



REV. PROC. 2007-52 AND THE ROAD TO

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than 'filling in the blanks.'

EXEMPTION

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Tax exemptions are a matter of legislative grace, and taxpayers have the burden of establishing their entitlement to exemptions.¹ Although the IRS does not necessarily grant tax exemptions to organizations, the organizations generally apply for IRS recognition of the exemption that the organization possesses as a matter of law.² Thus, the entity seeking recognition of exempt status must file an elaborate application with the IRS, satisfying this burden and establishing entitlement to exemption. On 7/23/07, the IRS released Rev. Proc. 2007-52, 2007-30 IRB 222, which essentially updated the Service's procedures for recognizing exempt status. Rev. Proc. 2007-52 articulates the procedures for issuing determination letters and rulings on the exempt status of organizations under Sections 501 and Section 521, other than organizations involving certain employee plans (pension, profit sharing, stock bonus, annuity and ESOPs, covered under Rev. Proc. 2007-6, 2007-1 IRB 189). It also seeks to provide guidance on the procedures for the modification and revocation of determination letters or rulings, as well as providing guidance on the administrative remedies available prior to seeking judicial review under Section 7428.

Rev. Proc. 90-27

Rev. Proc. 2007-52 supersedes Rev. Proc. 90-27, 1990-1 CB 514. To fully understand the impact of Rev. Proc. 2007-52, it is important to understand the framework for the recognition

of exempt status under the prior revenue procedure.

Under Rev. Proc. 90-27, the organization seeking exemption is required to file or mail an application for recognition of exemption to the appropriate IRS District Director. Rev. Proc. 90-27 provides for seven Key District Offices (Central, Mid-Atlantic, North-Atlantic, Midwest, Southeast, Southwest, and Western).³ The request for recognition must include the completed application and any supporting documents establishing entitlement to exemption. As the application proceeds, the specialist assigned to the case reviews the exemption application, its attachments, and all other information provided by the applicant organization. The specialist then determines whether the organization qualifies for the claimed status in light of the facts as presented and in applying clearly established rules as set forth in the Code, regulations, rulings, Treasury Decisions, and court decisions published in the Internal Revenue Bulletin (IRB).

The District Director then issues a determination letter, based on the factual findings, either denying or recognizing the exemption. This relates only to applications with issues specifically covered by precedent (published in the IRB), statute, or regulations. Any cases involving issues that lack clear guidance are referred to the National Office. If the key District Director wishes to recognize the exemption contrary to a prior ruling from the

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National Office, the Director would require technical advice from the National Office before issuing the determination letter. Furthermore, any applications from certain categories of applicants specifically reserved to the National Office by revenue procedure or by the Internal Revenue Manual are also referred to the Office.⁴

Rev. Proc. 90-27 also states that an incomplete application may be returned to the applicant without being considered on its merits, accompanied by a letter of explanation as to what more was required by the IRS. An applicant for exemption under Section 501(c)(3) would be informed of the time within which the completed application would need to be resubmitted in order for the application to be considered a timely notice under Section 508(a).⁵

Rev. Proc. 90-27 has slowly become more and more inaccurate over time, as it has generally not been modified to keep current with the Service's actual procedures for processing exemption applications. In 1995, for example, the IRS decided to centralize the processing of exemption applications at its Cincinnati Service Center instead of having those applications sent to one of the seven Key Districts.⁶ Rev. Proc. 90-27 was never modified to reflect this change, although the IRS did modify the instructions to the various exemption application forms.

Rev. Proc. 2007-52

One significant change made by Rev. Proc. 2007-52 is the formal centralization of the application processing at the Determinations Office in Cincinnati, Ohio. Under the new procedure, the Key District Offices no longer exist and the applications for exemption are processed in Cincinnati. Despite the centralization of the application process, certain applications may be processed in other EO Determinations offices or referred to EO Technical, which is the IRS office primarily responsible for issuing letter rulings on exempt organization matters (referred to in Rev. Proc. 90-27 as "the National Office").⁷ EO Technical

is also responsible for providing technical advice and technical assistance to other IRS offices on exempt organization matters.⁸ Generally, applications will be referred to EO Technical if they present issues that are not specifically covered by statute, regulations, a ruling, an opinion, or a court decision published in the URB,⁹ or if they fall into certain categories of cases reserved by the IRS for handling by EO Technical for the purposes of establishing uniformity or centralized control.

General procedures. Only organizations organized under Section 501(c)(3) technically need a formal determination from the IRS, but many of the other categories of exempts still generally seek determination from the IRS as a measure of proof and assurance. Formal determination from the IRS lends a certain element of credibility to a nonprofit organization in facing the general public and thus, while it may not always be required, it may sometimes be to an organization's advantage to seek such determination. There is also anecdotal information indicating that the IRS Service Center in Ogden, Utah, which receives all annual information returns from exempt organizations (e.g., Forms 990 and 990-EZ), will not accept such returns from organizations that have not applied for recognition of their tax exempt status. If this information is correct, organizations that exceed the annual information return filing threshold, and so must file such returns, presumably will also seek such a determination.

As outlined above, the determinations process generally occurs at the EO Determinations Office in Cincinnati. There, the specialist assigned to the case reviews the answers provided in the application process and evaluates whether or not the organization meets the legal requirements for exemption under the Code section at issue. It is essential that the application be concise and complete. The specialist will decide to issue (or not issue) a determination letter based on the information provided during the application process. Thus, during the application period, the organization must establish that its primary purpose is an exempt one and that it intends to achieve

¹ Christian Liches National Ministry, Inc., 470 F.2d 849, 31 AFTR2d 73-460 (CA-10, 1972).

² Hopkins, *The Law of Tax-Exempt Organizations* (John Wiley & Sons, 2007), § 23.1.

³ Rev. Proc. 90-27, § 4.

⁴ Rev. Proc. 90-27, § 6.02.

⁵ Rev. Proc. 90-27, § 5.03.

⁶ Treasury Inspector General for Tax Administration, "Additional Management Actions Are Needed to Ensure the Timely Processing of Customer Applications for Employee Plans and Exempt Organizations Technical Determinations" (No. 2000-10-179) (August 2000), at 2.

⁷ Rev. Proc. 90-27, § 8.01.

⁸ Rev. Proc. 2007-52, § 1.01(4).

⁹ *Id.* at § 1.02.

such purpose. In the case of a Section 501(c)(3) organization, it is essential that the application detail the organization's charitable purpose and how it intends to achieve that purpose. As stated in a court opinion, "a taxpayer must openly and candidly disclose all facts bearing upon the organization, its operations, and its finances so that the [court] may be assured that it is not sanctioning an abuse of the revenue laws by granting the claimed exemption."¹⁰ More recently, the IRS has given higher scrutiny to the achievement of an exempt purpose. For example, the IRS has denied exemption to several of the down payment assistance programs that emerged in the runup to the real estate crisis, saying that they failed to establish that their operations furthered a charitable purpose. Instead, it found, the organizations served private purposes in assisting home buyers.¹¹ This position of private benefit was also taken by the IRS with regards to a program geared towards providing state compliance assistance to home-schooling parents, where the IRS felt that the benefit was not a public benefit but, rather, a private benefit being conferred on the parents.¹²

If the application is incomplete, the Determinations Office will request additional information or return the application for completion. An application's start date for the purposes of computing the 270-day period for judicial review is on the date on which the IRS receives a "substantially completed" Form 1023.

Application requirements. Rev. Proc. 2007-52 requires the filing of a "substantially completed application," accompanied by the correct user fee, in order for an organization to seek exemption.¹³ This refers to four types of applications for recognition of exempt status under Section 501 and Section 521:

1. The Form 1023 application, required for exemption under Section 501(c)(3) or Section 501(c), (f), (k), (n), and (q)
2. The Form 1024 application (submitted in conjunction with Form 8718), for exemption under Section 501(c)(4), (5), (6), (7), (8), (9), (10), (12), (13), (15), (17), (19), or (25).

3. The letter application (submitted in conjunction with Form 8718), for organizations seeking exemption under Section 501(c)(11), (14), (16), (18), (21), (22), (23), (26), (27), or (28), or under Section 501(d).
4. The (electronic) Form 8871, required for political organizations claiming exemption under Section 527.

Substantially complete. A "substantially complete" application generally is one that is signed by an authorized individual and includes an Employer Identification Number. The numbered Form applications consist of several questions regarding the organizations planned operations and activities, including questions on the organization's planned budget and fundraising (in the case of a Section 501(c)(3) organization). These questions must be answered in narrative form and provide enough detail to allow the IRS to conclude that the organization plans to achieve a desired exempt purpose.

The completed application also must include the organization's financial details—namely, a balance sheet and expense statement for the current year and the three years preceding. This may sometimes be difficult, especially since many organizations seek exemption from the IRS prior to commencing operations. If the organization has not been in existence for four years, it must submit statements for the years in which it has been in existence. If the organization has not yet commenced operations, or has not yet completed one full year of operations, the application must consist of a proposed budget for two full accounting periods and a current statement of assets and liabilities. The financial details are of utmost importance, and the IRS has denied exemption in the past for an inadequate disclosure of such details. The failure to submit such details and records to the IRS raises an inference that the facts, if disclosed, would be to the detriment of the organization's sought-for exemption.¹⁴

Finally, the organization must include a copy of the articles of organization and the bylaws (if applicable). The articles of organization (or any other enabling document) must either be a "conformed copy,"¹⁵ be signed by a principal officer, or be accompanied by a written declaration signed by an authorized individual certifying that the document is a complete and accurate copy of the original.



**REV. PROC. 2007-52
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¹⁰ The Nationalist Foundation, TCM 2000-318.

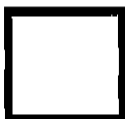
¹¹ Ltr. Rul. 200833022, Ltr. Rul. 200832035, Ltr. Rul. 200829044, Ltr. Rul. 200833024.

¹² Ltr. Rul. 200829058.

¹³ Rev. Proc. 2008-8; 2008-1 IRB 713 & 607.

¹⁴ Basic Bible Church of America, Auxiliary Chapter 11004, TCM 1983-287.

¹⁵ Rev. Proc. 68-14, 1968-1 CB 768.



**TO REQUEST
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On occasion, the IRS may require more information from the applicant organization, despite the submission of a complete application. This may happen if an application involves an issue regarding which contrary authorities exist and the organization has failed to disclose and distinguish the contrary authorities.¹⁶

Determination letter. The IRS generally will issue determination letters, rulings, and information letters on any aspect of the law of tax-exempt organizations, transactions that may have an impact on an organization's tax-exempt or public charity status, or transactions that may involve unrelated trade or business matters.¹⁷ Rev. Proc. 2007-52 outlines the standards for issuing a favorable determination letter, stating that such a letter will be issued only if the organization's application and supporting documents establish that it meets the particular requirements of the section under which it claims exemption.¹⁸

In the event of an adverse determination or ruling, the IRS generally will include a detailed discussion of its rationale for denying exemption and will advise the organization of its opportunity to appeal or protest the decision and request a conference.¹⁹ The appeals process is discussed below.

A favorable determination letter or ruling generally will have a retroactive effect to the date the organization was formed. Thus, it is generally more advisable for an organization seeking exemption to constitute itself as a corporation or trust than as an unincorporated association, because the date of formation is easier to determine. If the IRS requires that the organization make substantive amendments to its activities or its enabling documents (its articles of organization), the exemption will be effective only as of the date specified in the letter or ruling.²⁰

If a favorable determination is made, the organization must make the application and any supporting documents available to the public under Section 6104(a)(1). Such disclosure is not required if the IRS determines that it would adversely affect the organization, in which case limited disclosure rules may apply. The IRS, on the other hand, is also required to disclose adverse determination letters and rulings.²¹

Appeals and protests. As mentioned above, the IRS generally will advise the organization of its chance to appeal an adverse determination or ruling. The organization must, within 30 days from the date of the adverse

determination letter, submit a statement of the facts, law, and arguments in support of its position.²² The organization also must state in the letter whether it wishes to have an Appeals Office conference. The Determinations Office will review the appeal and will decide whether it believes the organization qualifies for the exempt status sought. If it does, the Determinations Office will issue a favorable determination letter.

If, however, the IRS maintains its position, the appeal and the exemption application are forwarded to the Appeals Office. At the Appeals Office, the appeal will be reviewed again. The Appeals office either will issue a favorable determination (or ruling) or, in the event that a conference was requested, will contact the organization to schedule a conference. The IRS may ask for the organization to submit more information at this conference, upon review of which the Appeals Office will decide on the exempt status of the organization. If an appeal notice is not timely made (or made at all) by the organization, the IRS will issue a final adverse determination letter or ruling.

Revocation or modification of determination or ruling. The issuance of a favorable determination by the IRS does not, in itself, grant exemption to an organization in perpetuity. The IRS may modify or even revoke a determination or ruling. Such modification or revocation may occur by a notice to the taxpayer to whom the determination letter or ruling was issued; enactment of legislation or ratification of a tax treaty; a decision of the U.S. Supreme Court; the issuance of a temporary or final regulations; or the issuance of a revenue ruling, revenue procedure, or other statement published in the IRB.²³ In several cases, such a revocation or modification may be retroactive.²⁴ In any event, the organization can seek an appeal of the revocation or modification. Upon exhausting the appeal remedies, the organi-

¹⁶ Rev. Proc. 2007-52, § 4.00(1).

¹⁷ Hopkins, *supra* note 2 at § 23.

¹⁸ Rev. Proc. 2007-52, § 6.01.

¹⁹ Rev. Proc. 2007-52, § 7.01.

²⁰ Rev. Proc. 2007-52, § 11.01(1).

²¹ Rev. Proc. 2007-52, § 8.02.

²² Rev. Proc. 2007-52, § 7.02.

²³ Rev. Proc. 2007-52, § 12.

²⁴ Rev. Proc. 2007-52, § 12.01. The revocation may be retroactive in the event of material omission or misstatement, misrepresentation of operations, or in the case of organizations to which Section 503 applies, the diversion of substantial corpus or income from the exempt purposes through a prohibited transaction.

zation's next step would be to seek declaratory judgment under Section 7428.

Judicial determinations. Prior to the enactment of Section 7428, a judicial review of an adverse determination by the IRS was extremely strenuous. An organization that was denied exemption had a single recourse—to wait for some sort of monetary controversy with the IRS. Although organizations attempted to obtain more immediate relief, that relief was denied and declaratory judgment actions were barred by the anti-injunction provisions of Section 7421(a).²⁵

The Tax Reform Act of 1976 provided a remedy to this problem in the form of Section 7428. It essentially allows certain organizations to bring an action for declaratory judgment in the Tax Court, the U.S. Court of Federal Claims, or the U.S. District Court for the District of Columbia. The action must involve an actual controversy relating to the recognition of exemption for organizations seeking (1) exemption under Section 501(c)(3), (2) classification as a private operating foundation under Section 4942(j)(3) or as a private foundation under Section 509(a), or (3) eligibility to receive tax-deductible charitable contributions under Section 170(c)(2). Organizations seeking exemption under other parts of Section 501(c) must still wait for a monetary dispute with the IRS to challenge an IRS refusal to recognize their claimed exempt status.

The "actual controversy" requirement relates to adverse notices of final determination²⁶ received by the IRS and even to untimely determinations (or the failure to make a

determination) for initial or continuing exemptions.²⁷ The "actual controversy" requirement has been interpreted very liberally by courts,²⁸ but there is a requirement that the IRS must have taken formal steps to revoke or to deny exemption.

To request declaratory relief, an organization must first exhaust all available administrative remedies. Under Rev. Proc. 2007-52, this includes the filing of a substantially complete application and following the rules for appeal (discussed above). The organization requesting declaratory relief under Section 7428 must have either received a final determination by certified or registered mail, or have waited out the 270-day period from when the substantially complete application was received by the IRS, in the event that no formal determination has been received by the organization.²⁹

Conclusion

In applying for recognition of tax-exempt status from the IRS, one cannot stress enough the necessity for clarity and conciseness. Most applications are denied because the applicant fails to show how it intends to further an exempt charitable purpose. Often, the organization fails to show, through the documents submitted, how its operations benefited the general public or a specified charitable class. Like any other legal documents, the application documents must be drafted with meticulous attention to detail and cautious regard for language. As mentioned in Rev. Proc. 2007-52, a substantially completed application consists of much more than "filling in the blanks." It requires concise and detailed financial information, properly drafted organizational documents, and well-drafted statements of purpose and activities.

The philanthropic sector is growing, and the advent of new exempt organizations will come with heightened scrutiny and greater regulation by the IRS. As philanthropy, and the public's interest in it, continues to grow, it is essential for philanthropic and other exempt organizations to be aware of the application rules and to seek proper guidance at the outset. ■

²⁵ *Bob Jones University*, 416 U.S. 725, 52 AFTR2d 83-5001 (1983).

²⁶ A determination, within the meaning of Section 7428(a)(1), is a final decision by the IRS affecting the tax qualification of a charitable organization.

²⁷ *Fishman and Schwartz: Nonprofit Organizations, Cases and Materials* (Foundation Press, 2006).

²⁸ In *Andlote Psychiatric Center, Inc.*, 95TC 371 (1992), the court concluded that actual controversy existed where the IRS issued a technical advice memorandum stating that the organization's exemption should be revoked. The court stated that with the issuance of a technical advice memorandum, final resolution was inevitable.

²⁹ Rev. Proc. 2007-52, § 10.03.