



Rebuttable Presumption - Intermediate Sanctions

If an organization meets the following three requirements, payments it makes to a disqualified person under a compensation arrangement are presumed to be reasonable, and a transfer of property or the right to use property is presumed to be at fair market value. The three requirements for establishing the rebuttable presumption are:

- 1) The compensation arrangement must be approved in advance by an authorized body of the applicable tax-exempt organization, which is composed of individuals who do not have a conflict of interest concerning the transaction,
- 2) Prior to making its determination, the authorized body obtained and relied upon appropriate data as to comparability, and
- 3) The authorized body adequately and timely documented the basis for its determination concurrently with making that determination.

The documentation of the authorized body should include the terms of the transaction and the date of its approval, the members of the authorized body present during the debate and vote on the transaction, the comparability data obtained and relied upon, the actions of any members of the authorized body having a conflict of interest, and documentation of the basis for the determination.

The Internal Revenue Service may refute the presumption of reasonableness only if it develops sufficient contrary evidence to rebut the probative value of the comparability data relied upon by the authorized body.

If an organization does not satisfy the requirements of the rebuttable presumption, a facts and circumstances approach will be followed.



Exemption Requirements - 501(c)(3) Organizations

To be tax-exempt under section 501(c)(3) of the Internal Revenue Code, an organization must be organized and operated exclusively for exempt purposes set forth in section 501(c)(3), and none of its earnings may inure to any private shareholder or individual. In addition, it may not be an *action organization*, i.e., it may not attempt to influence legislation as a substantial part of its activities and it may not participate in any campaign activity for or against political candidates.

Organizations described in section 501(c)(3) are commonly referred to as *charitable organizations*. Organizations described in section 501(c)(3), other than testing for public safety organizations, are eligible to receive tax-deductible contributions in accordance with Code section 170.

The organization must not be organized or operated for the benefit of private interests, and no part of a section 501(c)(3) organization's net earnings may inure to the benefit of any private shareholder or individual. If the organization engages in an excess benefit transaction with a person having substantial influence over the organization, an excise tax may be imposed on the person and any organization managers agreeing to the transaction.

Section 501(c)(3) organizations are restricted in how much political and legislative (*lobbying*) activities they may conduct. For a detailed discussion, see Political and Lobbying Activities. For more information about lobbying activities by charities, see the article Lobbying Issues; for more information about political activities of charities, see the FY-2002 CPE topic Election Year Issues.

Additional Information

- Application Process Step by Step: Questions and answers that will help an organization determine if it is eligible to apply for recognition of exemption from federal income taxation under IRC section 501(a) and, if so, how to proceed.
- Private foundations - requirements for exemption
- *Tax-Exempt Status*- online training available at the IRS microsite StayExempt.irs.gov.



Exempt Purposes - Internal Revenue Code Section 501(c)(3)

The exempt purposes set forth in section 501(c)(3) are charitable, religious, educational, scientific, literary, testing for public safety, fostering national or international amateur sports competition, and preventing cruelty to children or animals. The term *charitable* is used in its generally accepted legal sense and includes relief of the poor, the distressed, or the underprivileged; advancement of religion; advancement of education or science; erecting or maintaining public buildings, monuments, or works; lessening the burdens of government; lessening neighborhood tensions; eliminating prejudice and discrimination; defending human and civil rights secured by law; and combating community deterioration and juvenile delinquency.

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Inurement/Private Benefit - Charitable Organizations

A section 501(c)(3) organization must not be organized or operated for the benefit of private interests, such as the creator or the creator's family, shareholders of the organization, other designated individuals, or persons controlled directly or indirectly by such private interests. No part of the net earnings of a section 501(c)(3) organization may inure to the benefit of any private shareholder or individual. A private shareholder or individual is a person having a personal and private interest in the activities of the organization.

[Return to Life Cycle of a Public Charity](#)

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