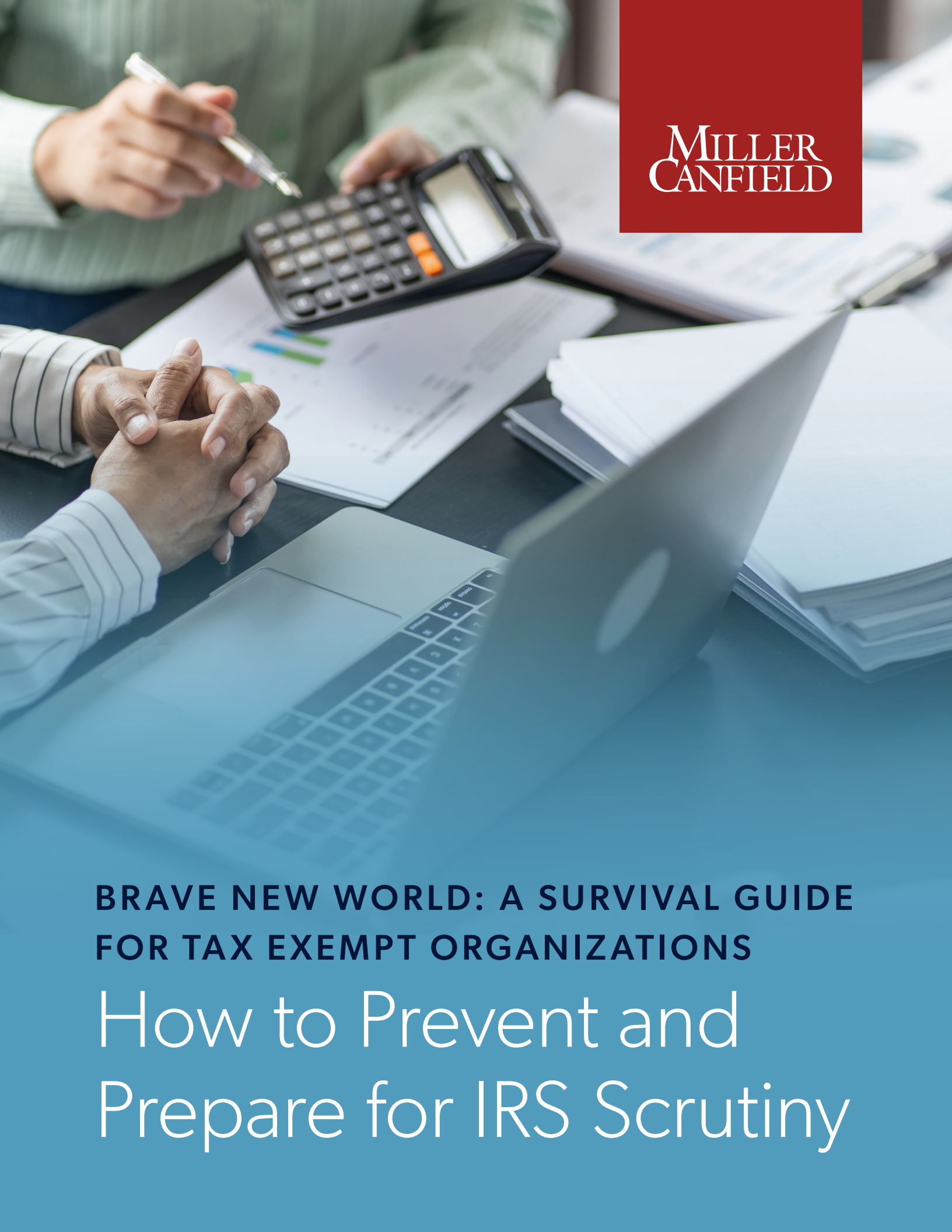


A background image showing a business meeting. In the foreground, a person's hands are clasped on a desk. In the background, another person is using a calculator and holding a pen over documents. A laptop is also visible on the desk.

**BRAVE NEW WORLD: A SURVIVAL GUIDE
FOR TAX EXEMPT ORGANIZATIONS**

How to Prevent and Prepare for IRS Scrutiny

Increased oversight and shifting political priorities have made it essential for exempt organizations to test their own compliance, tighten governance, and know their rights if their exemption is questioned.

This guide covers some rules of the game and boundaries on governmental authority, and offers clear steps for communicating with boards, members, and donors without fueling panic. The rules around tax-exempt organizations are extensive, and this material cannot cover everything. We intend to heighten your awareness of threats to your tax exemption and give some ideas for small and big things you can do to protect yourself. This is for educational purposes only and not intended to be legal advice. As with any tax issue, you should consult your own tax-adviser for guidance on the protection of your tax exemption. If you have any legal questions, please contact your Miller Canfield attorney.

» WHAT STEPS CAN WE TAKE TO PROTECT OUR EXEMPTION?

As a starting point, exempt organizations should review their compliance with the baseline requirements for tax exemption. First, we cover some administrative actions which may be easier to do. Then, we list more technical items which can endanger your exemption but may need more in-depth work.

A. First, address low-hanging fruit which may jeopardize your exempt status.

1. Check Your Articles of Incorporation.

Exempt organizations must be *organized* exclusively for an exempt purpose. This means that your articles of incorporation must state that your purposes are limited to exempt purposes and provide that your assets should be distributed to other Section 501(c)(3) organizations upon dissolution.¹

Your exemption can be revoked if the articles do not have the correct language. You should carefully read your articles to make sure they don't permit your organization to do anything outside of your charitable purpose. Stating explicitly that the intent is to conform to Section 501(c)(3) is a good practice but does not mean your actual purpose will qualify. You should also review your bylaws to make sure your language is compliant and consistent with your articles.

Also consider possible state tax exemptions that don't automatically apply to all Section 501(c)(3) organizations. Specific state standards may need to be satisfied, such as demonstrating a specific exclusive or principal purpose.

2. Ensure you have a conflict-of-interest policy—and comply with it.

A conflict-of-interest policy is not required under tax laws, but it helps demonstrate to the IRS that your organization promotes public interests and avoids private benefits to its insiders.

A good conflict of interest policy will help you identify conflicts with your board members and other insiders. It will also provide a procedure for disclosing conflicts and excluding insiders from participating in company decisions that could benefit them.

3. Have a document retention policy.

Exempt organizations, just like any other organization, should have a document retention policy to prevent important documents from being lost because of employee turnover or passage of time. For exempt organizations, it's possible that the government, potential partners, or donors could request documents even decades later.

We recommend that you keep the following documents for as long as you exist:

- Application for exemption
- Determination letter
- Any state exemption letters
- Attorney General initial registration

You should also retain six years of the following forms:

- IRS Forms 990 (annual returns)
- Attorney General annual reports

4. Prepare a response plan.

Exempt organizations should have a procedure in place to respond to a proposed revocation or other action from the government. Before any governmental actions, your organization should identify the person or people responsible for coordinating the entity's response so you can react quickly and responsibly. Remember that a revocation will probably not require an immediate response, so make sure you take the time you need to respond appropriately.

We do not recommend taking any extraordinary action before the government has notified you of an issue, such as pre-paying expenses, moving employees, moving funds, or creating new entities. Yet some preparation may help your organization respond in a methodical way and prevent mistakes from being caught unprepared.

5. Monitor the mail for IRS letters.

Some IRS exemption revocation letters may provide only a short window for a response, as explained below. Make sure you regularly check your snail mail for communications from the IRS and when you receive a letter from the IRS, open it right away. You need to check for a due date for a required response to avoid missing a hard deadline.

6. File periodic returns with the IRS, state tax agencies, Secretary of State, and (when required) the Attorney General.

Make sure to identify the employee or employees responsible for filing your Forms 990, any required

state returns, and any employment tax returns. Have an annual procedure to identify whether any other forms are required.

If your organization fails to file its annual tax return on Form 990 for three years in a row, its exemption will be automatically revoked by the IRS.

You should also file an annual report with your state's secretary of state to prevent your organization from being automatically dissolved under state law.



If your organization is registered or licensed as a charity with your state's attorney general, you will need to file another annual report with your attorney general. Holding raffles and other fundraisers or serving alcohol also likely have specific license or permit requirements.

Finally, if you have a state sales or property tax exemption, you should verify what reports or updates your state requires.

The takeaway here is simple: documentation matters. Make good recordkeeping a priority.

B. Next, be aware of more complex traps for the unwary.

1. Avoid private inurement (excessive benefits to insiders)

Your net earnings may not inure to the benefit of a private shareholder or individual. A private shareholder or individual (also called an insider) means a person having a personal or private interest in the activities of the organization. In other words, an insider is a person who has a special, close relationship with the organization, including the

organization's founders, trustees, directors, officers, key employees, members of the family of these individuals, and certain entities controlled by them.

Inurement means the flowing of income or assets, directly or indirectly, through the tax-exempt organization.

This prohibition is meant to prevent anyone in a position of power from siphoning off a charity's income or assets for personal use. For example, if your organization awards a contract to a company owned by a board member and pays an excessive fee to the company, that will constitute private inurement. But if an insider enters into an arms' length transaction and receives the same benefit as anyone else would in a similar transaction, then the transaction may not constitute private inurement.



Basically, if your organization enters into a transaction with an insider, you should follow procedures to make sure you can demonstrate that it is fair, reasonable, and arm's length and that you document those procedures.

Insiders should also recuse themselves from discussions or votes involving transactions between themselves (or companies related to them) and the tax-exempt organization. Still, from a risk-management standpoint, the least risky position is to avoid any transactions with insiders if at all possible.

2. Avoid excess benefit transactions.

The IRS imposes monetary penalties on tax-exempt entities and "disqualified persons" who participate in excess benefit transactions with tax-exempt entities. These are called "intermediate sanctions" because it's a penalty that's not as serious as losing your tax exemption.

A "disqualified person" generally means a person who exercises substantial influence over the affairs of the organization, or a member of their family or an entity owned more than 35% by such persons.² An excess benefit transaction generally means any transaction in which the disqualified person receives more than an unrelated third party would receive in a similar transaction.³

These rules are similar to the private inurement rules but are generally imposed when the behavior does not rise to the level to call into question the exemption of the organization. Generally, you should avoid any transaction (or the appearance of a transaction) that provides an excess benefit to a disqualified person.

Keep in mind that the IRS may ask you to prove a negative, meaning you will have to show why a challenged transaction is *not* an excess benefit transaction. Careful documentation remains paramount.

3. Promote public (not private) benefits.

Exempt organizations must serve a public interest rather than a private interest.⁴ You may not confer non-incidental benefits on an unrelated third-party. For example, the following types of entities were found to lack a public benefit:

- An organization which was established to train individuals for careers in political campaigns which conferred substantial private benefits on only Republican entities and candidates⁵
- An educational organization which researched only the history of one family
- An art museum which sells art from a group of artists, giving each artist 90% of the proceeds from their sales
- An organization created by a farm owner to provide low-income housing where preference was given to employees of the farm⁶

The private benefit rule is different from the private inurement rule because the private benefit rule applies to a private benefit to anyone, not just insiders.

Incidental private benefits are allowed. For example, a program that assigned Medicaid patients to doctors in private practice did provide incidental private benefits to the doctors. Yet the program still retained its tax exemption because the Medicaid patients were the primary beneficiaries, not the doctors.⁷

4. Limit lobbying.

No substantial part of your activities may consist of propaganda or otherwise attempting to influence legislation. If an organization crosses the line and a substantial part of its activities is attempting to influence legislation, it is labelled an “action organization” and loses its tax exemption.

Attempting to influence legislation means: (1) contacting, or urging the public to contact, members of a legislative body to propose, support, or oppose legislation; or (2) advocating the adoption or rejection of legislation.⁸ It does not mean merely making general political statements or having political views or having internal policies that reflect your organization’s viewpoints. It means taking action to influence legislators—not just having opinions. There must be some proposed legislation (or at least legislators) involved. Attempting to influence regulators in the executive branch is not considered lobbying for this purpose.⁹

Because the specific limit on lobbying is vague (a substantiality test), organizations may elect to use the lobbying expenditures test under Section 501(h). This test provides more certainty by establishing a bright line rule on the amount an organization may spend on lobbying and grass roots advocacy without violating the prohibition on lobbying. The Section 501(h) test provides a lobbying limit based on the amount of the organization’s exempt purpose expenditures. The limit ranges from 20% of the exempt purpose expenditures (for organizations with less than \$500,000), to \$1 million (for organizations with more than \$17 million in exempt purpose expenditures).

5. Do not promote a candidate for office.

Section 501(c)(3) prohibits an exempt organization from participating or intervening in any political campaign on behalf of or in opposition to any

candidate for public office. Although this prohibition seems absolute, the IRS has unevenly enforced it.

In addition, the definition of “participation” or “intervention” in a political campaign is not entirely clear. In general, participation or intervention in a political campaign means an activity that favors or opposes a candidate for office. It would include making a contribution for or against a political candidate. But the application of the rule to other scenarios is not so easy.

Depending on the facts and circumstances, promoting a candidate could also include:¹⁰

- Distributing statements or other communications
- Providing facilities or use of other assets
- Lending employees
- Partisan voter registration efforts
- Hosting debates that are not open to all or where the candidates are asked different questions
- Establishing a political action committee



If an exempt organization engages in political campaign activity, it becomes classified as an “action organization” and may lose its exemption.

Notice that this prohibition only applies to activities related to a candidate in a political campaign and not to merely making political or partisan statements or having policies that the executive branch could consider political, such as diversity, equity, or inclusion policies. For example, making a political statement about diversity on your website or having an inclusion policy, without mentioning political candidates, should not be disallowed under this rule.

The IRS considers several key factors to determine whether a communication is a campaign intervention:

- Whether the statement identifies one or more candidates for a given public office
- Whether the statement expresses approval or disapproval for one or more candidates' positions and/or actions
- Whether the statement is delivered close in time to the election
- Whether the statement makes reference to voting or an election
- Whether the issue addressed in the communication has been raised as an issue distinguishing candidates for a given office
- Whether the communication is part of an ongoing series of communications by the organization on the same issue that are made independent of the timing of any election
- Whether the timing of the communication and identification of the candidate are related to a non-electoral event such as a scheduled vote on specific legislation by an officeholder who also happens to be a candidate for public office.¹¹

Remember that if your organization makes a statement advocating a public policy (without even mentioning a political candidate), that may be subject to the lobbying limitation explained above.

In recent years, there has been some loosening in the enforcement of the prohibition on political campaigning. For example, in 2017, the administration issued an executive order telling the Treasury Department to be lenient in enforcement.

And in a recent 2025 case, the IRS settled with two churches who alleged that the prohibition against campaigning violated the First Amendment rights of free speech and exercise of religion.¹² In the settlement, the IRS agreed that good faith communication between a house of worship and its congregation on electoral politics is different from

participating or intervening in a political campaign. It is too early to say whether this case foreshadows a significant change in the IRS interpretation of the prohibition. Organizations for now should remember that this case has a narrow application to houses of worship and, in practice, may only apply to the two churches involved.

6. Watch your funding sources (avoid unintentional private foundation treatment).

By default, all exempt organizations under Section 501(c)(3) are private foundations unless they qualify as public charities. Both public charities and private foundations are exempt from tax and can receive deductible donations. But it is preferable to be classified as a public charity rather than a private foundation because a private foundation is subject to excise taxes and to more reporting requirements and restrictions on how it can operate.

Certain organizations may qualify as public charities based on their activities, such as schools, churches, and organizations which support the activities of other exempt organizations.

But those who don't qualify based on their activities may have to qualify by showing that a sufficient amount of their funding sources is "public." There are two separate public support tests, which are both based on whether the organization receives at least one-third of its income from so-called "good support."

- The first alternative one-third test is based on whether the entity receives at least one-third of its financial support from donations from a broad base of people, grants from the government, or other public charities.¹³ Good support under this test includes gifts, grants, contributions, and membership fees. The requirement for broad base support is intended to prevent control by a small group of donors. Therefore, good support does not include donations from a donor who donates too much of the total support of your organization. In particular, private donations from one donor count as good support only to the extent they do not exceed 2% of your total support.¹⁴

- The second alternative one-third test is basically the same as the first test but also includes funds from the organization's programs (exempt function income). This test is meant for organizations that run programs for the public and don't rely entirely on donations, such as a museum or symphony. This second test depends on whether the entity receives at least one-third of its financial support from a combination of: (i) a broad base of people who pay for goods or services from programs operated by the organization (exempt function income); (ii) member dues; (iii) a broad base of donations; and (iv) investment income. It has the same restrictions intended to prevent control by a small group. For the exempt function income, gross receipts received from one person are good support only up to \$5,000 or 1% of total support, whichever is greater.¹⁵ For the donations, private donations from one donor count as good support only to the extent they do not exceed \$5,000 or 2% of total support.¹⁶

These one-third good-support tests are calculated and reported each year on the organization's Form 990. If your organization fails the test on a four-year average, it may be reclassified as a private foundation. If your organization relies on a one-third test, it should pay special attention to this formula and whether it will continue to meet the tests in upcoming years. Not every aspect of the one-third tests is included here, so we recommend you contact your tax adviser or Miller Canfield attorney for additional information.

7. Stick to your specific exempt purpose.

Exempt organizations are not multi-purpose vehicles. For-profit businesses can undertake any legal activity and can switch from one activity to another, but exempt organizations must stay within their original exempt purpose. For example, an organization formed as a school cannot decide to change its purpose and become a homeless shelter without permission from the IRS.

If possible, exempt organizations should review their original exempt purpose on their application for exemption (Form 1023). They should also

periodically monitor their activities to make sure they are in line with their original and ongoing mission. To change the purpose or activities of your organization, check with your attorney to make sure your new activities fit within your exempt purpose. If not, you may find that you need to create a new exempt entity for your new project.

8. Avoid excessive income from an unrelated trade or business.

Exempt organizations are allowed to have some income from an unrelated trade or business without losing their exempt status. Unrelated business income is taxable and reported on Form 990-T. At some point, if an exempt entity has too much unrelated business income, it can threaten its exempt status.

Under Section 513, an unrelated trade or business is any trade or business which is not substantially related to the exempt purpose of the entity and is regularly carried on. For example, if a church runs a restaurant or a hospital runs a coffee shop, those would both be an unrelated trade or business. They are allowed to have these businesses but would have to pay taxes on the income and should make sure that the unrelated business income does not become excessive compared to their exempt purpose income.

Passive income is generally not considered unrelated business income. If your organization has unrelated business income, it should regularly monitor the scope of these activities to make sure it remains insubstantial in comparison to its exempt activities.

9. Avoid activities that are illegal or contrary to public policy.

An entity cannot be exempt if its activities are illegal or contrary to public policy. For example, an organization formed to promote world peace and disarmament did not qualify as exempt because its primary activity was the sponsorship of antiwar protests where it urged participants to violate local ordinances and breach public order.¹⁷ The IRS and the courts have also held that racial discrimination is against public policy, and therefore revoked the exempt status of schools that discriminate based on race.¹⁸

Recently, it was reported that the Trump administration has sought to use the illegality doctrine when the IRS argued that campuses with pro-Palestine protests were supporting terrorism and should lose their exempt status. However, IRS lawyers hindered these attempts by arguing that the law requires the IRS to produce a lengthy record of an investigation, which could take years.

This “public policy” doctrine has not been extensively used for revocations in the past. That said, it’s conceivable that the administration may take an aggressive approach to the meaning of “contrary to public policy” to challenge exempt organizations by asserting discrimination or promotion of unlawful acts.

10. Perform due diligence on grantees, funders, fiscal sponsors, partners, and employees.

If your organization will receive funding, provide funding to another organization, or have an ongoing relationship, you should examine the history and good standing of the other organization. For grant giving, you should enter into a formal grant agreement which requires ongoing certifications regarding the use of your grant for future years.

11. Consider other nonprofit classifications.

A Section 501(c)(3) organization is only one of the

many kinds of tax-exempt organizations listed in the Code. If your organization’s activities don’t fit into the charitable/educational mold, you may have other options. For example, here are some common Code Sections used for other kinds of tax-exempt entities:

- 501(c)(2)/501(c)(25): Title holding organizations can hold the title to real estate on behalf of other nonprofit organizations.
- 501(c)(4): Social Welfare Organizations can be used to advocate for litigation and policy, unlike a Section 501(c)(3) organization.
- 501(c)(6): Business Associations allow members of a profession or those with a common business interests to promote their industry through educational and networking programs.
- 501(c)(7): Social Clubs allow members to pool their resources for recreational purposes, such as a hockey team or boat club. They do not have to have a charitable purpose.

Donations to these other types of entities, however, may not be tax deductible to the donor. Contact a Miller Canfield tax attorney to strategize on the best form for your organization.

» WHAT IS THE LEGAL PROCEDURE TO REVOKE A FEDERAL TAX EXEMPTION?

If the IRS revokes an organization’s exemption, it must comport with constitutional law principles, including free speech, equal protection, and due process.

To protect equal protection and due process, the IRS must follow its own administrative procedures, as explained below. First, the IRS would issue a proposed revocation of exemption, usually without judicial review. Next, the exempt organization goes through the administrative process with the IRS, such as responding to a 30-day letter and providing any requested information. Once the taxpayer’s administrative remedies have been exhausted, and if the revocation is confirmed, the organization

may contest the revocation in one of three courts: the Tax Court; the U.S. District Court for the District of Columbia; or the Court of Federal Claims.

1. The Revocation:

An organization’s exempt status may be revoked by the IRS, courts, or Congress in one of the following ways:

- IRS Notice
- Legislation
- Tax treaty
- A decision of the Supreme Court

- Temporary or final regulations
- Revenue Ruling or Revenue Procedure
- Statement in the Internal Revenue Bulletin
- Automatic Revocation (if an organization fails to file a required annual return (Form 990) for three consecutive years)²⁰

The revocation must be based on a legal reason—on a failure to meet one of the above Section 501(c)(3) requirements. Common reasons for revocation in the past have been private benefits, private inurement, acting outside your exempt purpose, or substantial unrelated income.

2. Administrative Remedies

IRS procedures (Rev. Proc. 2025-5) lay out the administrative process for a revocation along with the taxpayer's rights to contest a revocation. First, the IRS (through Exempt Organization Determinations) must issue a notice of proposed revocation giving the organization at least a 30-day opportunity to contest.²¹ The notice of proposed revocation must: (1) include a detailed discussion of the basis for the IRS's revocation decision; and (2) inform the organization of its opportunity to protest/appeal the decision and request a conference with the Independent Office of Appeals.



To appeal, the organization must submit a protest letter, which is a statement of facts, law, and arguments in support of its position within 30 days from the date of the proposed adverse determination letter.

The organization must also state whether it requests an Appeals Office conference. Exempt Organization Determinations will review the protest and, if rejected, forward it to Appeals. Appeals will either issue a final revocation letter or schedule a conference first.

The revocation typically takes effect when the IRS issues a final adverse determination letter.

The opportunity to appeal and the right to a conference are not applicable in cases involving fraud, jeopardy, a quickly approaching statute of limitations, or where immediate action is necessary to protect the interests of the federal government.

3. Judicial Review

An exempt organization must exhaust administrative IRS remedies before it seeks declaratory judgment from a court on a proposed revocation.²² It is considered to have exhausted administrative remedies when it has no more appeals after it has been informed that revocation is recommended, but the organization doesn't have to wait for the IRS to issue an official "proposed revocation," or an "adverse determination."²³

After administrative remedies have been exhausted, the organization may contest the revocation in one of three courts: the Tax Court; the U.S. District Court for the District of Columbia; or the Court of Federal Claims.²⁴ This right to judicial review is explicitly provided by statute in Code Section 7428.

Generally, an organization's exemption will remain revoked during the course of court proceedings but may be retroactively reinstated if the court finds in favor of the organization.²⁵

4. Recent Executive Actions Threatening Exempt Organizations

The current administration has issued several documents focusing on exempt organizations. For example, on March 7, 2025, President Trump issued an executive order ("EO") called "Restoring Public Service Loan Forgiveness." That order requested revisions to the definition of public service to exclude certain organizations, such as organizations that aid or abet violations of immigration law, fund terrorism, promote gender affirming care, or engage in a pattern of disorderly conduct, public nuisance, vandalism, or obstruction of highways. Although this EO did not mention exemption revocation, it provides insight into the types of organizations that may receive greater scrutiny for revocation.

Other executive orders have focused on diversity, equity, and inclusion programs (DEI)—a main tenet of many exempt organizations.²⁶

Most recently, on September 25, 2025, the administration published a Memorandum titled, “Countering Domestic Terrorism and Organized Political Violence.” The document instructs government officials, including the IRS, to “investigate, prosecute, and disrupt entities and individuals engaged in acts of political violence and intimidation designed to suppress lawful political activity or obstruct the rule of law.” The IRS specifically is directed to take action against tax-exempt entities that fund “political violence or domestic terrorism.” In addition, the IRS is told to refer such organizations, and their employees and officers, to the Department of Justice for investigation and possible prosecution.

Moreover, The Wall Street Journal reported that a senior IRS official has created a list of potential targets for investigation.²⁷ The Trump administration is also reportedly seeking to make changes to IRS structure to allow it to pursue criminal inquiries of left-leaning groups more easily.²⁸ For example, it plans to weaken the involvement of the IRS Office of Chief Counsel in criminal investigations and install Trump allies in the IRS Criminal Investigation division.

Although the president is not authorized by the Constitution or federal law to unilaterally revoke the exempt status of a Section 501(c)(3) organization, these actions send a powerful message that the president intends to aggressively use existing tools to promote his policies and to challenge organizations which he believes act against those policies. Organizations would be well advised to plan accordingly.

» CAN THE IRS RETROACTIVELY REVOKE AN ORGANIZATION’S EXEMPT STATUS?

The IRS may retroactively revoke exemption and has broad discretion to do so.²⁹ But the decision to make a revocation retroactive is also reviewable by the courts. The IRS Commissioner also has discretion to limit retroactive revocation to the extent necessary to avoid inequitable results.³⁰

IRS guidance states that revocation or modification of an exemption determination may be retroactive in certain situations, including if:

1. There has been a change in applicable law;
2. The organization omitted or misstated material information. A misstatement of material information includes an incorrect representation or attestation as to the organization’s organizational document, the organization’s exempt purpose, the organization’s conduct of prohibited and restricted activities and the organization’s eligibility to file a short-form application (Form 1023-EZ); or
3. The organization operated in a manner materially different from that originally represented in an application for recognition of exemption.³¹

The courts have also upheld retroactive revocation in cases outside the circumstances outlined in the official guidance. For example, the Tax Court upheld the retroactive revocation of the exempt status for an organization that raised funds for schools when the schools did not show they had adopted IRS-required racial nondiscrimination policies. The organization claimed that revocation could not be retroactive because the cause did not fit into one of the above categories, but the court upheld the retroactive revocation.³²

On the other hand, the regulations also state that a retroactive revocation “will *ordinarily* take effect no later than the time at which the organization received written notice that its exemption ruling” might be revoked (emphasis added).³³

IRS procedures also allow an organization to formally request relief from retroactive revocation.³⁴ The request must be in writing and submitted to the agent or specialist assigned to the case.

» WHEN CAN THE IRS START COLLECTING TAXES FROM A REVOKED ORGANIZATION?

When an organization's exemption is revoked by a final determination letter or otherwise, it becomes a taxable nonprofit corporation, liable for regular federal income tax imposed on corporations. If the organization fails to pay taxes, the IRS may start proceedings to assess and collect tax due.

Even so, the IRS cannot attempt to collect tax due without at least notifying the organization of the basis of its revocation. Also, the IRS may only collect income tax for "open" years. A tax year is generally only open for three years since its tax return was filed, absent fraud or abuse.



An exempt organization's Form 990 informational annual return filed in good faith starts the clock on the statute of limitations, even though no taxes are payable on an informational return.

» WHAT LEGAL LIMITS APPLY TO THE GOVERNMENT IN REVOCATION PROCEEDINGS?

The government is limited by the Constitutional protections of due process and equal protection.

The IRS must follow its own procedures, and it must follow them equally for all kinds of organizations.

Further, under case law, if a revocation was prompted by political or similar considerations that demonstrate a lack of objectivity by the IRS, the revocation becomes null and void.³⁶ Courts are concerned not only with direct political intervention, but also with the creation of a political atmosphere that may affect the objectivity of those participating in the case.

Neither the Constitution nor federal law authorize the president to unilaterally revoke the exempt status of a Section 501(c)(3) organization. Code Section 7217 expressly prohibits the president, vice president and their employees from requesting an audit of a particular taxpayer. Any employee of the IRS receiving any such request must report it to the Treasury Inspector General for Tax Administration.³⁷ The criminal consequences extend to revenue officers or agents who participate in illegal audits requested by the president or fail to report them. The permitted punishment is a fine of up to \$5,000 and/or prison time up to five years.

Another law (Code Section 7214) also applies to revenue officers who engage in "any extortion or willful oppression under color of law," punishable by a fine of up to \$10,000 and/or prison time up to five years.³⁸

Furthermore, any illegal investigations of tax-exempt organizations may also violate taxpayer privacy laws, which include a private right of action that allows taxpayers to sue for damages when their tax data is unlawfully inspected or disclosed, in addition to criminal penalties. Under those privacy laws, federal officers are prohibited from willfully inspecting a return for a purpose other than one specifically authorized by law.³⁹

Furthermore, the government cannot disclose return or return information (which may include the public announcement of an investigation) under Section 7431.

Finally, if a revocation is successful, the organization will continue to exist as a nonprofit corporation under state law absent a state law to the contrary. The IRS has no ability to dissolve an organization, seize its assets, or take control of it.

» IF THE GOVERNMENT THREATENS OUR EXEMPTION, WHAT SHOULD WE TELL OUR DONORS? ARE THEIR CONTRIBUTIONS STILL TAX DEDUCTIBLE?

You should never give tax advice to your donors about their deduction. Instead, you should explicitly tell them to consult their own tax advisors regarding their taxes. But you can and should tell them the status of your exemption.

During the process of contesting a revocation administratively with the IRS or during any court process, qualifying charitable donations remain deductible. And if the organization is found to be exempt, then donations to it are treated as if they qualified as deductible donations under Section 170 for the whole time that the case was pending.⁴⁰

For cases in litigation, donations by individuals or other public charities may continue to be deductible during the litigation period, even if the court ultimately upholds the revocation.⁴¹ But if the court upholds the revocation, this relief is only available up to \$1,000 per donor. If the court rejects the revocation, donations made during the litigation period become entirely deductible subject to other limitations on charitable deductions.⁴²

If there is an adverse determination, you should inform your donors of the effective date of your revocation. But you should not try to advise them on the deductibility of their donations.

Tax exempt entities are presently navigating complicated times, perhaps more challenging than any other time. The best way forward is to remain true to the fundamentals, take an honest and unsparing look at your organization's compliance with the basic requirements for exempt status, communicate with others in the tax-exempt community, and prudently prepare to weather any storm. As the nursery rhyme teaches, better to have a house made of brick than one of straw or sticks.



This material is for educational purposes only and does not constitute legal advice. Consult your attorney for guidance regarding your specific circumstances.

FOOTNOTES

¹ Unless otherwise noted, all references to “Code” or “Section” are references to the Internal Revenue Code of 1986, as amended.

² Code Section 4958(f).

³ Code Section 4958(c).

⁴ Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii).

⁵ *American Campaign Academy v. Commissioner*, 92 TC 1053 (1989).

⁶ Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii); Rev. Rul. 72-147, 1972-1 C.B. 147

⁷ PLR 9615030.

⁸ Treas. Reg. Section 1.501(c)(3)-1(c)(3)(ii).

⁹ Treas. Reg. Section 56.4911-2(d)(3).

¹⁰ Rev. Rul. 2007-41, 2007-1 CB 1421.

¹¹ *Id.*

¹² *National Religious Broadcasters v. Long*, Civil Action No. 6:24-cv-00311, E.D. Texas.

¹³ Code Section 170(b)(1)(A)(iv).

¹⁴ Treas. Reg. Section 1.170A-9(f)(6).

¹⁵ Code Section 509(a)(2)(A).

¹⁶ Code Section 507(d)(2).

¹⁷ Rev. Rul. 75-384.

¹⁸ *Bob Jones University v. U.S.*, 462 U.S. 574 (1983).

¹⁹ Brian Schwartz, Richard Rubin and Joel Schectman, *Trump Team Plans IRS Overhaul to Enable Pursuit of Left-Leaning Groups*, Wall Street Journal, October 15, 2025.

²⁰ Rev. Proc. 2019-5, Section 12.01. Automatic Revocation under IRC Section 6033(j) has separate procedures for reinstatement.

²¹ Rev. Proc. 2025-5, Section 9.

²² Code Section 7428.

²³ *Anclote Psychiatric Center Inc.* (1992) 98 TC 374.

²⁴ Code Section 7428.

²⁵ See Code Section 7421(a).

²⁶ See this link (<https://www.councilofnonprofits.org/files/media/documents/2025/chart-executive-orders.pdf>) from the National Council of Nonprofits for a list executive orders affecting charitable nonprofits.

²⁷ Brian Schwartz, Richard Rubin and Joel Schectman, *Trump Team Plans IRS Overhaul to Enable Pursuit of Left-Leaning Groups*, Wall Street Journal, October 15, 2025.

²⁸ *Id.*

²⁹ Code Section 7805(b).

³⁰ *Automobile Club of Michigan*, 353 U.S. 180 (1957).

³¹ Rev. Proc. 2025-5, Section 12.03. Retroactive revocation may also apply to certain trusts that engage in certain prohibited transactions to divert funds away from its exempt purpose.

³² *Virginia Educ. Fund v. Commissioner*, 85 TC 743 (1985).

³³ Treasury Regulation Section 601.201(n)(6)(i).

³⁴ Rev. Proc. 2025-5, Section 12.04.

³⁵ Code Section 6501(g)(2).

³⁶ *Center on Corp. Responsibility, Inc. v. Shultz*, 368 F. Supp. 863 (D.C. Dist. 1973).

³⁷ Code Section 7217.

³⁸ Code Section 7214.

³⁹ Code Sections 6103 and 7431.

⁴⁰ Code Section 7824(c).

⁴¹ Code Section 7428(c)(1).

⁴² Code Section 7428(c)(2).