

Tipping and the IRS Public Support Test: A Simple Primer

What is tipping?

“Tipping” occurs when a donor, other than another charity, makes so large a grant to a publicly supported charitable nonprofit that it fails the IRS public support test. The public support test is a mathematical formula that provides a percentage of the total of revenue generated in a year by a nonprofit which comes from the general public, other nonprofits and the government. All charitable nonprofits must pass a public support test on a regular basis. You can fail the public support test by receiving a large grant from a single donor which is commonly referred to as “*being tipped out of public charity status*” and reclassified by the IRS as a *private foundation*. If the granting entity is a private foundation (PF), it is essentially precluded from giving a grant to another PF. Therefore, if you are seeking grants from a PF, you do not want to be one yourself. As such, a PF that is planning to give you a large grant wants to be certain that you are not *tipped* into private foundation status simply because of their grant.

What are the consequences of being a private foundation?

Any organization that is *tipped* into private foundation status will be required to file a different, far more complex tax return and will be subject to an excise tax on net investment income. Living donors will be more restricted in what portion of their gifts will be deductible as charitable contributions, and your scholarship programs will need to be approved in advance by the IRS. Perhaps the biggest consequence is that the organization will not be eligible for grants from other private foundations like the Rasmuson Foundation. Most PFs will not make grants to other PFs because of very complex rules and potential tax liability.

A Possible Solution to a One-Time problem

If your organization is applying for a large grant from a PF, which can often be the case during a capital expansion project, there is a potential it could *tip* your organization into private foundation status. If this happens, you should seek guidance from a Certified Public Accountant (CPA) in advance of your request. If the grant *tips* your nonprofit, one option may be to ask the IRS if they will consider the donation an “unusual grant.” An unusual grant is not considered in calculation of public support by the IRS and therefore will not *tip* you. The request from the IRS is filed on Form 8940 along with a user fee. To qualify you must show that the grant is unusually large, unexpected, and one that might *tip* the organization.

For more information or help with fund development planning, please connect with us at info@forakergroup.org or 907-743-1200.