

## IRS Issues Temporary Regulations Eliminating Advance Ruling Process and Making Other Changes to Implement the New Form 990

### *Alert*

On September 8, 2008, the Internal Revenue Service issued temporary regulations that eliminate the advance ruling period for new Section 501(c)(3) organizations, thus simplifying the approval process for new organizations seeking to be classified as publicly supported charities. The temporary regulations also make other important changes to implement the redesigned Form 990.

### **Elimination of Advance Ruling Process**

Under the old regulations, a new Section 501(c)(3) organization that had not completed its first tax year had to go through a two-step process to be recognized as a publicly supported charity: 1) it had to declare that it expected to be publicly supported and request an "advance ruling" from the IRS regarding its public charity status, and 2) at the end of the five-year advance ruling period, it had to file Form 8734 (Support Schedule for Advance Ruling Period) to establish that it met the public support test. If the organization met the public support test, it would receive a final determination letter from the IRS. If, on the other hand, the organization failed to meet the test, the IRS would reclassify it as a private foundation and the organization would be subject to the excise tax on net investment income retroactively for the advance ruling period.

Under the new regulations, which became effective on September 9, 2008, the advance ruling process and Form 8734 filing requirement are eliminated. If an organization can demonstrate to the IRS in its exemption application (Form 1023) that it can reasonably be expected to meet the public support test during its first five years, the organization will be classified as a public charity. The organization will retain its public charity status for its first five years and will not be subject to any private foundation excise taxes regardless of the amount of public support it in fact receives during that period. However, beginning with the organization's sixth tax year, it must demonstrate to the IRS on Schedule A of its annual Form 990 information return that it actually is publicly supported.

The new regulations provide the following transition rules:

- Section 501(c)(3) organizations that have received advance rulings that have expired or will expire on or after June 9, 2008 will be classified as public charities and no longer need to file Form 8734 with the IRS. The advance rulings will be considered final determinations, even if the organizations did not meet the public support test for their first five years.
- Organizations whose advance rulings had expired before June 9, 2008 are still subject to the old regulations. If such an organization did not file Form 8734, it will be reclassified as a private foundation unless it submits documentation to the IRS demonstrating that it met the public support test during the advance ruling period.
- New exemption applications submitted before September 9, 2008, the effective date of the new regulations, will be processed under the new rules.

## Other Changes to Implement the New Form 990

The new regulations also make other changes that are related to implementing the new Form 990, which must be used by organizations for tax years beginning in 2008, including the following:

- The public support computation period is now a five-year period (the four prior years plus the current year) instead of the four years immediately preceding the current tax year.
- Support must be reported using the organization's overall method of accounting, instead of requiring the cash method of accounting for support calculations.
- Threshold amounts have changed for reporting compensation paid to certain individuals, such as directors, officers, and key employees, to be consistent with the new Form 990 requirements.
- Compensation must be reported on a calendar year basis, even if the organization's fiscal year is not the calendar year, to better align with Form W-2 and Form 1099 reporting.

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