exempt status generally is still voluntary for social welfare organizations, notwithstanding the section 506 notification requirement.⁴ As a practical matter, social welfare organizations often apply for recognition of their tax-exempt status to obtain benefits such as IRS recognition of tax-exempt status and exemption from certain state and local taxes.

Absent action by Treasury or the IRS, taxpayers would have no mechanism to meet this new notification requirement. Therefore, on February 8, 2016, the IRS extended the date for submitting the required notification until at least 60 days from the issuance date of implementing regulations.⁵ On July 8, 2016, Treasury and the IRS issued temporary and proposed regulations setting forth the procedures for an organization to notify the IRS that it is operating as a section 501(c)(4) organization.⁶ Revenue Procedure 2016-41⁷ provides further guidance on these procedures and sets the user fee for providing the notification at \$50 for 2016.

Procedures for Providing Notice

All section 501(c)(4) organizations formed after July 8, 2016, must comply with the section 506 notification requirement in addition to any section 501(c)(4) organizations formed on or before July 8, 2016 that had not filed Form 1024 or at least one Form 990-series notice or return by that date.⁸ Organizations formed on or before July 8, 2016, that are subject to the notification requirement must provide notice to the IRS no later than September 6, 2016.⁹

To satisfy the notification requirement, an organization must create a free account on the IRS website,¹⁰ complete a new electronic Form 8976, *Notice of Intent to Operate Under Section 501(c)(4)*, and submit a \$50 user fee through Pay.gov.¹¹ The notice requires an authorized individual to attest to the following

² Consolidated Appropriations Act, 2015, Pub. L. No. 114-113, Division Q, Section 405 (Dec. 18, 2015).

³ Section 6652(c)(4).

⁴ But see section 6033(j)(2) (requiring organizations that lose tax-exempt status for failure to file required annual information returns or notices and want to regain tax-exempt status to apply to obtain reinstatement of such status).

⁵ Notice 2016-09, 2016-6 I.R.B. 306.

⁶ T.D. 9775, 81 Fed. Reg. 45,008 (2016); REG-101689-16, 81 Fed. Reg. 45,088 (2016).

⁷ 2016-30 I.R.B. 165 (July 8, 2016).

⁸ Section 1.506-1T(b).

⁹ Section 1.506-1T(b)(3).

¹⁰ <https://services.irs.gov/registration>.

¹¹ Rev. Proc. 2016-41, section 4.

information: (1) employer identification number ("EIN"); (2) name and mailing address of the organization; (3) date of formation; (4) state or jurisdiction of formation; (5) annual accounting period; and (6) whether the organization is either a social welfare organization or a local association of employees. The IRS will treat the notice as incomplete if any of the required information is missing, the organization's name or EIN do not match the records in the IRS Business Master File, or the organization fails to include payment of the correct user fee.

Within 60 days of receipt, the IRS will acknowledge a complete and properly submitted Form 8976. The IRS will reject incomplete Forms 8976 and will notify the organization of the non-acceptance and return or refund any user fee paid.

Effect of Notification

Neither the submission of the notification nor the IRS's acknowledgement of its receipt constitutes a request by an organization or a determination from the IRS that the organization qualifies for section 501(c)(4) tax-exempt status.¹² Further, submitting a Form 1024 does not relieve an organization of the requirement to submit the notification required by section 506. Form 8976 is not open to public inspection because it is not an application within the meaning of section 6104.¹³

Penalties

Failure to timely submit Form 8976 may result in the imposition of penalties on the organization.¹⁴ Unless the organization can demonstrate that the failure was due to reasonable cause, a penalty of \$20 per day, up to \$5,000, is imposed.¹⁵ After such a failure, the IRS may issue a written demand requesting Form 8976 by a specified date; failure to meet the demand will result in the imposition of a penalty of \$20 for each day during which the failure continues, up to \$5,000, on the person or persons responsible for the failure.¹⁶

Foreign Organizations

Both domestic and foreign organizations that intend to operate as section 501(c)(4) organizations generally are subject to the section 506 notification requirement.¹⁷ The IRS noted, however, that a foreign organization may be eligible for penalty relief if it submits the section 506 notification promptly after first commencing activities or earning income that triggers a filing requirement under section 6033. Revenue Procedure 2016-41 endorsed this suggested relief by setting forth an example for which reasonable cause penalty relief would be appropriate: A foreign organization that has not previously

¹² Notice 2016-09; section 1.506-1T(d).

¹³ Rev. Proc. 2016-41, section 7.01.

¹⁴ Section 6652(c)(4).

¹⁵ Section 6652(c)(4)(A).

¹⁶ Section 6652(c)(4)(B) (persons include any officer, director, trustee, employee, member, or other individual whose duty it is to submit the Form 8976).

¹⁷ T.D. 9775 (declining to except foreign organizations that do not conduct significant domestic activities (other than investment activities) from section 506).

conducted activities in the United States and that has no U.S.-source income submits Form 8976 within 60 days of commencing operations in the United States, even when such period is years after the organization's legal formation.¹⁸

Conclusion

The PATH Act's addition of a notification requirement has materially changed the procedure through which a section 501(c)(4) organization can be formed and maintain compliance. New social welfare organizations now have approximately two months after inception to notify the IRS that they are operating as such, regardless of whether they have applied for exemption or already filed an annual information return or notice. Although the notification process is not especially onerous, the prompt due date of the notification has the potential to catch newly formed organizations unaware, especially if they have been focused on formation as opposed to compliance requirements. Given the ease with which the Form 8976 can be completed, social welfare organizations should include the section 506 notification in the checklist of formation requirements to avoid having the 60-day notification window slip away in the flurry of other tasks facing newly formed organizations.

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¹⁸ Rev. Proc. 2016-41, section 8.03.