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2020 Nonprofit Tax Year-End Review

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Agenda

- Key Supreme Court rulings and pending cases
- PPP loan forgiveness
- Health care sharing ministries update
- Final UBIT siloing regulations
- Changes to 2020 Form 990-T
- Form 990 and PPP loan forgiveness amounts
- Update on e-filing Form 990 and Form 990-T
- Online Form 1023 update

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Agenda

- Form 4960 regulations
- Form 4968 regulations
- W-2 reporting of deferred employee payroll tax
- Form 1099-NEC
- Form 1098-T and HEERF payments
- CARES Act charitable giving provisions

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Our Lady of Guadalupe School v. Morissey-Berru (ministerial exception)

- Decided on July 8, 2020
- Plaintiff was a teacher at OLGS and brought an age discrimination claim against the school. She was deemed a “minister” under an earlier SCOTUS case (*Hosanna-Tabor*), which exempts religious institutions from anti-discrimination laws in hiring employees who are “ministers.”

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Our Lady of Guadalupe School (ministerial exception)

- The factors the Court considered important here were:
 - Teaching religion
 - Signing an annual agreement that highlighted the core religious nature of the education provided and how it would affect their performance review
 - Providing catechetical instruction every day
 - Preparing students for participation in Mass
 - Praying with students
 - Modeling the Catholic faith through their behavior and classroom instruction

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Our Lady of Guadalupe School (ministerial exception)

- Question: Do the First Amendment's religion clauses prevent civil courts from adjudicating employment discrimination claims brought against a religious employer, when the employee carried out important religious functions but was not otherwise a "minister?"
- Answer: Yes. The definition of "minister," which was a balancing of four factors in *Hosanna-Tabor*, is not subject to a rigid formula. Rather, the key inquiry is what the employee does. The teacher in this case was educating children in the tenets of the faith — which the Court saw as core to the institution's religious mission.
 - There needs to be a strong tie between the duties of the employee and the religious nature of the organization.

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Bostock v. Clayton County (SOGI, Civil Rights Act)

- Decided on June 15, 2020
- Bostock, a gay man, worked for Clayton County, Georgia child welfare services
 - He had a stellar record, but was terminated in 2013 after it was discovered he was gay from a workplace conversation in which he discussed his participation in a gay softball league
 - He filed a discrimination claim with the Equal Employment Opportunity Commission (EEOC), alleging discrimination because of sexual orientation under Title VII of the Civil Rights Act (CRA)

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Bostock v. Clayton County (SOGI, Civil Rights Act)

- Donald Zarda worked as a skydiving instructor at Altitude Express in New York
 - After several seasons with the company, he mentioned he was gay and was terminated days later

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Bostock v. Clayton County (SOGI, Civil Rights Act)

- Aimee Stephens worked at R.G. & G.R. Harris Funeral Homes in Garden City, MI.
 - When she started, she presented as a male. Then, after two years of employment, she began mental health treatment for despair and loneliness. She was diagnosed with gender dysphoria and it was recommended she begin living as a woman.
 - In her sixth year with the company, she wrote a letter to the management stating that she planned to “live and work full-time as a woman” when she came back from vacation.
 - She was terminated before she left for vacation.

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Bostock v. Clayton County (SOGI, Civil Rights Act)

- Question: Does Title VII of the CRA, which prohibits against employment discrimination “because of... sex” encompass discrimination based on an individual’s sexual orientation?
- Answer: An employer who fires an individual merely for being gay or transgender violates Title VII of the CRA. (Gorsuch and Roberts joined Ginsburg, Breyer, Kagan, and Sotomayor.)

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Bostock v. Clayton County (SOGI, Civil Rights Act)

- *Bostock* does not directly address the application of its holding to religious organizations
- Gorsuch noted the anxieties many religious organizations may feel, but noted the following mitigating factors
 - First: Title VII already permits organizations to make employment decisions based on religion
 - Second: *Hosanna-Tabor* (and now, *Our Lady of Guadalupe*) give religious organizations expansive discretion with regard to “ministers”
 - Third: The federal Religious Freedom Restoration Act (RFRA) may act as “a kind of super-statute, displacing the normal operation of other federal laws [that] might supersede Title VII’s commands in appropriate cases.”

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Bostock Takeaways

- Review documents and policies that may help demonstrate that your organization is clearly religious in nature (Articles of Incorporation, bylaws, website, statement of faith and practice signed by employees)
- Review the ministerial exception and whether it may apply to various employees

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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California v. Texas (Affordable Care Act challenge)

- Oral arguments on November 10, 2020
- In 2012, SCOTUS upheld the individual mandate in the ACA as a tax and not a penalty
- 2017: Congress set the tax rate to zero, effectively nullifying the tax but leaving the mandate in place
- Question: Is this still able to be characterized as a tax?
- Texas and several states challenge the law; California and several states joined to defend the law

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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California v. Texas (Affordable Care Act challenge)

- Questions: Is the individual mandate of the ACA, which now has a penalty of zero for not buying health insurance, now unconstitutional?
- If the individual mandate is unconstitutional, is it severable from the remainder of the ACA?

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Fulton v. City of Philadelphia (free exercise of religion)

- Oral arguments on November 4, 2020
- March 2018: Philly bars Catholic Social Services (CSS) from placing children in foster homes. Philly had a policy of requiring all its contractors to not consider the sexual orientation of the potential foster parents when making a placement determination.
- CSS would not license same-sex couples (though it should be noted it was never approached). CSS argued that its First Amendment right to free exercise of religion entitled it to reject same-sex couples.

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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Fulton v. City of Philadelphia (free exercise of religion)

- Questions: Should the Court revisit the decision in *Employment Division v. Smith*?
- Does the government violate the First Amendment by conditioning a religious agency's ability to participate in the foster care system on taking actions and making statements that directly contradict the agency's religious beliefs?

Seek the advice of qualified legal counsel when determining how these issues apply to your organization.

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PPP Loan Forgiveness

- Forgiveness available for qualifying expenses, including:
 - Payroll costs
 - Mortgage interest
 - Rents
 - Utilities
- There is no specific due date to file the loan forgiveness application but a borrower must begin making payments within 10 months after the conclusion of the Covered Period if an application is not filed by then

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PPP Loan Forgiveness (continued)

- Multiple loan forgiveness application forms released
 - **Form 3508S** – May be used by borrowers who borrowed \$50,000 or less, unless the borrower is a member of an affiliate group that together borrowed more than \$2,000,000
 - **Form 3508EZ** – May be used when:
 - The borrower is a self-employed, an independent contractor, or a sole proprietor who did not include any employee salaries in the computation of average monthly payroll in applying for the loan

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PPP Loan Forgiveness (continued)

- **Form 3508EZ** (continued)
 - The borrower did not reduce any employee's rate of pay by more than 25% and
 - Did not reduce the number of any employees or average paid hours between January 1, 2020 and the end of the Covered Period
 - The borrower was unable to operate during the Covered Period at the same level as at February 15, 2020 due to COVID-19-related government regulations or orders
- **Form 3508** – Used in all other situations

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PPP Loan Forgiveness (continued)

- Loan Necessity Questionnaire
 - Borrowers of \$2 million or more will likely receive a [Loan Necessity Questionnaire \(Form 3510\)](#) from their lender
 - [PPP Loan FAQ 53](#) discusses the PPP Loan Necessity Questionnaire
 - The questionnaire is used by the SBA to assess a borrower's certification that "[c]urrent economic uncertainty" made the "loan request necessary to support the ongoing operations" of the borrower

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PPP Loan Forgiveness (continued)

- Loan Necessity Questionnaire (continued)
 - Receipt of the questionnaire does not mean the SBA is challenging the borrower's loan application certification
 - The loan necessity questionnaire must be completed and returned within 10 days of being received

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Health Care Sharing Ministries

- In June 2020, the IRS issued proposed regulations that purport to permit an HRA to reimburse payments for membership in a health care sharing ministry
 - This includes:
 - An HRA integrated with a traditional group health plan
 - An ICHRA
 - A QSEHRA
 - An EBHRA
- Membership in a health care sharing ministry will not permit a member to make payments to an HSA

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Health Care Sharing Ministries (continued)

- The “catch”
 - There is a catch — the proposed regulations do not eliminate:
 - The requirement that a QSEHRA provide an insurance policy that provides *minimum essential coverage*
 - The requirement that an ICHRA be integrated with some form of qualifying insurance
- This means that the HRA must pay for both an insurance plan *and* the health care sharing ministry membership
- Stay tuned to see what the final regulations provide
- These rules will not be effective until the regulation is final

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Final UBTI Siloing Regulations

- The TCJA enacted Code section 512(a)6)
 - Requires that unrelated trade or business activities be tracked in separate silos
 - A net loss from one trade or business activity is no longer permitted to offset net income from a separate trade or business activity
- On December 2, 2020, final UBTI siloing regulations were published in the Federal Register

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Final UBTI Siloing Regulations (continued)

- Separate trade or business silos are identified by determining the 6-digit NAICS code applicable to an individual trade or business activity
 - Activities whose 6-digit codes share the same two leading digits are then permitted to be aggregated
 - The two leading digits correspond to 20 unique economic sectors
 - NAICS codes are maintained by the [U.S. Census Bureau](#)
 - NAICS codes may be looked up on the [NAICS site](#)
 - The final regs permit changes to NAICS codes without consent

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Final UBTI Siloing Regulations (continued)

- In addition to NAICS code-derived silos, the regulations identify four other relevant trade or business categories:
 - Investment activity
 - S-corporations
 - Specified payments from section 512(b)(13) controlled entities
 - Insurance income under section 512(b)(17)

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Final UBTI Siloing Regulations (continued)

- Investment activity
 - Debt-financed income
 - Qualifying partnership interests
 - De minimis test
 - Participation test
 - Qualifying s-corporation interests
 - De minimis test
 - Participation test

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Final UBTI Siloing Regulations (continued)

- Special rule for S-corporation interests that are not qualified S-corporation interests
 - Where an organization owns stock in an S-corporation, such S-corporation interest is treated as a separate unrelated trade or business for the purpose of section 512(a)(6)

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Final UBTI Siloing Regulations (continued)

- 512(b)(13) controlled organization specified payments
 - NAICS codes are not used in this situation
 - A **specified payment** includes any interest, annuity, royalty, or rent
 - Specified payments of different types received from the same 512(b)(13) entities are treated as belonging to the same, separate trade or business
 - Specified payments of the same type from two different 512(b)(13) entities are treated as from two, separate trades or businesses

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Final UBTI Siloing Regulations (continued)

- 512(b)(17) insurance income is treated as coming from the same unrelated trade or business activity
- If two or more unrelated activities that are carried on together would be treated as two separate unrelated trades or businesses under the NAICS codes, the “fragmentation rule” is applied to require that the two or more activities be separately examined to determine if they belong in the same or in different silos

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Final UBTI Siloing Regulations (continued)

- Shared expenses must be allocated among silos
 - The final regs require shared expenses to be allocated on a reasonable basis
 - The IRS has reserved providing further, concrete guidance in this area in the future
 - The proposed regulations had specified that an allocation based on gross revenue is presumptively unreasonable
 - The final regulations remove this restriction unless there are different charges for different populations

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Final UBTI Siloing Regulations (continued)

- Post-2017 NOLs from a discontinued activity, regardless of why it is discontinued, are suspended
 - Unlike passive-activity losses, suspended losses are not permitted to be used upon termination of an activity
 - Such suspended losses may be picked up and used in the future if a new trade or business in the same silo is initiated

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Changes to the 2020 Form 990-T

- Forms 990-T filed in February 2021 and later will be electronically filed
- The new [Form 990-T](#) core form now limits its content to:
 - Summarizing the unrelated business taxable income from all sources
 - Computing the tax
 - Reporting estimated tax payments and tax credits
 - A few statements regarding activities

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Changes to the 2020 Form 990-T (continued)

- The new [Form 990-T, Schedule A](#) is completed for each unrelated trade or business
 - The Schedule A is largely the same as the previous Schedule M

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Form 990, Schedule A and PPP Loan Forgiveness

- The IRS has stated publicly that forgiven PPP loan balances will not negatively impact an organization's public support test under sections 170(b)(1)(A)(vi) and 509(a)(2)
- The IRS has stated that this will be addressed in upcoming Form 990 instructions
- One IRS representative is quoted as stating that PPP loan forgiveness will be reported as a contribution from a government unit *in the tax year they are forgiven*
 - Does this mean there could be a book-to-tax difference?

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Online Form 1023 update

- Beginning January 31, 2020, applications for recognition of exemption must be filed online at pay.gov
- User fee remains \$600
- Must create a pay.gov account to file online
- Several features make it easier to navigate:
 - Yes/No questions automatically open up various schedules
 - Yes/No questions automatically skip various questions
- Be sure to save often (but know that it will take you out of the Form)

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Online Form 1023 update

- Need to complete the checklist and upload **one** PDF attachment that includes organizing document and bylaws, supplemental responses, and other material you think is helpful
- PDF attachment can be no larger than 15MB (about 250 pages) – if larger, you will need to reduce it, then call IRS Customer Account Services at 877-829-5500 for next steps

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Section 4960 Regulations

- On June 11, 2020, the IRS released proposed regulations implementing the excess executive compensation rules enacted under TCJA as Code section 4960
- Excess executive compensation is compensation in excess of \$1,000,000 and certain excess parachute payments
 - Wages paid to a minister for ministerial services are excluded from the definition of excess executive compensation
- The proposed regulations define many terms found in the statute

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Section 4968 Regulations

- On October 15, 2020 the IRS issued final regulations under section 4968 regarding the excise tax on endowment net investment income of colleges and universities
- The statute left open significant questions regarding the definition of a tuition-paying student and which assets are used directly in carrying out the institution's exempt purpose, which the regulations address

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W-2 Reporting of Deferred Employee Payroll Tax

- On August 8, 2020, President Trump issued a presidential memorandum allowing employers to defer the withholding and payment of the employee's portion of section 3102(a)
- The [IRS website](#) now provides guidance on how to report the deferral on the employee's Form W-2
 - Wages for which the tax was deferred in 2020 are included in Box 3
 - The deferred tax is **not** included in Box 4
 - Taxes subsequently withheld in 2021 are reported in Box 4 on a Form W-2c, entering the tax year 2020 in Form W-2, Box c

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Form 1099-NEC

7171 VOID CORRECTED

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.		OMB No. 1545-0116	2021	Nonemployee Compensation
		Form 1099-NEC		
PAYER'S TIN	RECIPIENT'S TIN	1 Nonemployee compensation \$		
RECIPIENT'S name		2 Payer made direct sales totaling \$5,000 or more of consumer products to recipient for resale <input type="checkbox"/>		
Street address (including apt. no.)		3		
City or town, state or province, country, and ZIP or foreign postal code		4 Federal income tax withheld \$		
Account number (see instructions)	2nd TIN not <input type="checkbox"/>	5 State tax withheld \$	6 State/Payer's state no.	7 State income \$

Form **1099-NEC** Cat. No. 72590N www.irs.gov/Form1099NEC Department of the Treasury - Internal Revenue Service
Do Not Cut or Separate Forms on This Page – Do Not Cut or Separate Forms on This Page

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Form 1099-NEC

- Should be used for tax year 2020 and beyond
- Used for nonemployee compensation (formerly placed on box 7 of the 1099-MISC)
- File this form for each person in the course of your ministry who has been paid at least \$600 for services performed as a nonemployee (including parts and materials)
- Independent contractors, “gig” workers, self-employed individuals

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Form 1099-NEC

- Due date is January 31 for filing Copy A
- State direct reporting requirements are affected because information reporting data for the 1099-NEC will not be included in the Combined Federal/State Filing program
- Form 1099-MISC is still used for:
 - Rents paid
 - Royalties
 - Attorney's fees
 - Other reportable income

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HEERF Payments and 1098-T

- Higher Education Emergency Relief Fund (HEERF) payments made to students who experienced unexpected expenses, unmet financial need, or other expenses should not be included in gross income.
 - They are classified as nontaxable disaster relief payments under section 139.
 - Further, on [December 14, 2020](#), the IRS stated that these amounts should **not** be reported on Form 1098-T. If they are reported, it “could result in the issuance of underreporter notices to students,” as well as cause confusion for students themselves.

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CARES Act Charitable Giving Provisions

- The CARES Act included a few enhancements to charitable contributions
 - For **cash** contributions made by individuals during 2020 to a public charity that is not a donor advised fund or supporting organization, the 60% of adjusted gross income limit is suspended
 - Accordingly such cash contributions are deductible to the extent of 100% of adjusted gross income
 - For **cash** contributions made by a corporation during 2020, the limitation on deductions is increased from 10% to 25%

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CARES Act Charitable Giving Provisions (contributions)

- The CARES Act included a few enhancements to charitable contributions (continued)
 - Individuals who do not itemize their contributions may claim up to a \$300 deduction in computing adjusted gross income
 - This limit is “per return” such that married individuals filing a joint return are limited to a single \$300 deduction

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Questions?



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