

LR
#10**EXEMPT ORGANIZATIONS (EOs): Require More Frequent Updates to Publicly Available Databases of EOs****TAXPAYER RIGHTS IMPACTED¹**

- *The Right to Be Informed*
- *The Right to Quality Service*

PROBLEM

The IRS's Tax Exempt and Government Entities (TE/GE) division maintains a list of tax exempt organizations (EOs) on two publicly accessible online databases, the Exempt Organizations Business Master File (EO BMF)² and Exempt Organizations Select Check (EO Select Check).³ When an EO fails to file an information return or notice for three consecutive years, its exempt status is automatically revoked.⁴ Shortly after this automatic revocation, which can sometimes be erroneous, the IRS removes the EO from its online-published lists of EOs and lists it as one whose exempt status was automatically revoked.

Unless the automatic revocation was due to IRS error, an automatically revoked organization must submit a new application to have its exempt status reinstated.⁵ Even if the IRS promptly reinstates the organization or discovers its error, IRS databases will not immediately reflect the organization's restored exempt status, as the IRS updates its databases only monthly, on the second Monday of every month. However, these databases are not updated at all during the month of January, meaning there is a two-month updating gap from the second Monday in December until the second Monday in February.⁶ Reinstated EOs may lose out on donations or grants they would have received had IRS databases accurately reflected their status, which may be an existential issue for some organizations. The number of automatic revocation reinstatement cases during this gap period alone exceeded 2,500 in both fiscal years (FYs) 2014 and 2015, and more than 70 percent of these cases were 501(c)(3) organizations.⁷ These delays undermine taxpayers' *right to be informed* and *right to quality service*.⁸

1 See Taxpayer Bill of Rights, available at www.TaxpayerAdvocate.irs.gov/taxpayer-rights.

2 The EO BMF (<http://www.irs.gov/Charities-&Non-Profits/Exempt-Organizations-Business-Master-File-Extract-EO-BMF>) contains information about EOs such as the organization's employer identification number (EIN), name and address, the Internal Revenue Code (IRC) § 501(c) subsection under which it is exempt, whether contributions to it are tax deductible, whether it is a private foundation or a public charity (and the type of public charity), the month and year it received its exemption ruling, and information from its Form 990 series return. See Exempt Organizations Business Master File Extract (EO BMF), available at http://www.irs.gov/pub/irs-soi/eo_info.pdf.

3 EO Select Check is an online search tool, available at <http://apps.irs.gov/app/eos/>, that allows users to search for organizations eligible to receive tax deductible contributions (Publication 78 data), organizations whose tax exemption has been automatically revoked for not filing a Form 990-series return or notice for three consecutive years (Auto-Revocation List), and organizations that have filed a Form 990-N (also called an e-Postcard), an annual notice required to be filed by small EOs. Unless otherwise indicated, we use "EO Select Check" to refer to the capability to determine whether an organization is eligible to receive tax deductible contributions (Publication 78 data). See Internal Revenue Manual (IRM) 25.7.6.1 (Jan. 1, 2015).

4 See IRC § 6033(j)(1) (requiring the IRS to publish and maintain a list of automatically revoked organizations).

5 See IRC § 6033(j)(2).

6 See IRM 25.7.5.1(1) (Jan. 1, 2015) (noting that the EO Standard Extract Program is a computer program that is run on a monthly basis (except for January) to allow for extraction of both entity and limited return information from EO accounts contained on the BMF).

7 TE/GE response to TAS research request (July 31, 2015).

8 For a detailed discussion of the EO database updating delay issue, see Most Serious Problem: *Exempt Organizations (EOs): The IRS's Delay in Updating Publicly Available Lists of EOs Harms Reinstated Organizations and Misleads Taxpayers*, *supra*.

EXAMPLE

A small, volunteer-run Internal Revenue Code (IRC) § 501(c)(3) EO is automatically revoked because it did not file a required information return or notice for three consecutive years.⁹ As a result, the IRS places the organization on the automatic revocation list and removes it from the EO BMF and EO Select Check online databases.

Once the organization discovers that its exemption was automatically revoked, it quickly applies for reinstatement of exempt status. The IRS promptly approves the application and sends the organization a new determination letter acknowledging the approval. However, this approval occurs in mid-December, after the IRS has already updated its online databases and the next update will not occur until February. The organization is contacted by a potential donor who would like to make a sizeable donation before the end of the year but wishes to confirm the organization's exempt status beforehand to ensure the donation will be tax-deductible. The potential donor is concerned because although the organization has a new determination letter, its name does not appear on the IRS's online databases. As a result, the organization may lose a critical donation because the IRS's online databases do not accurately reflect its exempt status.

RECOMMENDATIONS

To address IRS delays in updating its publicly available databases of EOs and their adverse impact on automatically revoked organizations that have been reinstated, the National Taxpayer Advocate recommends that Congress amend IRC § 6033 to require the IRS to:

1. Update EO BMF and Select Check on a weekly basis as is the case for Form 990-N updates; and
2. Implement an emergency process that, even when there is weekly updating, allows for manual database updates within 24 hours of the restoration of exempt status.

PRESENT LAW

Almost ten years ago, Congress passed the Pension Protection Act of 2006, which among other things, amended IRC § 6033 to provide for the automatic revocation of EOs that did not file a required information return or notice for three consecutive years.¹⁰ Once an organization is automatically revoked, the IRS is required by statute to place it on a list of automatically revoked organizations.¹¹ Automatically revoked organizations seeking reinstatement of exempt status are also statutorily required to submit a new application to the IRS (except for when the revocation was erroneous).¹²

In addition to being placed on the automatic revocation list, organizations that have been automatically revoked are removed from the two online databases of EOs, EO BMF and EO Select Check. These databases are of critical importance for two reasons. First, they allow potential individual donors to verify,

⁹ See IRC § 6033(j)(1).

¹⁰ Pub. L. No. 109-280 § 1223, 120 Stat. 780, 1090 (2006). The law went into effect for tax periods beginning after 2006. See IRC § 6033(j)(1) (providing that the effective date of the automatic revocation is the due date of the third annual return or notice).

¹¹ See IRC § 6033(j)(1). The only way an automatically revoked organization can be removed from this list is if the revocation was due to IRS error. This list of automatically revoked organizations is available online at https://apps.irs.gov/app/eos/main-Search.do;jsessionid=dK2bhgtr3luhznjUpp62cg__?mainSearchChoice=revoked&dispatchMethod=selectSearch.

¹² See IRC § 6033(j)(2). An automatically revoked organization may obtain retroactive reinstatement of its exempt status. See Rev. Proc. 2014-11, 2014-3 I.R.B. 411.

before making a donation, that their contributions will be tax deductible.¹³ Second, they allow private foundations to verify that they are making a grant to a qualifying public charity.¹⁴ IRS guidance provides that grantors and contributors may rely on an organization's listing on EO Select Check or EO BMF.¹⁵ In addition, grantors and contributors may, in some situations, rely on EO BMF information provided by a third party.¹⁶

There is no current legal requirement for the IRS to update its online EO databases at any particular interval.

REASONS FOR CHANGE

The IRS recognizes that potential donors and grantors may rely exclusively on its online databases.¹⁷ However, it does not update them in a timely manner, causing reinstated automatically revoked organizations, such as the one in the example above, to potentially lose donations or grants.¹⁸ Currently, EO Select Check and EO BMF are only updated monthly, on the second Monday of every month.¹⁹ An organization that misses the updating cutoff will not appear on the IRS lists until the next month. In addition, these databases are not updated at all during the month of January, meaning there is a two-month updating gap from the second Monday in December until the second Monday in February.²⁰ As a result, new and reinstated EOs that receive IRS approval of exemption after the early December cutoff will not appear on publicly available IRS databases until mid-February, which is well after the critical year-end fundraising push.

The number of automatic revocation reinstatement cases during this gap period alone exceeded 2,500 in both FYs 2014 and 2015, and more than 70 percent of these cases were 501(c)(3) organizations.²¹ However, the IRS disavows responsibility if an EO loses a donation or grant because its databases do

13 A charitable contribution deduction is allowed for donations to organizations described in IRC § 170(c). These are most commonly IRC § 501(c)(3) organizations.

14 Private foundations prefer making grants to qualifying IRC § 501(c)(3) public charities over other organizations as doing so relieves them of certain oversight requirements (called expenditure responsibility) that would otherwise arise, and eliminates the risk of incurring liability for an excise tax under IRC § 4945.

15 See Rev. Proc. 2011-33, 2011-25 I.R.B. 887.

16 *Id.*

17 See IRM 25.7.6.1(3) (Jan. 1, 2015); IRM 21.3.8.12.12(3) (June 18, 2012); IRM 21.3.8.12.13(3) (Nov. 16, 2012).

18 This delay may also affect newly-recognized tax exempt organizations that receive a determination letter but are not promptly listed on the online databases. However, the harm to reinstated automatically revoked organizations is arguably greater as these organizations were formerly tax exempt and had the ability to receive tax-deductible contributions.

19 IRM 21.3.8.3.8(1)(f) (Oct. 1, 2015) (noting "online Publication 78 data is generally updated the second Monday of each month"); IRM 21.3.8.12.13(2) (Nov. 16, 2012) (noting that EO BMF is updated or extracted monthly). The term "extracted" is used because the EO BMF is an extract of information regarding EO accounts from the larger BMF. See IRM 25.7.5.1(1) (Jan. 1, 2015). In response to a TAS information request, the IRS stated that the internal IRS EO BMF list is generally updated within two weeks of a favorable case closing. The IRS also stated that the program that produces the online EO BMF and EO Select Check extracts is run approximately the last full week of each month and posted online to irs.gov the second Monday of the following month. Any accounts that are updated and posted prior to the running of the extract program will appear online. This means that an EO account update could take between 30 to 60 days to be reflected on the online EO BMF and EO Select Check databases. TE/GE response to TAS research request (July 31, 2015). Thus, there is a disconnect between IRS internal database updating (approximately two weeks) and external (*i.e.*, online) database updating (30-60 days).

20 See IRM 25.7.5.1(1) (Jan. 1, 2015) (noting that the EO Standard Extract Program is a computer program that is run on a monthly basis (except for January) to allow for extraction of both entity and limited return information from EO accounts contained on the BMF).

21 TE/GE response to TAS research request (July 31, 2015).

not accurately reflect that the organization is exempt.²² It advises reinstated organizations to either show potential contributors a current IRS determination letter or ask them to contact the IRS's TE/GE toll-free line (and face lengthy hold times, courtesy disconnects, and poor levels of service) to verify the organization's exempt status.²³ These suggestions place a burden on the reinstated organization or the potential donor or grantor. Many donors or grantors may simply "move on" and make a donation or grant to an organization that appears on EO Select Check and EO BMF. Other donors or grantors have operational guidelines that require the EO to be listed on the IRS databases before consideration for donations or grants.²⁴

If the IRS were to update its online databases on a weekly basis, as it does for its list of Form 990-N (e-Postcard) filers,²⁵ it would alleviate the hardship on reinstated automatically revoked organizations and their donors or grantors. A legislative change requiring weekly database updating would also support fundamental taxpayer rights. Specifically, it would support donors and grantors' *right to be informed* of organizations that are tax exempt and eligible to receive tax deductible contributions. It would also support EOs' *right to quality service*, which includes a taxpayers' right to receive prompt assistance in their dealings with the IRS. Weekly database updating would also benefit the IRS by reducing the burden on the IRS's TE/GE phone line, as potential donors or grantors would no longer need to call the IRS to verify the exempt status of an organization not listed in the databases.

Although the IRS can update its EO Select Check database manually in between regular database updates and the National Taxpayer Advocate has directed TAS employees to require the IRS to do these manual updates within 24 hours, this *ad hoc* approach is not feasible or sustainable.²⁶ In addition, the IRS states that it cannot update the EO BMF manually.²⁷ Weekly database updating would limit the need for manual updates to emergency cases.

The IRS has previously moved to a more frequent updating interval, as Publication 78 data (that now appears on EO Select Check) used to be updated quarterly, but was moved to a monthly (with the exception of the gap period) updating schedule in January 2012.²⁸ However, due to the harm caused to many

22 IRM 21.3.8.12.13(3) (Nov. 16, 2012).

23 See IRS, *Exempt Organizations Select Check: Timing of Database Updates for Organizations Whose Exempt Status Is Reinstated*, available at <http://www.irs.gov/Charities-&-Non-Profits/Exempt-Organizations-Select-Check:-Timing-of-Database-Updates-for-Organizations-Whose-Exempt-Status-Is-Reinstated>. For detailed data about hold times, courtesy disconnects, and poor levels of service, see Most Serious Problem: *Exempt Organizations (EOs): The IRS's Delay in Updating Publicly Available Lists of EOs Harms Reinstated Organizations and Misleads Taxpayers*, *supra*.

24 See, e.g., Mathile Family Foundation, *FAQs – Tax Information*, available at <http://www.mathilefamilyfoundation.org/grantmaking/faqs/tax-information/>. These FAQs discuss in great detail the grant making restrictions on private foundations and that the foundation and its managers are subject to severe penalties if these rules are violated. The FAQs also advise potential grantees to **"make sure that the IRS BMF code currently represents your non-profit activities/operation (Form 990) and aligns with your Form 1023 filings and subsequent communications as approved by the IRS. When these separate designations do not agree, your organization is required to rectify discrepancies with IRS. Please consult with your tax advisor."** (bold and italic emphasis in original).

25 See IRS, *Exempt Organizations Select Check: Frequently Asked Questions*, FAQ #5, available at http://www.irs.gov/pub/irs-tege/faqs_eo_selectcheck.pdf.

26 In a February 2015 message to TAS employees, the National Taxpayer Advocate directed her case advocates to request manual updates within 24 hours if the IRS agrees an organization should be listed on EO Select Check as eligible to receive tax deductible contributions and to request an organization's removal from the automatic revocation list if this revocation was erroneous. TAS Wednesday Weekly, *Updates to Exempt Organizations "Select Check"* (Feb. 4, 2015).

27 TE/GE response to TAS research request (July 31, 2015). When asked why it cannot update the EO BMF manually, the IRS stated that the EO BMF is prepared by its IT personnel during a time frame available only once a month, "except in January IT is busy with other priorities and the EO BMF is not prepared." TE/GE response to TAS research request (Dec. 1, 2015).

28 IRM 25.7.6.3.5, *Cumulative List Indicator* (Jan. 1, 2015).

reinstated organizations, more frequent updating is now necessary and the IRS should implement such a change, which should not entail a significant additional cost or expenditure of resources. Because the IRS is unwilling or unable to make such a change, Congress should require it to do so.²⁹

EXPLANATION OF RECOMMENDATIONS

The proposals to amend IRC § 6033 to require the IRS to update its online EO databases more frequently would address IRS delays under the current process and their adverse impact on automatically revoked organizations that have been reinstated. A requirement that the IRS update its databases on a weekly basis would eliminate the current potential month or two updating delay and should not involve significant additional costs or resources. This would be in line with the IRS online weekly updating time frame for the Form 990-N (e-Postcard), which is the notice filed by small EOs.³⁰

Until the IRS can make appropriate programming changes, Congress should direct the IRS, through legislative history, to update EO Select Check manually for reinstated automatically revoked organizations. This short term fix will immediately alleviate the burden placed on these organizations. Once the IRS moves to a weekly updating schedule, the proposal recommends that Congress require the IRS to implement an emergency process that allows for manual online database updates within 24 hours of the restoration of exempt status. These changes would promote fair and efficient tax administration and protect two fundamental taxpayer rights, the *right to be informed* and the *right to quality service*.

29 In a response to a TAS information request regarding whether the IRS can update EO BMF and EO Select Check more frequently than the current monthly (except for January) intervals, the IRS stated that the program used to run these two extracts only runs every four weeks and “there is no way that the IT programmers can run the extracts more frequently.” TE/GE response to TAS research request (Dec. 1, 2015).

30 EOs that normally have annual gross receipts of not more than \$50,000 may file the Form 990-N rather than the more comprehensive Form 990 or Form 990-EZ. See Rev. Proc. 2011-15, 2011-3 I.R.B. 322.