

## Four Fast Ways to Form a Charity to Address COVID-19-Related Matters

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In the face of the COVID-19 outbreak, groups ranging from small neighborhood projects to large national initiatives are mobilizing quickly to help. Many of those groups have questions about whether they can achieve their goals by starting a nonprofit – that is, by forming a new entity that qualifies as a tax-exempt charitable organization under Section 501(c)(3) of the Internal Revenue Code.

### Baseline: The regular process

Under normal circumstances, forming a new entity and obtaining an IRS tax-exempt determination letter takes anywhere from a few weeks to 10 months or longer, depending upon a variety of circumstances including the IRS' current volume of requests. After forming a legal entity (usually, a nonprofit corporation under state law), the organization will fill out and submit an application for tax-exempt status on [IRS Form 1023](#). A typical application package is 50 – 100 pages long with attachments, including the 28 pages of the application itself. The organization must then pay a \$600 filing fee and can expect to be contacted by the IRS within 180 days of submission with confirmation of receipt.

Donations received prior to the entity's application receiving approval from the IRS will generally be retroactively treated as tax-deductible contributions if the entity's application is approved. Such donations will not be tax-deductible if the entity's application is rejected by the IRS. Accordingly, many potential donors will insist on the receipt by the entity of a favorable determination letter from the IRS before contributing to the entity.

### Some faster alternatives

In this new COVID-19 world, many would-be founders of tax-exempt entities are asking how they can expedite this process.

#### Expedited option 1: Partner with an existing tax-exempt entity

Often the fastest and most efficient way to be up and running is to join with an existing tax-exempt entity that is already working in a manner complementary to the mission the new founders wish to pursue. Rather than form a new entity and seek tax-exempt status, the founders add the new mission to the operations of the existing tax-exempt entity. The founders, volunteers and donors do everything they would otherwise do with a new entity but under the umbrella of the existing tax-exempt entity. In addition to the obvious cost savings from not having to duplicate overhead expenses, the name recognition of the existing tax-exempt entity will frequently open doors that would not be available to a brand-new startup entity.

#### Expedited option 2: Set up a fiscal sponsorship with an existing tax-exempt entity

In this alternative, the founders establish a nonprofit entity. But rather than waiting to receive a determination letter from the IRS, the new nonprofit entity enters into a [fiscal sponsorship](#) agreement with an existing tax-exempt entity. Fiscal sponsorship is an

arrangement through which an existing tax-exempt entity supports a new project through a contract called a fiscal sponsorship agreement, and thus enables the project to immediately raise tax-deductible money to support a particular exempt purpose. The purpose of the project must further the mission of the sponsor, and typically, the project is responsible for raising its own money, which is donated to the sponsor. A fiscal sponsor typically retains 5 – 15% of the funds raised by the sponsored project. Sometimes fiscal sponsorship is temporary – either because the project is waiting for its own IRS Form 1023 application to be processed or because the project itself is temporary (disaster relief can be a good candidate for a temporary project) – and sometimes fiscal sponsorship is long-term. Since a fiscal sponsorship agreement is a private contract, it can be set up quickly. The setup time depends upon how quickly the project can secure a fiscal sponsor and how long the parties take to reach a negotiated agreement. This could be as little as a week, but three to four weeks is more typical.

Often the reputation of the fiscal sponsor can open doors that would not be available to a new startup entity operating on its own. Any existing 501(c)(3) tax-exempt entity can serve as a fiscal sponsor, but there may be some advantages to using an experienced fiscal sponsor that already has an infrastructure in place for supporting newly launching projects. This may be especially true in the context of COVID-19 for organizations that need to act quickly and focus their attention on real-time developments in current events. The San Francisco Study Center provides a [national directory of fiscal sponsors](#) that can be filtered by geographic area or subject matter, including disaster relief. Since the sponsoring organization will control the funds raised by the new project, it is important that any new organization chooses a sponsoring organization that has a good reputation as a fiscal sponsor and a good alignment with the work of the new project. New projects should ask to speak to other projects the sponsor has supported in the past as a reference check.

### **Expedited option 3: Request expedited review from the IRS**

The IRS allows organizations to request [expedited processing of a Form 1023 application](#) for certain compelling reasons, including disaster relief. It is likely not sufficient that the organization's activities would benefit victims of COVID-19 or frontline responders. The organization must demonstrate that it is organized to provide critical relief and that the organization's ability to serve those needs will be materially and adversely affected unless the application is reviewed expeditiously.

Applicants requesting expedited review must use the regular IRS Form 1023 and must attach a written statement that fully explains the compelling reason for expedited review. We strongly recommend including:

1. A brief description of the disaster, an immediate need and details of how the organization will provide relief
2. An explanation of the immediate need for the specific disaster relief services the organization provides

Financial circumstances can also provide a compelling reason for expedited review. A newly forming initiative with a scheduled major fundraiser or a commitment for a significant grant that is contingent upon the organization receiving tax-exempt status by a certain date may have a compelling reason for expedited review. In those cases, the organization's written request for expedited review should include, to the extent applicable:

1. A description of any pending grants, including information about the grantor and the amount or property to be received
2. An explanation of how the loss of the grant(s) might impact the organization's ability to operate and provide relief (and the relative value of such grant as a percentage of annual funding)
3. A statement explaining any other anticipated consequences should the expedited processing be denied
4. The date an exemption letter is required, if applicable

The IRS does not guarantee expedited review for all applicants who request it. If the applicant does not provide a compelling reason for the request or if the IRS chooses in its discretion not to grant expedited review, the IRS will review the application in

accordance with its regular procedures.

One potential disadvantage of requesting expedited review is that certain foundations may have policies or preferences against making grants to organizations that filed an expedited review because of a perception that the IRS has not vetted these applications as diligently as general applications. Organizations that plan to seek foundation funding should check in advance with potential grantors about policies related to the eligibility of grant recipients who obtained expedited review.

Another important note about expedited review is that it is difficult to predict the volume of expedited requests the IRS will receive related to COVID-19. Typically, a disaster is tied to a particular region, but the COVID-19 outbreak has affected the entire world, which is likely to substantially increase the number of emergency relief-related expedition requests submitted to the IRS in a relatively short timeframe.

## **Expedited option 4: Use the EZ form**

Organizations with projected gross receipts of less than \$50,000 per year for the first three years and total assets under \$250,000 may be eligible to file the shorter version of 501(c)(3) application, called the IRS [Form 1023-EZ](#). The EZ form is streamlined – just three pages, compared with the standard form's 28 pages. In our experience, processing time for an EZ application is typically two to six weeks rather than two to 10 months. The filing fee is \$275 for the EZ application instead of the \$600 fee for the standard application. Applicants must file the IRS Form 1023-EZ online at [pay.gov](#).

One potential disadvantage of using the EZ application is that, like the expedited review, certain foundations may have policies or preferences against making grants to organizations that filed using the IRS Form 1023-EZ, because the EZ application requires so much less information and transparency than the regular form. Organizations that plan to seek grant funding should check in advance with potential grantors about policies related to the eligibility of grant recipients who used the EZ application.

An organization using the EZ application cannot request expedited review, since all EZ applications are already expedited.

## **More information**

Please note that newly forming charitable organizations must comply with requirements beyond the steps referenced in this article, including registering with the offices of relevant state attorneys general, annual reports and tax filings. For more information about requirements for charitable organizations, see the resources available from the [IRS' Charities and Nonprofits webpage](#), the [National Council of Nonprofits](#) or [BoardSource](#). For more information about fiscal sponsorships, please reference this [guide](#) published by New York Lawyers for the Public Interest.

For more information about COVID-19 topics relevant to nonprofits and small businesses, please visit [Cooley's COVID-19 resource page](#).

### [Coronavirus resource hub](#)

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