Recent Tax and Regulatory Developments Relevant to Church Leaders

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The link above is an exclusive webpage created for National Association of Church Business Administration – Central Florida Chapter attendees. At this link, you will find a digital copy of this outline, which includes embedded links to additional information and articles on the topics presented, as well as the PowerPoint presentation.
1. **Update on the Commission on Accountability and Policy for Religious Organizations**
   - Background and context
   - Issues in the Commission’s first report and related recommendations
   - Highlights of the Commission’s final report – Government Regulation of Political Speech by Religion and Other 501(c)(3) Organizations

   The issue is particularly relevant currently…churches are getting more frustrated…Mike Huckabee was quoted recently suggesting that churches be willing to relinquish their exemptions if necessary

   - [Commission on Accountability and Policy for Religious Organizations](#)

2. **Trending in the Federal Charitable Giving Tax Policy Arena…Is the Handwriting on the Floor?**
   - Fiscal pressures remain at an all-time high.
   - Major tax reform is at the top of the agenda for both parties – but with very different approaches.
   - President Obama clearly favors raising income tax rates on higher-income taxpayers, which would result in less income available for “discretionary” spending or giving.
   - President Obama clearly favors reducing the tax benefit for charitable giving by high-income donors (limiting it to 28%, regardless of the person’s tax bracket, which can be over 40% under current tax law, counting new taxes added with healthcare reform law).
   - Republican plans generally favor keeping tax rates at or below current levels, and generally do not involve reductions of benefits for charitable giving.
   - Nonprofits of all types almost universally oppose reducing the tax incentives for charitable giving. The lobbying is heavy.
   - Under tax law effective for 2013, itemized deductions are limited again beginning in 2013. (High incomers can lose up to 20% of itemized deductions – but if they and their tax advisors correctly understand the law, it is not a disincentive for increased charitable giving.)

   - Some ideas under consideration include:
     - Changing the deduction to a credit (at various percentage levels)
     - Allowing non-itemizers to deduct charitable gifts
     - Applying a “floor” to the deduction
       (This option is referred to by some as a “win-win” option because some study results indicate, depending on how it is applied, that a “floor” could actually result in increased charitable giving and increased tax revenue to the federal government.)
Applying a combination of the above concepts

- Some members of Congress (e.g., Max Baucus (Democrat) and Dave Camp (Republican)) are pulling out the stops to pursue “comprehensive tax reform.”

- Max Baucus (Democrat – Chairman of Senate Finance Committee) and Orrin Hatch (Republican – Ranking Member of Senate Finance Committee) have proposed a “blank page” approach, requesting fellow senators to make the case to keep ANY existing exclusion, deduction, credit, or other tax benefit.
  - The mortgage interest deduction
  - Charitable contribution deductions
  - Tax-free employee benefits, such as employer-provided healthcare
  - Clergy housing
  - Anything!

- Everything is on the table, and the 2014 Congressional election results will likely have a profound impact on the nature of that reform, if it does not come before then.

- Congressional Budget Office Offers “Floor” Option to “Curtail the Deduction for Charitable Giving”

3. Wisconsin Federal Judge Rules Clergy Housing Allowance Exclusion Unconstitutional

- Federal Judge Rules Clergy Housing Allowance Exclusion Is Unconstitutional
- Five Takeaways from Friday’s Housing Allowance Ruling
  - Written by Richard R. Hammar

4. The Atheists are Suing! The Atheists are Suing!

Freedom from Religion Foundation has filed federal lawsuits requesting that the courts end special treatment for churches and clergy:

- Exemption from requirement to apply for 501(c)(3) status
- Exemption from filing Form 990
- Clergy housing exclusion
- Lack of enforcement by IRS of political campaign prohibition

Source: Freedom from Religion Foundation

Secular Coalition for America has sent letters to President Obama and key members of Congress requesting the end of religious organization “privileging” in the Internal Revenue Code and IRS action:

- Church Audit Procedures Act
- Allegedly lax enforcement by IRS
- Exemption from requirement to apply for 501(c)(3) status
- Exemption from filing Form 990

Source: Secular Coalition for America
5. **Small Employer Health Insurance Tax...Changes for 2014**

The health care reform act adopted in early 2010 provides for a new tax credit that applies for 2010 and subsequent years for smaller businesses and tax-exempt organizations that pay certain health insurance premium costs for employees. For eligible organizations, the credit is “refundable,” meaning that even if an organization has no taxable income, it may receive a refund for the credit.

**The credit was intended to encourage small employers to offer health insurance coverage for the first time or maintain coverage they already have.**

In general, the credit is available to small employers that pay at least half the cost of single coverage for their employees. But, for years after 2010, employers must pay a “uniform percentage” of the employee premiums (not less than 50%). The rules for applying the uniform percentage requirement are very complex (far too complex for a credit intended to help small employers). And, the IRS website guidance does not accentuate the uniform percentage requirement that is in the law. It causes one to wonder if the IRS has decided not to enforce that requirement.

For 2010 through 2013, the maximum credit is 35% of premiums paid during the year by eligible small business employers and 25% of premiums paid by eligible employers that are tax-exempt organizations.

In 2014, an “enhanced” version of the credit is available... increases to 50% of premiums paid by eligible small business employers and 35% of premiums paid by eligible employers that are tax-exempt organizations, but it will apply only if the employer acquires the coverage through new special exchanges. The IRS has not yet published detailed guidance on the enhanced version of the credit.

The credit is specifically targeted to help small businesses and tax-exempt organizations that primarily employ low and moderate income workers. It is generally available to employers that have fewer than 25 full-time equivalent (FTE) employees paying wages averaging less than $50,000 per employee per year. Because the eligibility formula is based in part on the number of FTEs, not the number of employees, many businesses will qualify even if they employ more than 25 individual workers.

The maximum credit goes to smaller employers — those with 10 or fewer FTEs — paying annual average wages of $25,000 or less.

**Special note for churches and religious organizations:** Guidance issued by the IRS states that in calculating average employee wages, the wages of a minister are excluded from the calculation (because the minister’s wages are not FICA wages). However, if the minister is an employee for income tax purposes, the minister may be counted in determining the number of employees to be included in the calculation. As a result of these provisions, an organization employing ministers could have average employee wages that are significantly lower than the organization might think would be the case at first glance.

Tax-exempt employers claim the credit by filing Form 990-T and including Form 8941, which should be filed after carefully reading the instructions. Again, a nonprofit organization that qualifies for the credit is entitled to receive it even if it does not have an income tax liability and even if it does not ordinarily file Form 990-T. Form 990-T is due the 15th day of the 5th month after an organization’s tax year ends (for organizations whose fiscal year is the calendar year, the due date is May 15).

- [The Small Business Health Care Tax Credit](#) – GuideStone® Financial Resources Summary
6. **Additional Medicare Tax**

Beginning in 2013, the Additional Medicare Tax of 0.9% applies to employee wages in excess of $200,000 for single individuals and $250,000 for married couples filing jointly.

The tax applies to the employee only – there is no employer matching tax like that which applies for the regular Medicare tax.

The tax applies to wages reportable as “Medicare Wages” on Form W-2. The tax also applies to net earnings from self-employment. According to IRS guidance, an employer is obligated to withhold the Additional Medicare Tax when Medicare wages exceed $200,000 during the taxable year. The employer is not responsible for determining the actual amount of the tax, if any, that an employee is actually required to pay. Rather, the employee settles up the actual liability on his/her Form 1040.

While relatively few nonprofit organizations have employees with wages in excess of $200,000, those who do should adapt to the new requirement in 2013, and should advise any affected employees.

For churches, since ministers are considered self-employed for purposes of Social Security and Medicare taxes, their church wages are not subject to the withholding requirement. However, members of the clergy who are subject to the self-employment tax and who have net self-employment income in excess of the thresholds are required to pay the additional tax as part of their Form 1040 filing. [Ministers who have elected out of Social Security coverage are not subject to the tax.]

More information and details are available on the IRS’s website.

http://tinyurl.com/addmedtax

7. **New Limits on FSA Contributions**

Additionally, new limits apply beginning in 2013 for employee salary reduction contributions to Health Flexible Spending Arrangements (Health FSAs). Previously not limited by law, employee salary reduction contributions to a Health FSA are limited to $2,500 annually per employee beginning in 2013. Employers that offer flexible benefit plans commonly referred to as “cafeteria plans” or “Section 125 plans” that include Health FSAs need to address the law’s new limit and, in all likelihood, will need to amend their plan documents to reflect the new limit.

8. **Effective for plan years beginning after 2013, employers may no longer pay or reimburse employees for individual health insurance policy premiums on a pre-tax basis.**

For many years, employers have been permitted to reimburse employees for or directly pay the cost of individual health insurance policy premiums and exclude such amounts from the employee’s gross income. However, recent Internal Revenue Service (“IRS”) guidance described below effectively eliminates these “employer payment plans” after 2013.\(^1\)

IRS Notice 2013-54, which was issued in September 2013, essentially prohibits the use of employer payment plans regardless of whether the individual insurance policy would be purchased through a Health Care Exchange or outside of a Health Care Exchange. The notice is effective for plan years beginning on or after January 1, 2014.

Notice 2013-54 provides that employer payment plans are group health plans subject to the market reform provisions of the Affordable Care Act (“ACA”), including the prohibition on annual limits and the requirement to provide certain preventive care services with no cost sharing. The notice confirms that because employer payment plans are considered to impose
an annual limit of the cost of the individual insurance policy purchased through the arrangement and do not provide preventive services without cost sharing in all instances, such plans will, by design, violate the requirements of the ACA. According to the IRS, employer payment plans cannot be integrated with the individual insurance policies purchased under the plans in order to satisfy these requirements. That means that employer payment plans will violate the requirements of the ACA even if the employees covered under the plan purchase individual insurance policies that comply with the ACA.

An employer is still allowed to establish an arrangement under which an employee may choose between cash or an after-tax amount to be applied toward health coverage. The employer is just not permitted to provide reimbursement on a pre-tax basis. In addition, the notice would permit an employer to establish a payroll practice of forwarding post-tax employee wages to an insurance company at the direction of the employee, as long as the requirements described in the notice are satisfied.

Accordingly, for plan years beginning on or after January 1, 2014, employers will need to either eliminate employer payment plans or modify such arrangements to reimburse employees for health coverage on an after-tax basis.

1 It does not appear that the guidance would prohibit employers from establishing employer payment plans that reimburse premiums for HIPAA-excepted coverage, such as limited-scope dental or vision coverage.

The content regarding Notice 2013-54 was prepared for BMWL by attorneys Danny Miller and Allison McGrath Gardner of Conner & Winters, LLP.

9. IRS Offers New $500 Carryover Option for FSAs
   - IRS Modifies “Use-It-or-Lose-It” Rule for FSAs

10. New W-2 Health Coverage Reporting Requirements
    The Affordable Care Act adopted in 2010 requires employers to report the cost of coverage under an employer-sponsored group health plan on Forms W-2 issued to employees. As a result of complaints and concerns expressed by employers, implementation of the law was deferred to 2012, and for 2012 and following years, it only applies to larger employers (for now). Employers (including nonprofits) that filed 250 or more Forms W-2 in the prior year (e.g., 2011) are required to report on the following year’s (e.g., 2012’s) W-2s of their employees certain information about the cost of group health care coverage sponsored or provided by the employer. The information is required to be reported for the employee’s information purposes only, and the requirement to report the information does not mean that the benefits are taxable.

    According to the IRS, “The purpose of the reporting requirement is to provide employees useful and comparable consumer information on the cost of their health care coverage.”

    ERISA-exempt self-insured church plans are excluded for now (regardless of size).

    The reporting requirement does not apply to smaller organizations until the IRS issues additional guidance. The IRS has stated that such guidance will be issued with at least six months’ advance notice.

    The IRS recently updated its guidance for applying the new reporting requirement on its website, adding more clarity and information.

11. **New Fee Applies to Employers with Self-Insured Health Plans, Including Some HRAs (PCORI Fees)**

Much of the focus regarding compliance with the Affordable Care Act (ACA) has been on the requirement that employers with 50 or more full-time employees (including full-time equivalents) offer health insurance coverage to their full-time employees or pay a penalty – a requirement for which the effective date has been postponed until January 1, 2015. Another provision affects certain employers that offer self-insured health and welfare plans (including certain health reimbursement arrangements (HRAs)), and if applicable, it should have been addressed by July 31, 2013 for organizations whose plan years ended in late 2012.

ACA created the Patient-Centered Outcomes Research Institute (PCORI), a private, nonprofit corporation, to conduct research and evaluate health outcomes, clinical effectiveness, risks, and benefits of medical treatments, etc. ACA requires PCORI to be funded, in part, by a fee collected from health plan providers. For fully insured plans, the fee will be paid by the health insurance issuer (the insurance company). For self-insured plans, the plan sponsor (employer) is required to pay the fee.

**What types of plans are covered?**

The guidance for applying the PCORI fees is new and not very “user-friendly” – especially as it relates to common employer-sponsored self-insured plans. The limited official guidance that exists supports the view that the most common example for most employers of a self-insured health plan to which the PCORI fee may apply is a health reimbursement arrangement (HRA) – a plan under which the employer reimburses or pays certain health care expenses from its own assets. The guidance indicates that the fee does not apply to most flexible spending accounts (FSAs) or to Health Savings Accounts (HSAs), and it does not apply to stand-alone vision and dental plans.

In some cases, it may be necessary to consult special benefits counsel to make a determination of whether the fees apply. Given the fact that the fee is rather low-cost item for most self-insured plans sponsored by nonprofit employers, and filing is relatively simple, some organizations simply opt to pay the fee with respect to plans for which applicability is uncertain. The costs and effort required to make a determination where applicability is uncertain may far outweigh the cost of simply paying the fee.

**Form for reporting and due date**

For self-insured plans to which the fee applies, the PCORI fee is reported on Form 720, which is to be filed by the plan sponsor (employer) by July 31 of the calendar year immediately following the last day of the plan year. The fee applies to plan years ending after September 30, 2012 and before October 1, 2019. For applicable self-insured plans with plan years ending after September 30, 2012 and before January 1, 2013, Form 720 was due July 31, 2013. Even though Form 720 is designed to accommodate quarterly filings, the PCORI fees are only due annually, and no estimated payments (advance payments) are required.

**Calculating the fee**

The amount of the PCORI fee applicable for plan years ending on or after October 1, 2012, and before October 1, 2013, is $1 multiplied by the “average number of lives covered under the plan for the plan year” (the fee will be increased to $2 the following year and adjusted thereafter based on increases in the projected per capita amount of National Health Expenditures).

The individuals taken into account in determining the “average number of lives covered under the plan for the plan year” include employees, spouses, and dependents that are covered under the plan. However, a special rule applies with respect to covered HRAs and FSAs if the employer does not sponsor other types of self-insured plans. If that is the case, an employer may treat the HRA or FSA as covering only one life per participant, and is not required to count spouses and dependents. As stated above, the fee will not apply to most FSAs.
The average number of lives covered under the plan is determined annually after the end of the plan year under one of three methods provided in the Regulations. The three allowed methods are:

- The actual count method;
- The snapshot method; and
- The Form 5500 method.

A simplified summary of the three methods is provided below. More specific details regarding the calculation methods are provided in the Regulations.

**Actual count method**

Under the actual count method, the employer adds the actual number of covered persons on each day of the plan year and divides by the number of days in the plan year.

**Snapshot method**

Under the snapshot method, the taxpayer picks a day or days from each calendar quarter and adds the actual number of covered persons on each of those days, then divides by the number of days selected as the snapshot.

**Form 5500 method (for plans that file the Form 5500)**

Under the Form 5500 method, the taxpayer uses the number of participants (not including spouses and dependents) reported on the Form 5500, Annual Return/Report of Employee Benefit Plan filed for that plan year provided it is filed no later than the due date for the PCORI fee. If the plan offers coverage for the employee only (i.e., self-only coverage), the number is the beginning-of-the-year participant count plus the end-of-the-year participant count, divided by two. If the plan offers dependent coverage, the number is the beginning-of-the-year participant count plus the end-of-the-year participant count (not divided by two).

**Special rule for first year**

For the first year of the fee (plan years beginning before July 11, 2012 and ending on or after October 1, 2012), a plan sponsor (employer) may determine the average number of covered lives using “any reasonable method.”

The IRS has published information on its website with guidance related to the PCORI fees. [http://www.irs.gov/uac/Newsroom/Patient-Centered-Outcomes-Research-Institute-Fee](http://www.irs.gov/uac/Newsroom/Patient-Centered-Outcomes-Research-Institute-Fee)

- New Fee Applies to Employers with Self-Insured Health Plans Including Some HRAs

12. **Worker Classification Audits – The Next Big Thing in Light of Healthcare Reform**

**Large employers** – attempting to avoid the employer mandate penalty for specific workers by treating them as independent contractors

**Employers on the edge of becoming large** – attempting to avoid classification as a large employer by treating workers as independent contractors

**Note** – misclassified workers will have a strong incentive to report their misclassification to the IRS. They may file Form SS-8 to have the IRS rule on their classification and Form 8919 to claim that the employer did not withhold taxes.
Multiple-entity employers – attempting to avoid classification as a large employer through the use of multiple entities

The stakes are VERY high, and the IRS will be zeroing in on this issue with force.

Avoiding Significant Liability under the IRS Settlement Program

On September 21, 2011, the IRS announced a new program to permit employers to voluntarily reclassify workers as employees for federal employment tax purposes in cases where the employer is concerned that workers have been improperly treated as independent contractors. The “Voluntary Classification Settlement Program” (VCSP) provides significant relief from federal employment taxes for eligible employers that agree to treat workers as employees prospectively.

Generally, in order to qualify for participation in the VCSP, an employer:

• Must have consistently treated the workers as nonemployees;
• Must have filled Forms 1099 for such workers a required for the three preceding calendar years;
• Must not have any dispute with the IRS as to whether the workers are nonemployees or employees for federal employment tax purposes
• Must not be under an employment tax audit by the IRS; and
• Must treat the workers as employees for all subsequent year.

If an employer chooses to participate in the VCSP and the IRS agrees to allow it, then the employer:

• Must pay 10% of the employment tax liability that may have been due on compensation paid to the potentially misclassified workers for the most recently completed tax year using special rules;
• Will not be liable for any interest and penalties on the liability; and
• Will not be subject to an employment tax audit with respect to the worker classification of the workers for prior years.

If an employer wishes to participate in the VCSP, an application must be submitted using Form 8952 at least 60 days before the date that the employer would begin classifying these workers as employees. For example, if the employer wishes to begin classifying these workers on January 1, 2014, then the application would need to be filed on or before November 2, 2013.

The IRS has not indicated how long the VCSP will be available.

This program presents a very favorable opportunity to correct worker misclassification.

Participation in this program could be very beneficial and cost-effective for employers that may have been improperly treating workers as independent contractors. The opportunity to avoid an audit of past worker classification liabilities and settle them for 10 cents on the dollar with no penalties or interest is truly remarkable. BMWL strongly urges its clients with concerns about past worker classification liabilities to carefully consider applying for settlement under the VCSP.
Additional information about the program is available in Announcement 2012-45 and on the IRS website:

- Voluntary Classification Settlement Program (VCSP)
- IRS Worker Classification Settlement Program Requirements Relaxed
- With New Health Care Laws, Expect Tough Enforcement of Worker Classification

13. Direct Charitable IRA Distribution Exclusion Status Update

14. Return of the “Pease” Limitation

How the “Pease” Limitation Really Works

- Reduction of itemized deductions for higher-income taxpayers
- Provision named after the late Congressman Don Pease from Ohio, who invented it
- It is essentially an increase in the income tax rate for higher-income taxpayers (Urban Institute-Tax Policy Center).
- Some writers and financial professionals have misinterpreted and misinformed their constituents about the effects of the Pease limitation.
- It is not a disincentive for increased charitable giving.
- For MFJ taxpayers with AGI over $300,000 ($250,000 for single taxpayers), most itemized deductions are reduced by 3% of the excess of AGI over the base amount. [Medical expenses are excluded.] (But cannot reduce itemized deductions by more than 80%)

Example
Bill and Linda Thomas have adjusted gross income of $350,000 for 2013. They gave $40,000 to charity, had $15,000 in mortgage interest, and paid real estate taxes of $5,000. Total itemized deductions = $60,000.

Since their AGI exceeds the MFJ base of $300,000 by $50,000, their itemized deductions are reduced by 3% of the excess, or $1,500. (Note that the $1,500 is nowhere near 80% of their itemized deductions.)

- The $1,500 reduction is a function of their income, not their deductions.
- Their itemized deductions would be reduced by $1,500 if their charitable contributions were zero or $100,000.

Only in highly extraordinary cases (very high AGI and very low itemized deductions) will a taxpayer not get the full tax benefit of increased charitable giving due to the Pease limitation.

15. New Simplified Option for Deducting Home Office Expenses

The Internal Revenue Service announced earlier this year a simplified option that many owners of home-based businesses and some home-based workers may use to figure their deductions for the business use of their homes.
The new optional deduction, capped at $1,500 per year based on $5 per square foot for up to 300 square feet, will reduce the paperwork and recordkeeping burden on small businesses by an estimated 1.6 million hours annually.

"This is a common-sense rule to provide taxpayers an easier way to calculate and claim the home office deduction," said Acting IRS Commissioner Steven T. Miller. "The IRS continues to look for similar ways to combat complexity and encourages people to look at this option as they consider tax planning in 2013."

The new option provides eligible taxpayers an easier path to claiming the home office deduction. Currently, they are generally required to fill out a 43-line form (Form 8829) often with complex calculations of allocated expenses, depreciation and carryovers of unused deductions. Taxpayers claiming the optional deduction will complete a significantly simplified form.

Though homeowners using the new option cannot depreciate the portion of their home used in a trade or business, they can claim allowable mortgage interest, real estate taxes and casualty losses on the home as itemized deductions on Schedule A. These deductions need not be allocated between personal and business use, as is required under the regular method.

Business expenses unrelated to the home, such as advertising, supplies, and wages paid to employees are still fully deductible.

Current restrictions on the home office deduction, such as the requirement that a home office must be used regularly and exclusively for business and the limit tied to the income derived from the particular business, still apply under the new option.

The new simplified option is available starting with the 2013 return most taxpayers file early in 2014. Further details on the new option can be found in Revenue Procedure 2013-13.

16. IRS Still Doesn’t Know What a “High-Level Treasury Official” Is…Not Launching New Church Tax Inquiries

Federal tax law permits the IRS to initiate a church inquiry or examination so long as certain criteria are carefully met. The criteria for a church tax inquiry include a requirement that a “high-level Treasury official” must determine, based on written evidence, that the church is not exempt, that it has a liability for unrelated business income tax, or that it has otherwise engaged in taxable activities.

Subsequent to a national restructuring of its operations, the IRS designated a particular official as its “high-level Treasury official” with authority to make the required determination. However, a federal court ruled in 2009 that the official designated by the IRS did not meet the statutory definition of a high-level Treasury official. The IRS has not yet rectified the issue and reports indicate that the IRS has ceased inquiries and examinations of churches until the matter is resolved. The IRS claims to be nearing completion of new regulations addressing the matter.


The Department of Homeland Security has issued a new version of Form I-9, the form employers are required to complete to document the identity and employment eligibility of workers. The new form is available at:

The new version of the form must be used now. Older versions of the form are not acceptable for use after May 7, 2013.

**Homeland Security Issues New I-9 Form**

18. **IRS Issues “Fix-It” Guide to Correct 403(b) Plans**

Given the frequency with which the IRS has identified compliance issues in connection with 403(b) retirement plans commonly used by churches and other 501(c)(3) organizations, the IRS has issued a “Fix-It” Guide to help nonprofit employers and plan administrators address common compliance issues.

The new guide is available at:


19. **IRS Finally Says Officially that Contributions to Disregarded Single-Member LLCs (DSMLLCs) of 501(c)(3) Organizations Are Deductible**

(Consistent with Previous Guidance Related to Grants by Private Foundations to DSMLLCs)

The IRS recently issued long-awaited guidance regarding the tax treatment of contributions made to disregarded single-member limited liability companies (DSMLLCs) owned and controlled by nonprofit 501(c)(3) organizations. Nonprofit organizations sometimes utilize single-member limited liability companies (SMLLCs) to own property or conduct activities for risk management purposes. While generally treated as a separate legal entity under state law for liability purposes, a SMLLC may be “disregarded” under federal tax law – meaning that for federal income tax purposes, it is treated as if it were simply a division of its owner (the “single member”) and not a separate entity – hence, the term “disregarded.”

Given the federal tax treatment of DSMLLCs, logic would dictate that contributions to a DSMLLC whose single member is a 501(c)(3) organization would be treated as contributions to the 501(c)(3) organization for federal tax purposes. However, the IRS has not issued formal guidance to that effect – until now. Notice 2012-52 states that charitable contributions made to a DSMLLC of a 501(c)(3) organization are treated as having been made to the 501(c)(3) organization, and the 501(c)(3) organization is considered the donee for purposes of acknowledgments (donor receipts) for contributions. The IRS also notes, “To avoid unnecessary inquiries by the Service, the charity is encouraged to disclose, in the acknowledgment or another statement, that the SMLLC is wholly owned by the U.S. charity and treated by the U.S. charity as a disregarded entity.”

The IRS’s new guidance is consistent with guidance published in 2010 stating that a grant by a private foundation to a DSMLLC of a 501(c)(3) public charity is generally treated as a grant by the foundation directly to the public charity.

Source: IRS Notice 2012-52

20. **New Florida Law Provides Protection for Nonprofits from “Clawbacks” of Charitable Contributions under Fraudulent Transfer Law**

One of the more insidious risks nonprofit organizations face with respect to charitable contributions is the risk that contributions received from a particular donor may later be ruled “fraudulent transfers” or “fraudulent conveyances” under federal bankruptcy law or applicable state law. The nonprofit organization that receives the contributions may have no idea that a donor is facing bankruptcy or that a donor may have obtained the donated funds in an ill-gotten manner (such as a Ponzi scheme). If such conditions are present, a bankruptcy trustee, creditors of a donor, or law enforcement authorities may assert that contributions made to the nonprofit organization were “fraudulent transfers” and, as a result, must be returned by the nonprofit organization to a receiver to pay the creditors or to be used for other purposes. The laws that require such refunds are often referred to as “clawback” laws.
Clawbacks of charitable contributions can be particularly damaging to an organization – especially in cases where the contributions are large and the organization has spent the money on operations or assets before learning of the clawback claim. Accordingly, we generally advise our clients to carefully evaluate large or unusual gifts…and if there is any concern about the possibility of a clawback claim, consult with legal counsel and consider holding the assets for a period until it is deemed safe by the organization’s legal counsel to spend them.

Numerous instances of clawbacks of charitable contributions occurred during the Great Recession and they still occur today.

In response to concerns about this issue, the Florida Legislature adopted a new provision in the law, effective July 1, 2013, that provides some protection for nonprofit organizations from clawback claims in certain circumstances.

Following is an excerpt from the Legislative staff analysis summarizing the provisions of House Bill 95:

The bill creates a statutory defense in the Florida Uniform Fraudulent Transfer Act (FUFTA) to protect qualified charitable or religious groups against clawback actions that attempt to recover charitable contributions, if the recipient organization received the contribution in good faith. Under current law, creditors have a statutory remedy against debtors known as a “clawback” action which require a debtor’s fraudulently transferred property to be surrendered back to the creditors or fraudulently incurred debts to be voided.

The bill also defines “charitable contribution” and “qualified religious or charitable entity or organization.” The bill states that a natural person’s charitable contributions are fraudulent transfers if they were received within 2 years before the commencement of a FUFTA, bankruptcy, or insolvency proceeding, unless: a) the transfer was made consistent with the debtor’s practices in making charitable contributions, or b) the transfer was received in good faith and did not exceed 15% of the debtor’s gross annual income for the year in which the transfer was made. These requirements parallel those found in the Bankruptcy Code’s protection for charitable contributions against a bankruptcy trustee’s clawback action.

Source: Chapter 2013-189, Florida Laws, Committee Substitute for House Bill 95, as passed by the Florida Legislature and approved by Governor Scott

- New Florida Law Provides Protection for Nonprofits from “Clawbacks” of Charitable Contributions under Fraudulent Transfer Law
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