



DID YOU KNOW?

Did you know that a nonprofit organization is not the same as a tax-exempt organization?

Nonprofit (or in some states, such as Illinois, not-for-profit) status is a function of state corporate law. Most nonprofit entities are organized as corporations, though in recent years, state laws have allowed for the creation of nonprofit limited liability companies as well. Whether or not an organization is “nonprofit” simply indicates that the governing documents stipulate that no private interest is served by the organization, and for this reason, some states (such as Delaware and Virginia) call these entities “nonstock” corporations.

Whether or not an organization is tax-exempt is a function of federal tax law. Most (if not all) organizations recognized as “tax-exempt” are organized as nonprofit/not-for-profit/nonstock entities under the applicable state corporate law. Being organized as a nonprofit is not sufficient, however, to be recognized as tax-exempt. An organization must petition the IRS for recognition as a tax-exempt organization through filing an application with the IRS depending on the type of tax-exempt status sought. The most common type of tax-exempt organization is a charitable organization recognized under Code Section 501(c)(3). However, there are many other types of tax-exempt organizations such as business leagues (like chambers of commerce), social clubs, cemeteries, fraternal organizations, and many more. The process and IRS timing varies based on the status sought.

Bottom Line: While many organizations are both nonprofits and tax-exempt, being organized as a nonprofit is not sufficient to become tax-exempt, nor is it automatic. When counseling clients about the creation of a “nonprofit” or a “501(c)(3)” entity, it is important to fully understand what the client intends to accomplish. Assuming a client intends to set up a charitable organization (the most common request we receive), it is best to advise the client that there are two phases – (i) the state law incorporation and governance set-up and (ii) the petition to the IRS for tax-exempt status. Finally, both state corporate law and federal tax law have ongoing compliance obligations, and the client should be mindful of meeting those going forward.

If you have any questions, please contact the author or one of Taft’s Tax attorneys.



[Megan Okun](#) / (513) 357-9631 / mokun@taftlaw.com

***To be sure of hitting the target, shoot first, and call whatever you hit the target. --
Ashleigh Brilliant***