

# IRS Loosens, and Tightens, Disclosure of Nonprofit Taxpayer Information

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On August 16, 2022, the Internal Revenue Service issued a final regulation on its ability to provide state governments with information regarding organizations seeking to become exempt and those already exempt from federal income taxation under Section 501(c) of the Internal Revenue Code.<sup>1</sup> The new rule was initially proposed on March 15, 2011,<sup>2</sup> however, its provisions were not finalized until now.

General counsels of established and well-known nonprofits will likely not have an issue with this new rule, but fledging nonprofits facing compliance and revocation issues should take note.

Previously, the IRS shared only certain taxpayer information with authorized officials of state governments, specifically: the IRS could disclose to such state officials (1) whether the IRS refused to recognize an entity as exempt from taxation or (2) whether an entity already exempt was operating in a manner not meeting or no longer meeting the requirements to be a tax-exempt organization.<sup>3</sup> Importantly, the IRS would only make such disclosures upon a final determination.<sup>4</sup>

## Disclosures No Longer Require a Final Determination

Although the federal statute authorizing such disclosures does not require the IRS to have already made a final determination, it provides the IRS with broad discretion in determining when it may disclose certain information to state governments.<sup>5</sup> The new rule has, among other things, removed the final determination requirement, thereby finally aligning the IRS's disclosure regulations more closely with the statute.

Now, the IRS may share information about proposed revocations and denials of tax-exempt status, even before an administrative appeal has been made, or a final revocation or dismissal has been filed.<sup>6</sup> Such information may include federal tax returns and other information about federal tax returns, which may be provided to state governments in connection with any proposed sanctions against a nonprofit organization.<sup>7</sup>

## Disclosure Requirements and Restrictions

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To balance out these disclosures, the new regulation makes clear that tax returns and information about tax returns are confidential and that a state government receiving such information cannot share or disclose such information unless authorized by law.<sup>8</sup> Furthermore, the IRS may require that any state government receiving such information enter into a nondisclosure agreement requiring that it maintain sufficient safety protocols to ensure such federal taxpayer information will be kept secure.<sup>9</sup> Oftentimes, any sharing of taxpayer information is subject to a disclosure agreement negotiated between the IRS and the state government seeking the information.

Under the new rule, such disclosures may only be made as necessary for the state to administer its charitable solicitation laws, and generally require a written request for such information by an authorized state official.<sup>10</sup> Previously, any final determinations by the IRS were automatically disclosed to state governments.<sup>11</sup> However, the IRS may disclose evidence that an organization is not in compliance with state charitable organization requirements to certain authorized state officials of its own volition.<sup>12</sup>

## **Additional Provisions**

The new rule also allows the disclosure of federal taxpayer information in certain civil or judicial administrative proceedings under certain circumstances and upon notice to the IRS. In addition, it expands the list of people in a state government eligible who may receive federal taxpayer information. It also makes clear certain confidentiality and redisclosure requirements of those state officials who have received federal taxpayer information.

## **Conclusion**

This regulation was a long-time coming, with the rulemaking starting in 2011. It appears the rule became more of a priority following the Supreme Court's recent decision in *Americans for Prosperity Foundation v. Bonta*, which dealt with the State of California's misuse of nonprofit taxpayer data. *Bonta* was a 2021 United States Supreme Court case that struck the State of California's requirement that nonprofits disclose personally-identifying information listed on their federal tax returns to the State upfront.<sup>[13]</sup>

In sum, the new rule allows the IRS to disclose taxpayer information related to a possible revocation or denial of tax-exempt status to certain state officials, even though there has not been a final revocation of the organization's tax-exempt status. However, such disclosure may only be provided to the extent necessary for the state to carry on its charitable solicitation laws, and generally must be preceded by a written request from a state official unless the subject matter of the disclosure is evidence of noncompliance with state charitable organization requirements.

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## **FOOTNOTES**

<sup>1</sup> Disclosure of Information to State Officials Regarding Tax-Exempt Organizations, 87 Fed. Reg. 50240 (Aug. 16, 2022) (to be codified at 26 C.F.R. pt. 301).

<sup>2</sup> Disclosure of Information to State Officials Regarding Tax-Exempt Organizations, 76 Fed. Reg. 13,932 (Mar. 15, 2011).

<sup>3</sup> 26 C.F.R. § 301.610(c)-1 (2021).

<sup>4</sup> *Id.*

<sup>5</sup> 26 U.S.C. § 6104(c)(2)–(3).

<sup>6</sup> Disclosure of Information to State Officials Regarding Tax-Exempt Organizations, 87 Fed. Reg. 50240, 50244–45 (Aug. 16, 2022) (to be codified at 26 C.F.R. pt. 301).

<sup>7</sup> *Id.* at 50245.

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> *Id.* at 50244–45.

<sup>11</sup> 26 C.F.R. § 301.6104(c)-1(a) (2021).

<sup>12</sup> Disclosure of Information to State Officials Regarding Tax-Exempt Organizations, 87 Fed. Reg. 50240, 50244–45 (Aug. 16, 2022) (to be codified at 26 C.F.R. pt. 301).

<sup>13</sup> *Americans for Prosperity Foundation v. Bonta*, 141 S. Ct. 2373, 210 L. Ed. 2d 716 (2021).

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