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Exempt Organizations: Tax Reform Provisions to Watch

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The Ways and Means Committee of the U.S. House of Representatives released its long-awaited tax bill on November 2, 2017. The bill is entitled Tax Cuts and Jobs Act, H.R. 1 (TCJA). Note that there is nothing in the title referencing tax simplification . The full text of the bill is 429 pages. Of interest to nonprofit organizations are the following provisions:

- A tax exempt organization will pay a 20% excise tax on any executive compensation in excess of $1 million. The excise tax applies only to the top five executives, and includes all remuneration and benefits, other than amounts that are excludable from the executive s gross income such as donations to a qualified retirement plan. (TCJA §3803) This 20% excise tax applies to all organizations described under §501(a), along with political organizations exempt under §527, §115 state and local governmental entities, and farmers cooperatives.
- The Johnson Amendment would be partially repealed, and §501(c)(3) religious organizations would be free to express partisan political statements during the ordinary course of the religious organization s activities, assuming its expenses in making those statements are de minimis. (TCJA §5201) Note that this applies only to religious organizations. All other §501(c)(3) organizations are still prohibited from engaging in any partisan political activities and/or partisan political speech.
- Private foundations will now be subject to a 1.4% investment tax, rather than the 1% or 2% investment tax under §4940. This is one of a very few provisions that would simplify current law. (TCJA §5101) The 1.4% tax would also be collected from certain private colleges and universities on their net investment income. (TCJA §5103)
- Private foundations would be exempt from the excess business holding excise tax for any of its 100% subsidiaries (by voting stock) that annually distribute all net operating income to the private foundation. The foundations that are eligible for this exemption are limited to those that have independent executives and boards of directors. Thus, the exemption would not apply to foundations where the majority of the members of the board of directors are substantial contributors or executives of the foundation. (TCJA §5104)
- Donor advised funds would be subject to additional reporting requirements regarding their policies on inactive donor advised funds as well as a requirement to report the average amount of grants made from their donor advised funds. (TCJA §5202)
- The bill clarifies that the unrelated business income tax applies to all tax-exempt organizations recognized under §501(a), along with §115 state and local entities such as public pension plans. (TCJA §5001)
- Any net income that a tax-exempt organization realizes from research would now be subject to the unrelated business income tax, unless the research is publicly available. (TCJA §5002) Previously, net

income from research performed by colleges, universities, hospitals or performed for government entities was also generally exempt from UBIT regardless of whether the research was publicly available.

Whether any of these provisions will be passed by Congress and signed into law as currently stated is unknown. Several of the provisions are controversial, such as the partial repeal of the Johnson Amendment. Combining politics and religion is generally not a good idea, and it could be subject to a constitutional challenge as a violation of the separation of church and state. Other revenue raisers, such as taxing net research revenue and imposing a net investment tax on certain private colleges and universities, may come under attack as well. The 20% tax on excess compensation of nonprofit executives may receive less scrutiny, since those excise taxes could more easily be avoided through tax planning initiatives. Stay tuned!

TAGGED: taxes, tax, Tax Cuts and Jobs Act, Ways and Means Committee, tax exempt organizations, nonprofits, tax reform