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Unusual Tax-Exempt Reporting in an Unusual Year

Presented by:

Shannon T. Forkin, CPA, CGMA – Tax Partner

Marissa A. Spring – Tax Senior

Dannible & McKee's Virtual Nonprofit Conference

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In this session you will gain additional knowledge on tricky reporting areas that NPOs may encounter. We will discuss ways that organizations can document their activities and prepare their records to eliminate any surprises and be ready for the year-end reporting requirements.

What are we covering today?

Paycheck Protection Program Round 2.

Changes and other items to be aware of:

- 1099 Reporting;
- Charitable Contributions Deduction;
- Private Foundation Tax Rate;
- Auto Revocation; and
- Electronic Filing.

Events during COVID-19, including gaming and raffles.

In-Kind Contributions.

Additional Reminders.

Resources.

Polling Question

Did your organization receive funds from PPP Round 1?

- a) Yes;
- b) No; or
- c) I don't know what this is.

PPP Round 2

On December 27, 2020 President Trump signed the Economic Aid Act into law to provide continued assistance to individuals and businesses that have been financially impacted by the ongoing coronavirus pandemic.

Authorizes the SBA to guarantee Paycheck Protection Program Second Draw Loan, under generally the same terms and conditions available under the PPP Small Business Act.

PPP Round 2

Re-opens the program for First Draw Applicants.

Last day to apply is March 31, 2021.

Streamlined the forgiveness process for PPP loans of less than \$150k.

Simplified Forgiveness

For PPP loans of up to \$150,000, forgiveness is now simplified.

- Only required to sign and submit a one-page certification. The certification will require the borrower to provide a description of the number of employees that the borrower was able to retain because of the PPP loan, the estimated amount of the PPP loan proceeds spent on payroll costs, and the total PPP loan value. The certification also will include an attestation that the borrower has complied with the requirements of the PPP loan.
- The SBA may review and audit loans that fall within this category. The SBA may also modify the amount of the PPP loan or the amount forgiven if it finds fraud, ineligibility, or other material noncompliance.
- Borrowers of these loans must retain records to prove compliance for four years with respect to employment records, and three years with respect to all other records.

PPP Round 2

Eligibility Criteria:

- Non-profit organizations – 501(c)(3) .
- Eligible 501(c)(6) nonprofit trade organizations and business leagues
- A nonprofit public broadcasting entity with a trade or business under NAICS 511110 or 5151.
- Generally, must have under 300 employees.
- In operation on or before February 15, 2020 and is still in operation.
- Demonstrate a 25% reduction in gross receipts .
- Has received a First Draw PPP Loan, and has used or will use the full amount of their first PPP loan before Second Draw is disbursed.

PPP Round 2

25% reduction in gross receipts:

- Must demonstrate a 25% reduction in gross receipts in any quarter of 2020 relative to the same 2019 quarter.
- A reduction in annual receipts of 25% or greater in 2020 compared to 2019.
- If applicant was not in existence during 2019, but was in operation on February 15, 2020, they must demonstrate a 25% reduction from the gross receipts of the entity during the first quarter of 2020 compared to the second, third, or fourth quarters of 2020.

PPP Round 2

Gross receipts:

- Gross receipts include all revenue in whatever form received or accrued (in accordance with the entity's accounting method) from whatever source, including from the sales of products or services, interest, dividends, rents, royalties, fees or commissions, reduced by returns and allowances. Generally, receipts are considered 'total income' plus 'cost of goods sold,' and excludes net capital gains or losses as these terms are defined and reported on IRS tax return forms.
- For an eligible nonprofit organization, a veteran's organization, an eligible nonprofit news organization, an eligible 501(c)(6) organization or eligible destination marketing organization, gross receipts means gross receipts within the meaning of Section 6033 of the Internal Revenue Code of 1986.
- Gross receipts also do not include funds received from the initial PPP loan.

PPP Round 2

Loan Amounts:

- 2.5 average monthly payroll (3.5 average for 72 NAISC Codes).
- Maximum \$2 million.

PPP Round 2

Forgiveness:

- 60% of loan proceeds must be used for eligible payroll expenses to qualify for forgiveness.
- Borrowers choose a covered period for loan forgiveness purposes. The period selected must begin on the date of the origination and end on such date selected by the borrower that occurs during the period beginning on the date that is eight weeks to 24 weeks after such origination date.
- Up to 100% of the loan is eligible for forgiveness.
- Unforgiven balances – 5-year term, 1% rate, no collateral, no personal guarantee.

PPP Round 2

Eligible Expenses:

In addition to using PPP loans for payroll costs (60%), covered mortgage service and rent, and utility payments, PPP loan proceeds can be used for these new categories of expenses:

- *Covered operations expenditures* – payments for business software or cloud computing services that facilitate business operations; product or service delivery, processing, payment, or tracking payroll expenses; human resources, sales and billing functions; or accounting or tracking or supplies, inventory, records and expenses.

PPP Round 2

- *Covered property damage costs* – costs related to property damage, vandalism, or looting from public disturbances during 2020 that were not covered by insurance or other compensation.
- *Covered supplies costs* – expenditures by the borrower to a supplier of good that are (a) essential to the operation of the business at the time of such expenditure; and (b) made pursuant to a contract, order or purchase order in effect before the borrower's covered period or, in the case of perishable goods, during the borrowers covered period.

PPP Round 2

- *Covered worker protection expenditures* - any operating or capital expenditures that facilitate the adaption of the borrower's business activities to comply with The U.S. Department of Health and Human Services ("HHS"), Centers for Disease Control and Prevention ("CDC"), or Occupational Safety and Health Administration ("OSHA") requirements (or equivalent state or local requirements), with respect to COVID-19 during the period beginning March 1, 2020 and ending on the date the national emergency declaration ends. These expenditures include the costs of purchasing, maintaining or renovating assets that create or expand drive-through window facilities; air or air pressure ventilation or filtration systems; physical barriers like sneeze guards; expansion of additional indoor, outdoor or combined business spaces; health screening capabilities; or the purchase of certain personal protective equipment ("PPE"). However, the definition excludes residential real property or intangible property.

PPP Round 2

Required Documentation:

- Second Draw Borrower Application Form (SBA Form 2483-SD).
- Documentation required to substantiate an applicant's payroll cost calculations is generally the same as documentation required for First Draw PPP Loan.
- No additional documentation required if the applicant uses the same 2019 figures to determine Second Draw and uses the same lender as First Draw.
- Loans with principal amount less than \$150k do not have to submit documentation of 25% revenue reduction at time of application.

PPP Round 2

Application Certifications:

- Current economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant.
- The funds will be used to retain workers, and maintain payroll, or make payments for mortgage interest, rent, utilities, covered operations expenditures, covered property damage costs, covered supplier costs, and covered worker protection expenditures as specified under the Paycheck Protection Program Rules.
- The applicant has not and will not receive another loan under the Paycheck Protection Program (this does not include Second Draw loans).
- Information provided is true and accurate in all material respects.

Employee Retention Tax Credit (ERTC)

The new law extends the CARES Act credit for retaining employees to July 1, 2021 and expands the usefulness of the refundable payroll tax credit by:

- Reducing the required decline in gross receipts from 50% to 20%;
- Increasing the refundable payroll tax credit from 50% to 70%;
- Covering up to two quarters for a total benefit of \$14,000 per covered employee in 2021; and
- Providing that employers that receive PPP loans may still qualify for the ERTC with respect to wages that are not paid for with forgiven PPP proceeds.

This payroll tax credit is particularly helpful for nonprofits deemed too large to participate in the Paycheck Protection Program.

Polling Question

Is your organization currently in the process of preparing and issuing your annual 1099 Forms?

- a) Yes, we prepare them internally;
- b) We have our accountant prepare the forms;
- c) We do not need to file 1099 forms; or
- d) I don't know what this is.

Changes to Form 1099 Reporting

Form 1099s and Backup Withholding.

- Publication 1281 requires organizations to request Form W-9s for all of its vendors to confirm that they are not required to withhold taxes.
- If organization doesn't receive Form W-9 then it is required to withhold.
- Form 1099s should be filed for payments received over \$600 (and subject to additional requirements as well).
- Form 1099-MISC with an amount for Nonemployee Compensation should be mailed by February 1st.
- The most significant change to the Form 1099 in 2020 is the breakout of NEC from Box 7 of Form 1099-MISC to its own Form 1099-NEC. These types of payments will now be reported in Box 1 of the new 2020 Form 1099-NEC.

Charitable Contribution Deductions

The CARES Act Change to Deducting Charitable Contributions.

Charitable contributions were previously only deductible if taxpayers itemized their deductions.

Under the CARES Act, taxpayers who do not itemize their deductions can deduct up to \$300 for cash contributions made in 2020.

The CARES Act also temporarily suspended the limits on charitable contributions made in 2020.

- For individuals, deductible contributions increased from 60% to 100% of their AGI.
- For corporations, deductible contributions increased from 10% to 25% of taxable income.
- The enhanced deduction limit for businesses donating food inventory for the care of the ill, needy, and infants increased from 15% to 25%.

Change in Private Foundation Excise Tax Rate

For tax years beginning on or before December 20, 2019, the excise tax is 2% of net investment income but is reduced to 1% in certain cases.

For tax years beginning after December 20, 2019, the excise tax is 1.39% of net investment income, and there is no reduced 1% tax rate.

IRS Prematurely Issued Auto Revocation Notices to Tax Exempt Organizations

Organizations that do not file a tax return for three consecutive years automatically lose their tax-exempt status.

When the tax return due dates were extended to July 15th, the IRS was unable to update their program that sends the auto-revocation notices, which caused the revocation notices to be sent out prematurely.

The IRS released a statement acknowledging that they prematurely issued auto-revocation notices to multiple tax-exempt organizations.

The IRS has set-up a fax number dedicated to receiving correspondence from organizations wanting to repeal the auto-revocation and provide proof of their Form 990 filings:

- Fax Number: (855) 247-6123.

The IRS has a list on their website of organizations on the auto-revocation list.

E-File Will Be Required for Form 990-T Beginning in 2021

In 2020, the IRS continued to accept paper filings of Form 990-T, Exempt Organization Business Income Tax Return.

The IRS expects E-Filing to be required for Form 990-T beginning February 2021.

For reporting on tax year 2020, the new Schedule A of Form 990-T will reflect separate reporting of each trade or business as required by the Tax Cuts & Jobs Act of 2017. Filers will report total unrelated business taxable income tax based on Schedule(s) A information and compute the tax on the Form 990-T.

E-File Will Be Required for Form 990-EZ

For tax years ending before July 31, 2021, the IRS will accept either paper or electronic filing of Form 990-EZ Short Form Return of Organization Exempt from Income Tax.

For tax years ending July 31, 2021, and later, Form 990-EZ must be filed electronically.

Those who previously filed paper forms will receive a letter from the IRS informing them of the change.

Electronic Filing for CHAR500

New York State Charities Bureau has recently revamped their online filing through their website – much simpler.

Step-by-Step Checklist to ensure you have everything ready to complete online filing.

Returning Users can check filing status online.

IRS Requesting Feedback on Form 990

The IRS is looking to potentially revise multiple tax forms, including Form 990 and the Form 1023/1023-EZ applications.

They were looking for input from the public on “whether the collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; the accuracy of the agency's estimate of the burden of the collection of information; ways to enhance the quality, utility, and clarity of the information to be collected; and ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques or other forms of information technology.”

The deadline for comments was January 11, 2021 – we will see what changes come about.

Polling Question

Has your organization had to cancel or reschedule an event this past year due to COVID-19?

- a) We cancelled all events;
- b) We rescheduled to a later date;
- c) We were able to reinvent with a virtual event; or
- d) None of the above.

Events During COVID-19

Revenue when Cancelling or Postponing Events.

Postponed Events.

- If the event has been postponed to a later date, then there should not be a change in tax treatment.

Cancelled Events.

- If the event is cancelled, pre-sold ticket revenues will need to be addressed.
- If ticket holders agree to donate the ticket cost rather than be refunded, they should be recorded as contributions, not event revenue as they previously would have been.
- If ticket holders want a refund, the ticket cost should be taken out of revenue.
- Organizations should consider sending an acknowledgement letter to donors informing them that the refunded contribution is now no longer deductible, particularly for refunded contributions received in 2019.

Events During COVID-19

Virtual Events.

- While a virtual event still holds value, it is less than an in-person event.
- The change in fair market value would increase the contribution portion of the ticket.
- Organizations can consider either increasing the donor's contribution or refunding the fair market value of what they are not receiving, such as food and entertainment.

Events During COVID-19

Virtual Events Can Trigger UBIT.

- As a result of COVID-19 and related health and safety restrictions, many organizations are choosing to hold their events virtually.
- Under Revenue Ruling 2004-112, the IRS held that income received from a virtual online trade show did not qualify for the exclusion from UBIT.
- There is currently no recent guidance on how the IRS will treat interactive virtual events.
- Based on the example given in Revenue Ruling 2004-112, for a trade show to potentially be exempt from UBIT it must (1) be conducted regularly and relate to the organization's exempt purpose, (2) stimulate interest in and demand for the products of the particular industry or industry segment, and (3) educate those in attendance on new developments, products, and services related to the organization's tax-exempt purpose.

Events During COVID-19

The IRS puts emphasis on the networking, trade and educational components that are usually connected to in-person trade shows. Essentially, if the networking, trade, and educational components are missing from the trade show or event, the organization could be subject to UBIT.

Since virtual event platforms have come a long way since 2004, there are a number of factors to consider whether a virtual trade show in 2020 would be excluded from UBIT. The event should:

- Relate to the organization's exempt purpose.
- Stimulate interest in and demand for the products and services of the industry.
- Educate attendees on new developments, products, and services related to the organization's exempt purpose.
- Include networking, trade and educational components.
- Have limited time availability so that it can be interpreted to be a "specific event" similar to how it would be with an in-person event.
- Look and feel as close to an in-person event as possible.

Gaming and Raffles

A raffle is considered a form of lottery. A raffle generally refers to a method for the distribution of prizes among persons who have paid for a chance to win such prizes, usually determined by the numbers, or symbols, on tickets drawn.

Gaming is not a charitable activity. It does not further the exempt purposes of most organizations. Gaming's contribution to the operation of an exempt organization is generation of funds to pay expenses associated with the conduct of the organization's exempt activities.

Gaming and Raffles

An exception include organization whose exempt purposes include social or recreational activities. For those organization, gaming itself may further an exempt purpose.

A charity conducting gaming as an insubstantial part of its activities will not ordinarily jeopardize its tax-exempt status but may be subject to the tax on unrelated business income (UBI).

There is no “bright-line” or numerical test prescribed by the IRS to determine what is “substantial”.

Gaming and Raffles

Unrelated Business Income – Three conditions must be met for the activity to be classified as an unrelated trade or business:

- The activity must be considered a trade or business. Does it generate revenue?
- The activity must be regularly carried on. Conducted with a frequency and continuity comparable to activities of a non-exempt organization; and
- The activity must not be substantially related to the organization's exempt purpose.

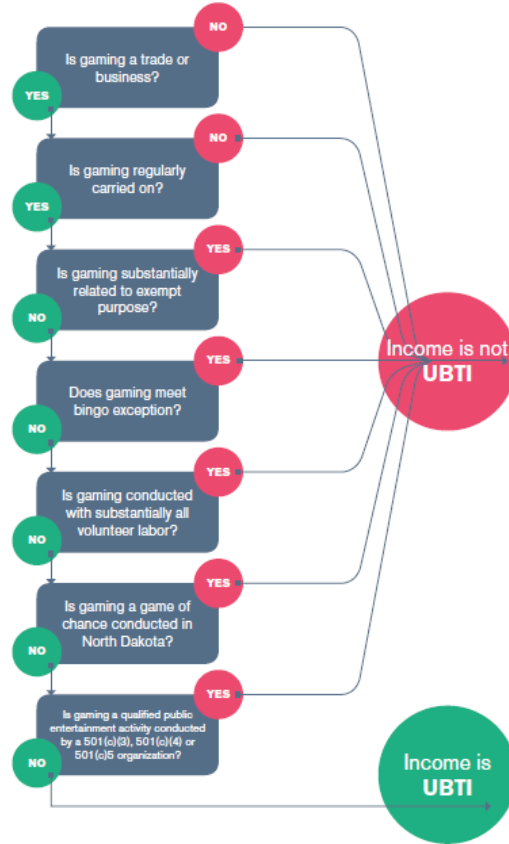
Gaming and Raffles

Even if the three conditions are met for UBI there are exceptions:

- Certain bingo games;
- Activities conducted with substantially all volunteer labor;
- Qualified public entertainment activities; and
- Games of chance conducted in North Dakota.

Gaming and Raffles

Is It Unrelated Business Taxable Income (UBTI)? (Does Not Apply to 501(c)(7) Organizations)



Gaming and Raffles

Exempt Organization Reporting Requirements:

If revenue from gaming exceeds a threshold amounts, you will also be required to complete Schedule G, *Supplemental Information Regarding Fundraising or Gaming Activities*, to your Form 990 or Form 990-EZ.

If you pay the winners more than a certain amount, you must report the amount to the IRS on Form W-2G and possibly withhold income tax. Unless the winnings are from poker, keno, bingo or slots, you must report winnings, including raffles when the amount paid is:

- \$600 or more, and
- At least 300 times the amount of the wager.

Gaming and Raffles

NYS Gaming Commission.

Certain restrictions apply:

- Only persons eighteen or older may purchase or sell tickets.
- No sales more than 180 days prior to date of occasion.
- Winner is not required to be present.
- Authorized location.

Gaming and Raffles

NYS Gaming Commission.

Registration Requirement Categories:

- Cumulative net proceeds for all raffles will meet or exceed \$30k (License Fee and Games of Chance Identification number).
- Cumulative net proceeds will meet or exceed \$5k per drawing or \$20k-\$30k total in a calendar year. (Obtain Games of Chance Identification Number).
- Cumulative net proceeds from a single raffle will be less than \$5k and total during the calendar year will not meet or exceed \$20k.

Polling Question

Does your organization have a policy in place to value and recognize In-Kind Contributions received?

- a) Yes;
- b) No; or
- c) We do not receive in-kind contributions.

In-Kind Contributions

Types - goods, services, etc. that support the organizations mission.

Recognized as contribution revenue and related asset or expense.

In-Kind Contributions

In-Kind Goods:

- Tangible items that can be utilized or resold for cash.
- If the items cannot be used or resold, then they should not be recognized.
- They can be new or used.
- They must be donated unconditionally and without receiving anything in return.

In-Kind Contributions

In-Kind Services:

- Services that would help a nonprofit directly or indirectly supports its mission.
- Includes services donated by individuals, small or large businesses, corporations, organizations, etc.
- Examples - marketing, accounting, legal, teaching and catering.
- Only services that the organization would have purchased had they not been donated would be recorded as In-Kind services.
- Volunteer hours are only considered In-Kind Contributions if they are providing a “specialized skill” i.e., volunteers checking guests into an event would not be considered an In-Kind Contribution because it is not a specialized skill.
- In-Kind Services are recognized at the fair market value of the service provided.

In-Kind Contributions

In-Kind Rents:

- In-Kind Rent is valued at the fair market value of the rent.
- If rent is free, recognize the full fair market value of the rent as an In-Kind Contribution.
- If rent is discounted, the recognized In-Kind Contribution would be the difference between rent expense paid and the fair market value.

In-Kind Contributions

Items Donated for Resale:

- Example - items donated to be sold at a charity auction.
- These contributions must be recorded at the estimated amount to be received when the items are sold.

In-Kind Contributions

Form 990 Reporting :

- Only In-Kind Contributions of tangible goods/property are required to be reported on Form 990.
- The value of In-Kind Services and rent/use of facilities are shown as a reconciling item on Form 990, when reported on financial statements.

Reminders for Tax-Exempt Entities

Public Disclosure Requirements.

IRC Section 6104 contains the public inspection requirements.

Forms required to be made available for public inspection:

- Form 990 and 990-EZ and corresponding schedules with the exception of redacted Schedule B and excess contributions list from Schedule A.
- Form 990-PF and Schedule B.
- Form 990-T.
- Form 1023.

Reminders for Tax-Exempt Entities

Why must Forms be made available for public inspection:

- Promotes Compliance.
- Ensures Accountability and Transparency.
- Serves as a Public Relation Tool.

Reminders for Tax-Exempt Entities

Number of Volunteers.

- Form 990 Question - estimate if necessary.
- Volunteers are individuals who serve the organization without compensation including full-time and part-time members of the organization's governing body.
- Most of the time the board is made up of volunteers

Reminders for Tax-Exempt Entities

Program Service Descriptions.

- Advertise your organization.
- Include specific details such as clients served, days of care provided, number of students.
- Include reasonable statistics of successes.

Reminders for Tax-Exempt Entities

Independent Board Members.

A member of the governing body is considered “independent” only if all four of the following circumstances applied at all times during the year:

- The member was not compensated as an officer or other employee of the organization or of a related organization;
- The member did not receive compensation exceeding \$10k during the year as an independent contractor;
- Neither the member, nor any family member was involved in a transaction with the organization required to be reported on Schedule L; and
- Neither the member, nor any family member was involved in a transaction with a related organization required to be reported on Schedule L.

Reminders for Tax-Exempt Entities

Conflict of Interest Policy.

If an organization states that it has a conflict-of-interest policy, but it doesn't monitor conflicts, IRS might ask questions.

Organization needs to describe their monitoring practices and how it deals with potential conflicts.

The description should include:

- Which persons are covered under the policy;
- The level at which determinations are made;
- The level at which the conflicts are reviewed; and
- Restrictions imposed on persons with conflicts.

Reminders for Tax-Exempt Entities

Significant Diversion of Assets.

Any unauthorized conversion or use of the organization's assets.

Material diversions are lesser of:

- \$250,000;
- 5% of gross receipts; or
- 5% of total assets.

Form 990 question must be answered, and incident must be described in detail including:

- Nature of diversion.
- Dollar amounts or other property involved.
- Corrective action taken.
- Pertinent circumstances.

Reminders for Tax-Exempt Entities

Compensation.

- IRS permits nonprofits to pay executives “fair and reasonable” compensation.
- There is no formula to determine what is reasonable.
- However, if the nonprofit is not paying the right amount it could be subject to taxes.
- The penalties for an excess benefit transaction are levied on both the executive who received the benefit and the board members who approved it or didn’t prevent it.
- Biggest risk - reputation of both the organization and the individuals involved.

Reminders for Tax-Exempt Entities

The organization can establish rebuttable presumption of reasonableness by:

- Approving compensation in advance.
- Approval by only independent board members.
- Basing compensation on data obtained before the compensation is paid.
- Documenting the process and decision at the time it is made, including terms of the transaction, members that voted and comparable data used.

Nonprofit Resources

TechSoup - www.techsoup.org.

- Offer discounted services to implement and manage your organization's technology.
- It can help reduce computer software expenses (i.e., QuickBooks).

GuideStar - www.guidestar.org.

- Providing nonprofit organizations with up-to-date data.
- How does your organization compare to similar organizations?

Nonprofit Resources

IRS Website -

<https://www.irs.gov/charities-non-profits/tax-exempt-organization-search>.

- Verify that you are eligible to receive tax-deductible charitable contributions.
- Check the listing of automatically revoked organizations.

New York State Charities Bureau -

https://www.charitiesnys.com/RegistrySearch/search_charities.jsp.

- Verify registration status.
- Find prior filings and documents.

Questions





Shannon T. Forkin, CPA, CGMA Tax Partner

Email: sforkin@dmcpas.com

Web: www.dmcpas.com

Address:

Mohawk Harbor
220 Harborside Drive
Suite 201
Schenectady, NY 12305

Phone: (518) 836-5661, ext. 151



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Scan to add Shannon to your contacts.

A professional headshot of Marissa A. Spring, a woman with long blonde hair, smiling. She is wearing a black blazer over a white blouse with black polka dots. The background is a dark, textured grey.

Marissa A. Spring Tax Senior

Email: mspring@dmcpas.com

Web: www.dmcpas.com

Address:

DM Financial Plaza
221 South Warren Street
Syracuse, NY 13202

Phone: (315) 472-9127, ext. 128

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