

## TAX FAQ: 501 (c)(3) TRANSITION

As of March 30, 2010

Q1. What is AFA's tax status?

A. As of April 1, 2006, the Headquarters AFA organization became a 501(c)(3) tax exempt organization. On 24 September 2009, AFA was notified that Chapter and State organizations were exempt under section 501(c)(3), effective 8 February 2007, with a Group Exemption Number of 5392.

Q2. Did AFA Headquarters' Tax I.D. number change with the change in status?

A. Yes, on 1 April 2006:

- AFA assumed the Employer Identification Number (EIN) formerly belonging to the Aerospace Education Foundation (AEF) (52-6043929)
- AFA's former EIN (53-0177555) now belongs to the AFA Veteran Benefits Association (AFAVBA)

Q3. Are all AFA's subordinate units (regions, states and chapters) also 501 (c)(3) organizations now?

A. States and chapters submitted on our Group Exemption Request are included (regions are not "exempt organizations," but rather a management level). We did not include Schriever and Shooting Star Chapters on the exemption request at their request.

Q4. What does the retroactive date of 8 February 2007 for 501(c)(3) mean?

A. Only that this was the date when the first IRS management level recommended approval. The retroactive date is to our benefit, in that, you can claim your expenses (to the extent allowed) for all of 2009 and offer significant donors the assurance that their contributions were deductible (it probably would not be worth the effort to amend returns or find the records necessary for prior years).

Q5. Will Headquarters make copies of the appropriate documents available to the units?

A. Yes. Hard copies were provided to Region/State President's attending training in October, and we have posted all applicable guidance on our website under "Field Resources." (It is also as easy to download current documents from the IRS.gov website.) It is a good idea to download/save your own personal copies of the following reference documents in any case:

1. IRS Pub 4221-PC, *Compliance Guide for 501(c)(3) Public Charities* at: <http://www.irs.gov/pub/irs-pdf/p4221pc.pdf>;
2. IRS Pub 1771, *Charitable Contribution Substantiation and Disclosure Requirements* at: <http://www.irs.gov/pub/irs-pdf/p1771.pdf>; and
3. IRS Pub 557, *Tax-Exempt Status for Your Organization* available at: <http://www.irs.gov/pub/irs-pdf/p557.pdf>.

- Q6. Will AFA Headquarters set up a structure to provide tax advice and reporting for its subordinate units?
- A. No. AFA Headquarters' goal is for its subordinate units to be able to function essentially as they have for the past several decades as 501(c)(19) organizations. AFA's 501(c)(3) status will allow some units to expand their operations to include accepting charitable donations; however, AFA Headquarters will not set up a reporting system for all chapters to allow a few to engage in major charitable fundraising activities umbrella. The biggest stumbling block to doing this is state/local registration requirements. In any case, units are responsible for their own compliance and reporting at the local, state, and national level.
- Q7. How will the change of AFA from a 501(c)(19) organization to a 501(c)(3) organization affect my unit?
- A. Once the unit has transitioned to (c)(3) status in most cases (see FAQ below) they will not need to take any action or make any changes in their activities or reporting. AFA Headquarters annually reports to the IRS on the existence of chapter and state organizations formed under its group exemption (although individual units still must comply with IRS reporting, for example, Form 990, 990EZ or 990-N, as discussed below).
- Q8. What does 'in most cases' mean?
- A. Our goal was to be able to support chapters as subordinate (c)(3) organizations just as we did for all the years AFA was a (c)(19) organization. Most of our units' operations will not change substantially and neither should their administrative and reporting requirements. In some cases local or state law may require specific registration or reporting if they undertake charitable, fundraising activities (see below). Those units will be responsible to abide by local and state requirements and to comply.
- Q9. Don't some states require that (c)(3) organizations apply to them or register with them separately?
- A. Yes. This is an area of increased scrutiny for the IRS and local governments, so the caution about checking your own state's requirements applies. Chapter and state units that continue non-insurance, public education and patriotic activities previously accomplished as subordinate units under the 'old' AFA should be able to continue business as usual. If the state or chapter begins fund raising/charitable activities, some will be required to register and report. If in doubt, check with your state or with a tax or fund raising advisor familiar with the laws of your state. (Information on your state's requirements should be readily available from you State and/or local government on its official website, and a list of those websites is available on the AFA website under "Field Resources.")

Q10. Will I have to file an IRS Form 990 or 990-N?

A. ALL units are required to file the appropriate IRS reporting forms. Units are required to file an IRS Form 990 based on their normal (three-year average) gross receipts (not “net” after expenses). If those exceed \$25,000 per year, you will have to file a 990 or 990-EZ. (The \$25,000 limit goes to \$50,000 for the 2010 tax year.) There are also “total asset” thresholds, but the lowest of these is \$500,000.

Most of our chapters/states do not reach the 990 thresholds, but they are still required to file a 990-N “e-Postcard” electronically (this is the only way to file). This is a simple process, and there are step-by-step instructions available under “Field Resources” on the AFA website.

Q11. My chapter (or state) has also set up an independent 501(c)(3) organization. What will the effect on that organization be? Can we still have it?

A. Chapter (and state) established independent 501(c)(3) organizations can continue to operate just as they always have with no change. If the chapter/state independent 501(c)(3) is organized as a member-based organization, affiliating with AFA Headquarters as the chapter or state entity may be an option. Again, local and state legal advice on such issues is the responsibility of the chapter or state unit.

Q12. Will my chapter (or state) have to apply to the IRS for an individual tax designation as a 501(c)(3) organization?

A. Depends what one means by “tax designation.” All subordinate units are required to have their own EIN and also report that number to Headquarters (DO NOT attempt to get a new EIN unless HQ instructs you to do so – your current EIN has been transferred to the new GEN). Concerning a separate tax status or standing, that is not necessary; the Headquarters group exemption can be extended to cover all of our chartered units.

Q13. Will my chapter (or state) get a new EIN number? Do we have to re-file an SS-4 form?

A. NO. Your EIN has been transferred to the new Group Exemption Number 5392, but all states and chapters will **still require** an individual EIN, and if you have filed a new SS-4 and received a different EIN, you must inform Headquarters as soon as possible.

Q14. Will our ability to sponsor revenue generating programs to support chapter/state programs change when we become a (c)(3)?

A. That is entirely a chapter decision.

- If a chapter does not choose to offer a charitable tax deduction to participants, chapter revenue generating programs can continue just as they do now with no change in reporting requirements.
- If a chapter wants to offer charitable tax deductions, there will be additional recordkeeping and reporting requirements. Headquarters will provide guidelines that chapters will be expected to follow and report to Headquarters. States and chapters will be responsible for any local or state reporting that is required.

Q15. So just to be clear, my chapter WILL be able to offer a charitable tax deduction?

A. Yes, however if a chapter chooses to do so, it MUST also be prepared to take on additional administrative, recordkeeping and reporting responsibilities as well.

Q16. What sort of requirements would I have?

A. That depends on what your unit decides to do. In general you need to do the following:

- You must keep careful records of your expenses and revenues as well as of the donors/participants. These must be retained by the chapter as a primary responsibility and reported to Headquarters as part of the unit's quarterly reports.
- You must provide receipts to your donors for the amount of their gift.
- If that gift is part of a purchase price (e.g. a dinner or golf tournament) you must provide a receipt that shows how much of their payment represents 'fair market value received' and how much represents a 'charitable contribution' (the gross price less the fair market value of benefits received, e.g. golf tournament registration fee less greens fee, cart, tournament prizes, food and beverage and any other benefits). Cost is not the measure, so if you pay \$1000 for 20 dinners that would have sold for \$75 each, the fair market value is \$75 for each donor, not \$50 (1000/20).
- You must be able to show that funds raised in this manner were used for a permitted purpose under the 501(c)(3) exemption.
- Further, if such funds are for a designated educational purpose such as a scholarship, you must separately account for them and show that they went toward that purpose and no other. It would be prudent to keep them in a separate account. Your selection process should make it clear that members and their families should not be given any advantage in the scholarship selection process; those serving on the committee making such decisions should have no family member or business associate's family member competing for a scholarship.

Q17. Are separate books/accounts required for charitable activities and general operations of a chapter?

A. It would be prudent for chapters to establish separate accounts for each major charitable activity they undertake. For example, to manage an account for general activities of the chapter a 'general operating' account should be established. The general operating account may be funded by fund raising activities where no charitable benefit is received by the participants and donations to this account are for unrestricted use. To manage and account for contributions received for a specific charitable purpose a separate account should be established for each of these activities. For example, establish a scholarship account to manage all donations to the chapter scholarship fund, and establish a separate account for an annual charity golf event to manage this event and its proceeds.

Q18. How can money be used?

A. To answer how money can be used, you first must determine if any restrictions have been placed on the contribution by the donor. If the donor specifically calls for the money to be used for scholarships, then you must ensure the donation is only used for that purpose. If the contribution is in support of a symposium or special education event, the money must be

used for this purpose. If no restriction is attached to the donation, the funds received are available for all legal activities of the chapter.

Q19. What kinds of things qualify as charitable events?

A. The question is really whether the sponsor (the AFA unit) represents any or all of the gift, donation or payment for the event as a tax-deductible, charitable contribution. For example, let us take a chapter dinner.

- The chapter may charge the EXACT COST of the dinner. In that case there are no funds raised and NO charitable deduction.
- The chapter may charge MORE than the exact cost of the dinner but not represent the difference as a charitable contribution. In that case funds have been raised but no special accounting or documentation is required and no receipt need be given the participant/donor.
- The chapter may advertise the event as being “charitable,” in which case there is a need for additional record keeping. In that case careful records must be kept not only of the actual cost and amounts received, but also of the estimated FAIR MARKET VALUE of the dinner. Fair Market Value can be determined from what a comparable restaurant would charge a single customer for his or her meal, or if it is held in a hall, it can be the actual expenses which are then marked up to reflect the difference between wholesale cost and retail value of what donors receive; each participant/donor must be given a receipt for the amount of their donation (amount paid less the estimated fair market value of their dinner and the event must be reported to Headquarters both on a net cost (total revenue minus cost) and a net of fair market value donation basis (total revenue minus fair market value per attendee) as part of the chapter’s quarterly financial report.
- A simple question for any chapter, state or region to ask when determining if payment to an event includes a charitable donation is whether there was anything tangible received in return for the payment – lunch, dinner, golf, air show ticket, exhibit space, etc? If so, the amount paid minus the fair market value of the tangible benefit equals the charitable donation. It is the *retail* [fair market] value of items, such as a dinner, not the wholesale cost incurred by the hosting unit that must be deducted. Your good faith estimate, if documented, will be acceptable.
- An easy and very clean way for a chapter, state or region to distinguish the difference from paying for something tangible and making a donation is for the invitation or receipt for an event to specifically state that \$X dollars of the price is a charitable donation for the purpose of: 1) funding chapter operations, or 2) funding a chapter scholarship, or 3) funding education outreach activities, or 4) funding Vision Classrooms, etc.

Q20. Isn’t there a cutoff amount for when I have to provide a receipt to a donor?

A. Yes. Generally speaking you need not provide such a receipt to a donor if the amount paid is less than \$75 or no tangible benefits were provided. However, if a receipt is requested you should be fully prepared to provide it as a sound business practice. You should also be aware that if the donation exceeds \$250, the donor is required to have a formal receipt from the receiving organization (the AFA unit) in order to take an income tax deduction. You should be prepared to provide this receipt as well.

Q21. Are AFA dues tax deductible?

- A. No. Members receive goods (*AIR FORCE* Magazine and other mission specific services) for their dues payment, so dues are not deductible.
- Only ‘contributions’ are deductible. For example if a member receives an annual renewal notice of \$45 but sends in \$70, the extra \$25 may be considered a contribution that is tax deductible.
  - Keep in mind that how dues are handled on an individual’s tax return is something over which AFA has no control, and much depends on the individual’s personal tax status and method of filing. Some members may decide to deduct their dues payment as a business expense (Professional Organization dues) but AFA doesn’t give tax advice and members should be told to consult a tax professional.

Q22. Are convention or conference registration fees tax deductible?

- A. They would not be deductible due to AFA’s 501(c)(3) status unless they specifically include a contribution for a charitable purpose (e.g. a registration includes a specific amount to be contributed to a scholarship fund.) Whether they are otherwise deductible as a business expense would depend on the individual’s personal tax status and method of filing.

Q23. Does the above Q&A pertain to the national convention and conference or for my own state convention?

- A. AFA Headquarters will specify what, if anything, is deductible for any events it sponsors. States (or chapters) will have to make their own determination and comply with procedures regarding the use of the funds and providing recipients receipts if the amount of the donation exceeds \$250 (\$75 if some *quid pro* gift or benefit flows back to the donor) or to make clear what portion of a fee charged for an event is over and above the cost of the event and can therefore be considered a charitable contribution.

Q24. What about Community Partner dues? Are those deductible?

- A. For the overwhelming majority of Community Partners the question is moot.
- Community Partners are businesses and most treat the entire amount of their fee as a business expense. In the future they can do the same and most will, even those who pay more than the standard \$90 fee.
  - In any case, the same logic applies as for any other donation. The Community Partner arrangement is that the business pays the chapter \$XX.00 – normally \$90.00. From that, the chapter pays AFA \$45.00. This latter portion is not tax-deductible. So the question is about the dollars represented by (\$XX.00 minus \$45.00), regardless of whether that ‘\$XX.00’ is \$75.00 or \$1500.00.
  - The chapter can accept the difference in the Community Partnership fee as a tax-deductible contribution on the same basis as it would any other such contribution, the extent that the money it receives (less the \$45.00 that goes to Headquarters) represents a true contribution and not payment for additional services or products received – such as greens fees for a golf tournament, dinners, etc. If the chapter chooses to do that, they must do just as they would for any charitable contribution: provide the donor clear documentation of how much of the fee is a charitable donation and how much represents

payment for services. The chapter must keep copies for their own records, and if the donation is directed toward a specific purpose, for example, a scholarship, then that money must be spent for the designated purpose.

Q25. Will there be specifics on how to use our tax deductible, tax exempt status to avoid paying state sales taxes and other local taxes.

A. No. State and local laws vary widely. There is no uniform answer for all. Each unit will have to determine what it needs to do to be in compliance with local laws and regulations.

Q26. Will chapters have to report their spending using the same chart of accounts that Headquarters uses? If not, then how can Headquarters report without requiring the same level of detail from the chapters?

A. No.

- Chapters are not required to use the parent's chart of accounts. The financial reports submitted by chapters do not flow into AFA Headquarters' financial statements so there's no need to have consistent account numbers. This leads to the question, "if chapter activities don't flow into the parent's financial statements, why must we send in a report?" To wit...
- Chapters are covered by a 'group exemption,' therefore AFA Headquarters (the parent) has an obligation to assure that chapters, covered by that exemption, are operating consistently with the tax exempt purpose. Our due diligence requirement is met by reviewing chapter reports submitted. That way, if we are audited by IRS, we have documentary evidence from the chapter that their activities are consistent with the exempt purpose.
- The only exception is in reporting on legislative activity (see below).

Q27. What is legislative activity reporting about?

A. Chapter or state activities which are specifically related to contacting Congress or other government officials seeking support for legislation will require special reporting to Headquarters. Because AFA has made the 501(h) election with IRS to have its legislative activity measured objectively, each chapter must also keep track of its legislative activity and report this to Headquarters annually. Headquarters will provide a standard format for reporting these types of activities to it, and this form will also enable any chapter that files its own form 990 EZ (because it normally has over \$25,000 in gross receipts ) to provide the figures required on that form; those chapters should also make the 501(h) election. Since both AFA and all of its chapters are tested together as one unit to make sure there is no excess legislative activity, it makes sense for each chapter that can do so to make the 501(h) election; this will make it less likely any chapter would ever lose its tax exemption for excess lobbying. Since Form 990-N does not at present have a place to make the 501(h) election, there is nothing chapters filing that form can do, but similarly, their funds available for legislative activity are similarly limited. AFA will make it clear, in the case of inquiry by IRS, that such chapters are already covered by the 501(h) rules, but those filing a form 990 or 990-EZ should specifically make the election.