



The IRS Commissioner And Nonprofit Organizations

By Bruce R. Hopkins

Many in the nonprofit community predict that a massive piece of legislation regarding tax-exempt organizations and charitable giving is heading our way. Others dismiss the thought, saying that not much will actually happen.

Whatever your opinion, it would be a mistake to play down the significance of the Senate Finance Committee hearing held on April 5 on Charities and Charitable Giving: Proposals for Reform. Of great interest was the testimony of the Commissioner of Internal Revenue, Mark Everson.

Two of the themes running through this testimony were:

- 1) the rapid growth of the tax-exempt sector, and
- 2) the inability of statutory law in the exempt organizations context to keep up with the transformation of the activities of exempt organizations.

In particular, Commissioner Everson noted the official number of exempt organizations (1.8 million), the value of exempt organizations' assets (over \$3 trillion) and annual revenues for charities (\$897 billion).

A Less Compliant Environment?

Other external factors that Commissioner Everson sees that are causing a "less compliant environment" include a lack of adequate enforcement of the law by the IRS in recent years, "recent trends toward bad corporate practices" by exempt

entities, the rise of abusive transactions in the exempt organizations context, and efforts by terrorists to use charities to raise funds.

A positive development, he added, is improved transparency in the sector.

Mr. Everson identified two categories of compliance problems in the charitable sector.

1) Charities that abuse their status, namely through:

- abusive donor-advised fund arrangements,
- supporting organizations providing undue private benefit,
- corporation sole abuses,
- charitable trust abuses, and
- abusive credit counseling organizations.

2) Misuse of charities by third parties. These can include:

- overstated charitable deductions,
- abusive tax shelters with exempt organizations as accommodation parties,
- issues as to the reasonableness of compensation,
- terrorist financing, and
- political campaign activities by public charities.

He summarized the IRS's response to all of this in terms of "revitalization" and "refocus." Recent budget increases for the IRS were summarized, as were the agency's attempts to pursue the "right cases" and enhance transparency through electronic filings, revision of the Form 1023, planned changes to the Form 990, and expanded imaging of returns.

Raising Some Questions

Commissioner Everson raised these questions:

- Have changes in the practices of tax-exempt organizations created gaps in the statutory or regulatory framework?

- Does the IRS have the flexibility to respond appropriately to compliance issues?
- Should more be done to promote transparency?
- Does the agency have the resources it needs to do the job in this area?

Lurking in the first of these questions is the heart of the problem. The practices of exempt organizations have indeed created gaps in the statutory framework, but this is nothing new. Congress has allowed this law gap to persist and widen for decades. Probably three-quarters of the subjects involving the law of tax-exempt organizations entail little or no statutory law.

The Internal Revenue Code is essentially silent on matters such as private inurement, private benefit, political campaign activities, commerciality, use of subsidiaries, and involvement of exempt organizations in joint ventures, just to name a few. The IRS lacks the capability to substitute regulations and rules for this statutory law gap.

Senate Finance Committee Chairman Charles Grassley opened the hearing by stating that it had a twofold purpose: 1) strengthening the role of charities in the U.S., and 2) closing the "tax gap" (\$300 billion overall) as it relates to charitable giving. But the tax gap will not be closed until the statutory law gap is closed.

Where The IRS Is Headed

Commissioner Everson concluded his testimony by outlining where he believes the IRS must head in the next five years:

- Maintain a high level of quality service to the sector.
- Strengthen enforcement activities.
- Increase electronic submissions.
- Tailor the agency's compliance efforts by focusing on specific segments of the exempt organizations community.

It would be wise to keep an eye on this issue in the months ahead.

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