

Federal Tax Information

Income Tax Issues for Exempt Organizations

As long as there have been federal income taxes, there have been organizations that Congress has exempted from those taxes. Congress decided that the work of some organizations was so important it wanted them to keep their funds for their work, rather than paying part to the federal government. Many Posts erroneously assume that, because they are a VFW Post and are non-profit, they are automatically exempt from federal taxes. That is not the case. The IRS has established some specific procedures for obtaining and maintaining exempt status, and that procedure must be followed.

Congress established several categories of organizations that are exempt from federal income taxes. Those categories are usually referred to by the sections of the **Internal Revenue Code (IRC)** that grant tax exempt status. The more common ones are:

- ***Section 501 (c) (3)** : charitable, educational, and religious organizations;
- ***Section 501 (c) (4)** : social welfare organizations;
- ***Section 501 (c) (7)** : social clubs.

Veterans of Foreign Wars National Headquarters has obtained its exemption under a special veterans service organization provision, Section 501 (c) (19). The National Headquarters exemption does not cover other units. In most cases, the Department Headquarters has obtained a “group exemption” (discussed below) that covers Posts in the Department.

If your Post is not covered under a Group Exemption and has not applied for and been granted a separate exemption, you are urged to do so. To obtain a separate exemption, a Post must file an IRS **Form 1024**. A Form 1024 can be obtained by contacting a local IRS office. VFW Posts should be eligible for exemption under section 501 (c) (19), provided they have properly requested this exemption. Exemption under Section 501(c) (19) offers the most flexibility, because the exemption offers the broadest exempt purposes. Section 501 (c)(19) status may be the only exemption available if your Post operates a canteen. It is highly recommended that you seek exemption under 501(c)(19). To obtain additional information concerning procuring and maintaining tax exempt status for your Post, review IRS Publication 557, “Tax Exempt Status for Your Organization”, or contact your local Internal Revenue Service office. It is also strongly recommended that you consult with an accountant, attorney or other tax professional for advice concerning the appropriate exemption and compliance with IRS requirements.

Group (“Blanket”) Exemptions

You should check with your Department Headquarters to see if it has been issued a group exemption letter that covers your Post. If it has, you are not required to file a separate application for exemption on Form 1024 unless your Post no longer wants to be included in the group exemption letter or is no longer eligible for exemption under the statutory section upon which the group exemption was issued. However, to be included in a group exemption, each Post must authorize the Department Headquarters to include it in the group. The authorization must be signed by a duly authorized officer of the Post and retained by the Department Headquarters for which the group exemption is in effect.

To maintain a group exemption, the Department Headquarters must submit annually to the Internal Revenue Center with which it files its information returns the following information:

1. Data regarding all changes in purpose, character or method of operation of the Posts included in the group exemption:
2. Lists of the Posts fitting the following three categories:
 - A. Posts that have changed their names or addresses during the year,
 - B. Posts no longer to be included in the group exemption, and
 - C. Posts to be added to the group exemption because they are newly formed or because they have recently authorized the Department Headquarters to include them.
3. Information required to be submitted by the Department Headquarters on behalf of Posts to be included in the initial group exemption is required for the new Posts to be added to the exemption.

Submission of this information does not relieve the Department Headquarters or any Posts from supplying any additional information which the IRS requires in order to determine whether the conditions for continuing the exemption are being met. Additionally, inclusion in a group exemption does not relieve the Post of any obligation it has to file income and payroll tax returns or pay taxes.

Most Departments have obtained a group exemption under Section 501(c)(19). As the result of some recent IRS recommendations, those Departments that have group exemptions under Section 501(c)(4) are in the process of submitting applications for group exemption under Section 501(c)(19). You may be asked to provide information to support that application. Failure to provide that information may result in your Post losing its group exemption and require that you file for a separate exemption

Return of Organization Exempt From Income Tax (Form 990)

Organizations exempt from income tax under Section 501 (c) of the IRC are generally required to file Form 990 by the 15th day of the fifth month following the close of their accounting year. If the organization's annual gross receipts are normally more than \$25,000, the organization must file Form 990 or 990-EZ. With the passage of the Pension Protection Act of 2006, smaller tax-exempt organizations with gross receipts under \$25,000 are now required to electronically file Form 990-N, also called the e-Postcard, with the IRS annually. Organizations that do not file Form 990-N, or an information return Form 990 or 990 EZ for three consecutive years, will have their tax-exempt status revoked as of the filing due date of the third year.

Gross receipts are considered to be normally less than \$25,000 if the organization is:

1. Up to a year old and has gross receipts of \$37,500 or less during the first tax year;
2. Between one and three years old and has averaged \$30,000 or less in gross receipts during each of its first two tax years; or
3. Three years old or more and has averaged \$25,000 or less in gross receipts for the immediately preceding three tax years.

If annual gross receipts are normally more than \$25,000, the organization must file Form 990 or 990-EZ. For tax years beginning in 2008, if an organization has gross receipts less than \$1,000,000 and total assets at the end of the year less than \$2,500,000, it may file form 990-EZ. However, if either gross receipts or assets are above those limits, Form 990 must be filed.

For purposes of filing requirements, gross receipts include: total contributions; gifts and grants; program service revenue; membership dues and assessments; gross investment income (including interest, dividends, gross rents, and other investment income); gross income from the sale of assets other than inventory; gross income from special fundraising events; gross sales net of return allowances, and any other revenue.

IRS regulations require that all tax-exempt organizations make both their Application for Exemption and 990's for the last three years available for public inspection at their principal office and provide copies in response to written requests, subject to the payment of reasonable fees. There are substantial penalties for violation of these regulations.

Exempt Organization Business Income Tax Return (Form 990-T)

An exempt organization may also be required to file Form 990T if the organization's gross income from business unrelated to the organization's exempt purposes is \$1,000 or more. The obligation to file Form 990T is in addition to the obligation to file an Informational Return (Form 990). Unrelated business income tax (**UBIT**) is defined as gross income derived by an organization from any unrelated trade or business regularly carried on by it, and not substantially related to its exempt purposes. While the IRS considers many factors in determining whether the activity is unrelated trade or business, an important factor is the degree to which the activity unfairly competes with taxable businesses. Generally, the tax applied to unrelated business income does not apply to:

- A. Dividends;
- B. Interest;
- C. Royalties;
- D. Rents (other than certain rents on property acquired with borrowed funds); and
- E. Gains from sales of assets.
- F. Member's dues submitted to National and Department

The rules applicable to unrelated business income can be complicated, depending upon the nature and extent of your Posts activities. If you are unsure about your Post's obligation to file a 990T or report certain types of income, you are encouraged to consult with a tax professional concerning these important issues. 990T's are not subject to public disclosure.

Gambling/Bingo

The Internal Revenue Service has been very active in recent years with respect to gambling activity by tax exempt organizations. This includes such things as pull tabs, machines, raffles, etc. Such activities may be subject to Unrelated Business Income Tax (UBIT) and may also be subject to the Federal Wagering Excise Tax and Federal Occupational Tax. The rules with respect to gaming income are also complicated and you should consult IRS Publication 3079 for details. You should also consult a professional tax advisor.

The Internal Revenue Code (IRC) contains a specific provision exempting Bingo proceeds from unrelated business income tax where state and local law permits such games to be carried on by non-profit organizations and these organizations do not compete with taxable entities. This exception applies to bingo games even though they are regularly carried on with paid workers.

Section 513 (f) of the IRC (defining unrelated trade or business) specifically provides:

(f) CERTAIN BINGO GAMES.-

- (1) In general, the term 'unrelated trade or business' does not include any trade or business which consists of conducting bingo games.
- (2) Bingo Game Defined.-For purposes of paragraph (1), the term 'bingo game' means any game of bingo-
 - (A) of a type in which usually -
 - (i) the wagers are placed,
 - (ii) the winners are determined, and
 - (iii) the distribution of prizes or other property entry is made in the presence of all persons placing wagers in such game,
 - (B) the conducting of which is not an activity ordinarily carried out on a commercial basis, and
 - (C) the conducting of which does not violate any state or local law.

The Internal Revenue Service has taken the position that the Bingo exemption applies only to regular Bingo and does not apply to "instant" bingo, pull tabs or other gaming, even if it is conducted during a Bingo session.

Department of the Treasury Bureau of Alcohol, Tobacco & Firearms Advisory

If your Post operates a canteen or otherwise sells alcoholic beverages on a regular basis, the Post may be required to pay a federal Special Occupational Tax of \$250 and obtain a Special Tax Stamp on or before July 1. Failure to pay the tax could result in a substantial fine. The law requires every retail dealer in liquors, other than a limited retail dealer, to file a special tax return (ATF Form 5630.5) and pay the special tax to the Bureau of Alcohol, Tobacco and Firearms. The term "limited retail dealer" includes a veterans organization making sales of distilled spirits, wine or beer on the occasion of any kind of entertainment, dance, picnic, bazaar or festival held by it, if the organization is not otherwise engaged in business as a dealer. The ATF generally takes the position that a "limited retail dealer" is one that occasionally serves alcoholic beverages in connection with an event but that a regularly conducted clubroom would not qualify. Title 27 CFR, part 194 contains the complete regulations concerning this tax. ATF has published a booklet, ATF P 5170.2, which addresses this issue. The booklet can be obtained from the District Director (Regulatory Enforcement), Bureau of Alcohol, Tobacco and Firearms for your region.

Warnings for VFW Posts

1. Don't assume your Post is exempt. Check with your Department to see if they have your Post under a group exemption. If not, obtain your own exemption.
2. Know which section of the Internal Revenue Code your Post is exempt under and know what the requirements are to maintain the exemption.
3. Remember that Ladies and Mens Auxiliaries are separate organizations. They may not be exempt under the Post exemption.

4. If a Post has “social members”, the Post is not in compliance with the By-Laws and the Post may not be in compliance with the requirements for exemption under 501 (c) (19). Member documentation (such as member applications) should be maintained and up-to-date.
5. Non reporting and non-payment of payroll taxes for Post employees not only puts your Post at risk with the IRS, but also puts the individual Post officers at risk.
6. Become acquainted with what constitutes Unrelated Business Income and ensure it is reported properly and taxes are paid if required.

Payroll Taxes

Tax exempt status does not relieve the Post of the obligation to file returns and pay federal and state payroll taxes (withholding, FICA, FUTA, etc.). If payments are being made to individuals for services rendered to the Post or any club room or any facility operated by the Post, it is likely that returns must be made and taxes paid. Failure to do so can result in severe tax consequences to the individual, the Post and responsible Post Officers.

IRS PUBLICATION 3386

The IRS has issued a very useful publication entitled Tax Guide for Veterans' Organization, Publication 3386. It is highly recommended that you obtain a copy and consult it when questions arise concerning your Posts' tax obligations. A copy can be downloaded from the IRS website at irs.gov/pub/irs-pdf/p3386.pdf