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Form 1023 [Application for Recognition of Exemption under Section 501(c)(3) of the Internal Revenue Code]

Chapter 17: Determining How and When to File for Exemption

Key Issue 17D: Applying for a Group Exemption Letter.

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General Rules

An exempt organization with subsidiaries can request a group exemption letter on behalf of its subsidiaries. (Form 1023 is not used to make such requests.) The benefits to a subsidiary organization of inclusion in a group exemption include (1) exclusion from filing Form 1023 (or Form 1024), (2) the ability (but not the requirement) to be included in a group Form 990 return and thus avoid filing a separate Form 990, and (3) enjoyment of the goodwill resulting from affiliation with the central organization. However, organizations considering inclusion in a group exemption should note that generally no group Form 990-T can be filed to report unrelated business income (see Key Issue 11C for the exception); effectively, a separate Form 990, Schedule A, must be filed for each subsidiary, and a subsidiary organization will not be listed in the IRS online tool-EO Select Check (an online search tool that allows users to check certain information about an organization's federal tax status and filings), which may curtail donations. See Key Issue 17J for additional discussion of EO Select Check.

The central organization can apply for the group exemption letter when it submits its own exemption application or after the IRS recognition of its exempt status. (The central organization cannot include itself in the group exemption request.) If a central organization applies for exempt status when it requests a group exemption letter for subordinates, it must provide all of the information for its own exemption (i.e., Form 1023, copies of organizing documents, etc.) in addition to the information described in this key issue for its subordinates. If the exempt status of a central organization is recognized by the IRS before the central organization applies for a group exemption, it must submit the necessary information for its subordinates, plus a statement that includes (1) its employer identification number, (2) the date of the letter recognizing its exempt status, (3) the location of the IRS office that issued the exemption, and (4) copies of any amendments to its governing instruments or internal regulations that have been made subsequent to the granting of its original exemption [Rev. Proc. 80-27; Reg. 601.201(n)(8)].

Observation: The IRS asked more than 2,000 central organizations to complete a group rulings

questionnaire. The questionnaire is intended to help the IRS better understand-

1. the relationship between central and parent organizations of group rulings and their subordinates, and
2. how these organizations satisfy their exemption and related filing requirements.

The IRS is currently analyzing the responses.

Definition of Subordinate Organization

Subordinate organizations eligible for inclusion in a group exemption are chapters, locals, posts, or units of a central organization. Subordinate organizations must establish that they are affiliated with the central organization and are subject to its general supervision and control. Rev. Proc. 80-27 does not define "general supervision and control" of the subordinate organization. However, apparently little interaction between the central organization and its subsidiaries is required. Each organization covered by the group exemption must be exempt under the same paragraph of IRC Sec. 501(c) (although not necessarily the same paragraph under which the central organization is exempt) and should be on the same accounting period as the central organization if it will be included in group annual (Form 990) returns.

An organization cannot be included in a group exemption if it (Rev. Proc. 80-27):

1. does not have an organizing document (e.g., articles of incorporation or a trust agreement);
2. is organized and operated in a foreign country; or
3. is a private foundation.

Information Required in the Application

The central organization must submit the following information for subordinate organizations that wish to be included in a group exemption [Rev. Proc. 80-27; Reg. 601.201(n)(8)(iii); IRS Pub. 557]:

1. Information verifying that the subordinates are:
 - a. affiliated with the central organization,
 - b. subject to its general supervision or control,
 - c. all eligible to qualify for exemption under the same paragraph of IRC Sec. 501(c),
 - d. not private foundations if the application involves Section 501(c)(3),
 - e. all using the same accounting period as the central organization (if the subordinates plan to file an annual return on a group basis each year), and
 - f. all organizations that were formed within the 27-month period [15 months per Reg. 1.508-1(a)(2) plus a 12-month automatic extension allowed by Reg. 301.9100-2] preceding the date the group exemption letter is being filed.

Warning: If a group exemption application covers one or more subordinates that were not formed within the 27-month period preceding the application, *all* subordinates will be recognized as exempt *only* from the date of application (Rev. Proc. 80-27). Thus, a subordinate formed outside of this

period may need to be excluded from the group exemption application (and file its own application for exemption) to permit other subordinate organizations to receive exemption from the date of incorporation.

2. A detailed description of the purposes and activities of the subordinate organizations, including the sources of receipts and the type of expenditures.
3. A sample copy of a uniform governing instrument (if such an instrument has been adopted by the subordinates) or copies of representative instruments.
4. An affirmation by a principal officer of the central organization that the information about the purpose and activities of the subordinate organizations provided in the group exemption letter is true and correct (i.e., the subordinates are operating in accordance with their stated purposes).
5. A statement that each subordinate included in the group exemption letter has been authorized by an officer of the subordinate to be included in the group exemption.
6. A list of any subordinates included in the group exemption that have previously obtained from the IRS a ruling or determination letter regarding exempt status.
7. An affirmation by a principal officer of the central organization that the subordinate organizations included in the group exemption are not private foundations [if the group exemption involves Section 501(c)(3) organizations].
8. A list of names, mailing addresses, actual addresses (if different), and employer identification numbers of the subordinate organizations included in the group exemption letter.
9. Information confirming that any subordinate organization that is a school (including a school affiliated with a church) is in compliance with the racial nondiscrimination policies set out in Rev. Rul. 71-447 and Rev. Proc. 75-50.
10. Information confirming that any school affiliated with a church is racially nondiscriminatory in accordance with Rev. Rul. 75-231.

This information should be provided in a letter (rather than on Form 1023) signed by a principal officer of the central organization (Rev. Proc. 80-27; IRS Pub. 557). Presumably the letter should be mailed or delivered by an IRS-approved private delivery service to the Internal Revenue Service; 201 West Rivercenter Blvd., Covington, KY 41011.

Note: The central organization should also complete Form 8718 and pay the current user fee when the group exemption request is submitted to the IRS. (See "User Fee" discussion in Key Issue 17E.) The IRS can decide whether to immediately return submissions that are not accompanied by a properly completed check or money order for the user fee or that are accompanied by a check or money order for less than the correct amount. In these cases, the filer will likely be contacted and given a reasonable amount of time to submit the proper fee. Paying the user fee by certified check or money order should expedite the processing of the application.

The central organization will receive a determination letter from the IRS as to the exempt status of its subordinates. If a favorable determination is received, a group identification number will be assigned to the group. This group number must appear on any Form 990 (or Form 990-EZ) filed for a subordinate organization included in the group exemption letter [whether the subordinate organization files its own

Form 990 (or Form 990-EZ) or is included in a group return]. [See Key Issue 1E and Checklist C107 for information on filing group (Form 990) returns.]

Required Annual Filing

For a group exemption letter to remain in force, the central organization must annually submit certain information to the IRS, in addition to filing Form 990 for the central organization and subordinate organizations. The information should be sent to: Department of the Treasury, Internal Revenue Service Center, Ogden, UT 84201-0027 (per Form 990 instructions) at least 90 days before the end of the central organization's tax year and should include the following [Rev. Proc. 80-27; Reg. 601.201(n)(8)(iv)]:

1. All changes in the purposes, character, or method of operation of the subordinates included in the group exemption letter.
2. A separate list by category of subordinates that fit within each of the following categories:
 - a. Subordinates that have changed their names or addresses during the year.
 - b. Subordinates that are no longer included in the group exemption letter because they have ceased to exist, disaffiliated with the central organization, or withdrawn their authorization to be included in the group exemption letter.
 - c. Subordinates to be added to the group exemption letter because they are newly organized or affiliated or because they have recently authorized the central organization to include them.

Each list should include the name, mailing address (and actual address, if different), and employer identification number of the subordinates listed. (If none of these changes apply for the year, the central organization should include a statement to that effect.)

3. If a subordinate is being added to the group exemption, the central organization must supply the same information about the new subordinate that would have been required if the subordinate had been included in the original application for a group exemption. However, if the information the central organization previously provided about its subordinate organizations is materially the same for the new subordinate, a statement to that effect may be submitted in lieu of providing specific information on the new subordinate (Rev. Proc. 80-27).

Events Causing Loss of Group Exemption

A group exemption letter can be terminated or revoked, either for a subordinate organization or for the group as a whole. A group exemption ceases to apply to a subordinate organization if (Rev. Proc. 80-27):

1. the central organization notifies the IRS that the subordinate no longer conforms to the requirements for inclusion in the group exemption,
2. the central organization notifies the IRS that the subordinate no longer authorizes its inclusion in the group exemption, or
3. the subordinate organization fails to file a required annual information return (e.g., Form 990 for an organization whose annual return is not part of a group filing).

Planning Tip: If the group exemption is terminated or revoked for a subordinate organization, the central organization can file for reinclusion of the subordinate in the group exemption at the time of its next annual submission, or the subordinate can apply for exempt status separately. If the application is made within 27 months of the subordinate's withdrawal from the group exemption, its exempt status continues uninterrupted. The 15-month filing deadline is effectively extended by 12 months [Reg. 301.9100-2(a)(2)(iv); Rev. Rul. 90-100].

A group exemption ceases to apply to the entire group of subordinate organizations affiliated with a central organization if the central organization (Rev. Proc. 80-27; IRS Pub. 557):

1. ceases to exist,
2. ceases to qualify for exemption under IRC Sec. 501(c),
3. fails to submit the information required annually regarding the subordinate organizations (discussed earlier in this key issue under the heading "Required Annual Filing"),
4. fails to file its annual information return (e.g., Form 990), or
5. is notified by the IRS that the group no longer meets the conditions for continued effectiveness of the group exemption.

Example 17D-1: Revocation of the central organization's exempt status.

Stop the Ozone Deterioration, Inc. (STOD), was formed several years ago and received a favorable determination letter from the IRS indicating it qualified as a Section 501(c)(3) organization. STOD has 23 local chapters that received a group exemption in 1994 and subsequently filed a combined Form 990. In the current year, STOD's exempt status was revoked because it no longer operated exclusively for charitable purposes. If STOD's local chapters wish to maintain their exempt status, they have two options:

1. One of the chapters can apply for exempt status and then apply for a group exemption for the other 22 chapters (or any lesser number of chapters that authorize inclusion). The former subordinate applying for exempt status would become the new central organization. This alternative may not be acceptable to any chapter that does not want to be under the control of the new central organization.
2. Each of the subordinate chapters may apply separately for tax-exempt status.

As long as the group exemption letter (if option 1 is selected) or the Forms 1023 are filed within 27 months of the date on which STOD's exempt status is revoked, each chapter's exempt status continues uninterrupted.

Filing Annual Returns for the Group

A central organization can file a "combined" annual return (Form 990) for all or any of its subordinates (the central organization must file a separate return), or the central organization and each of its subordinates can file separate Forms 990 (or Forms 990-EZ). (See Key Issue 1E and Checklist C107 for information on filing group returns.) However, a consolidated Form 990-T cannot be filed—each subordinate organization and the central organization generally must file a separate Form 990-T if one is required. (See Key Issue 11C for when a consolidated Form 990-T is permitted.)

Compliance Checks with Parent Organizations

To better understand the relationship between parent/central organizations and their subordinates and to learn how they satisfy their exemption and filing requirements, the IRS is asking more than 2,000 central/parent organizations to complete a group rulings questionnaire. This is a compliance check rather than an audit or examination.

An audit or examination is a review of an organization's book and records, in contrast to a compliance check, which is a review to determine if:

1. an organization adheres to recordkeeping and information reporting requirements, and
2. its activities are consistent with its tax-exempt purpose.

Although there is no penalty for refusing to submit a compliance check, the IRS can open a formal examination, regardless of whether the organization agrees to participate in the compliance check.

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