

What's Up These Days with the Form 1023-EZ?

06.02.17 | Linda J. Rosenthal, JD



The Internal Revenue Service used to have a huge problem: it generally took 18 months to two years to process even a fairly straightforward 501(c)(3) tax-exemption application.

That's when a big change was proposed: the introduction of the Form 1023-EZ for the many new, smaller, organizations.

We posted about that rollout in July 2014, and about the early reaction and results [here](#), [here](#), and [here](#). Tim Delaney, the President and CEO of the National Council of Nonprofits summed it up fairly well: "It's easier to get tax-exempt status under Form 1023-EZ than it is [to get a library card](#)." It did, however, clear up the backup.

So, How is the Form 1023-EZ Doing These Days?

The Taxpayer Advocate Service "is an [independent organization within the IRS](#)." Its job is "to ensure that every taxpayer is treated fairly and ...[knows and understands its] ...rights."

Each year, the TAS issues a report to Congress that "[analyzes the most serious problems](#) facing taxpayers, recommends tax law changes to Congress, and presents original research studies into issues affecting taxpayers."

Report on 2015

In [Critics' Concerns About Form 1023-EZ: Spot On](#) (March 18, 2016), we told you about the section of the TAS [2015 Annual Report to Congress](#), relating to exempt organizations. It was brutal, beginning with the "highlights" section on the cover, which read: "Recognition as a Tax-Exempt Organization is [Now Virtually Automatic](#) for Most Applicants."

Going downhill from there, the Report was a "[stinging indictment](#) of the IRS's 'absurd' handling of applications for tax exemption, especially the recently introduced" 1023-EZ:

- The Form 1023-EZ “invites noncompliance, diverts tax dollars and taxpayer donations, and harms organizations later determined to be taxable.
- The approval rate for 1023-EZ applications is 95%, but when the agency does a pre-determination review on a sampling basis, the approval rate is just 77% when documents or basic information are reviewed, “rather than relying only on the attestations contained in the form.”
- In the same pre-determination samplings, almost 20% of applicants, “despite their attestations to the[] contrary, did not qualify for exempt status as a matter of law.” These results are consistent with the Taxpayer Advocate Service’s own representative sample of 1023-EZ applications: “37% of the organizations ... did not satisfy the legal requirements for exempt status.”

The Taxpayer Advocate Service recommended revisions to the Form 1023-EZ , as we reported in the [March 18, 2016 post](#).

Report on 2016

Did the situation improve in 2016? The Taxpayer Advocate Service’s most recent report opens: “Form 1023-EZ: The IRS’s Reliance on Form 1023-EZ Causes It to Erroneously Grant ... § 501(c)(3) Status to Unqualified Organizations.”

Ouch!

The problem continues to be that the streamlined application requires applicants only to “attest that they meet the requirements for qualification as” 501(c)(3) organizations.

Currently, “most applications” for 501(c)(3) status are “submitted on Form 1023-EZ.” And “the IRS approves 94 percent of Form 1023-EZ applications.” TAS concludes: “[T]oo many organizations that are either unqualified or are not eligible to use the Form 1023-EZ process, manage to slip through and get approved.”

This is “an unacceptably high rate,” demonstrating the need for revisions to the Form 1023-EZ. While the IRS had already agreed to require a narrative statement of applicants’ activities,” still – according to the TAS – it’s not enough.

Unless already available online at no cost, applicants must submit their articles of incorporation with “acceptable purpose and dissolution clauses.” The IRS should also require “summary financial information.” No decision on tax exemption should be made before then.

New Form 990-EZ

The IRS has recently released an “updated Form 990-EZ, Short Form Return of Organization Exempt From Income Tax, that will help tax-exempt organizations avoid common mistakes when filing their annual return.”

The revised Form 990-EZ “includes 29 ‘help’ icons describing key information needed to complete many of the fields within the form, with links to additional assistance at IRS.gov. These “pop-up”

boxes tell the applicant how to avoid common mistakes in the application process. The change was made also to encourage online filing which produces fewer errors than paper-filed returns.

Conclusion

We'll monitor and report on any new developments related to the updated Form 1023-EZ.

— *Linda J. Rosenthal, J.D., FPLG Information & Research Director*