

REQUEST FOR BOARD PERMISSION TO PROCEED TO FORMAL PROCESS

Request for Permission to Proceed with Formal Regulatory Process to Amend California Code of Regulations, title 18, sections 23701, 23772, 23775, 23776, 23777, and 23778

INTRODUCTION AND BACKGROUND

California Code of Regulations, title 18 ("CCR"), Sections 23701 to 23778 set forth regulations implementing California Revenue and Taxation Code ("R&TC") sections 23701 to 23778, relating to exemptions from franchise and income tax. The regulations were last amended in 2009 or earlier.

Since 2009, R&TC sections 23701, 23772 and 23778 have been amended. (See Senate Bill (SB) 401 (Stats. 2010, ch. 14); Assembly Bill (AB) 36 (Stats. 2011, ch. 17); SB 1341 (Stats. 2012, ch. 710); AB 1677 (Stats. 2012, ch. 858); AB 1173 (Stats. 2013, ch. 536); AB 154 (Stats. 2015, ch. 359); AB 94 (Stats. 2017, ch. 104); and SB 934 (Stats. 2020, ch. 59).))

As a result, Franchise Tax Board ("FTB") staff is proposing amendments to the regulations to implement the amendments to the statutes. Although R&TC sections 23775, 23776, and 23777 have not been amended since 2009, FTB staff is also proposing amendments to the regulations at CCR Sections 23775, 23776, and 23777 to implement amendments to the related statutes.

INTERESTED PARTIES MEETINGS

FTB staff held an Interested Parties Meeting ("IPM") on June 18, 2024. At the IPM, FTB staff explained the purpose of the proposed amendments and received public comments. Thereafter, on July 3, 2025, FTB staff issued a Thirty-Day Notice and revised regulatory text that included further amendments to revise the structure, syntax, cross-references, formatting, grammar, and punctuation in the regulations, and make the regulations more easily readable.

After the IPM and Thirty-Day Notice, FTB staff made additional non-substantive changes to the regulations such as adding commas to correct grammar, inserting words to make certain phrases consistent throughout the regulations, modifying statutory references in the Notes sections, and revising several words or phrases to clarify the language of the regulations.

REQUEST FOR PERMISSION

FTB staff believes that the proposed amendments provide necessary updates to reflect statutory changes and necessary clarifying changes to the regulations. FTB staff now requests the Board's permission to commence the formal regulatory process under the Administrative Procedure Act.

FRANCHISE TAX BOARD

CALIFORNIA CODE OF REGULATIONS, TITLE 18, DIVISION 3, CHAPTER 3.5, SUBCHAPTER 4 – EXEMPT ORGANIZATIONS, ARTICLE 1 – EXEMPTIONS FROM FRANCHISE OR CORPORATE TAX, AMEND SECTION 23701.

Text of Proposed Regulation

Section 23701 is amended to read:

§ 23701. Exemption from Taxation.

(a) In General.

– (1) ~~In General~~ Revenue and Taxation Code section 23701 provides an exemption from corporate franchise tax and ~~or corporate income tax~~ for organizations that are organized and operated for nonprofit purposes within the provisions of a specific section of Article 1, Chapter 4, or are described in ~~subject to~~ Revenue and Taxation Code sections 23701h or 23701x (relating to certain title-holding companies), if both of the following occur:

(A) An application for exemption is submitted in the form prescribed by the Franchise Tax Board.;

~~(B) A filing fee of twenty five dollars (\$ 25) is paid with each application for exemption filed with the Franchise Tax Board after June 30, 1983; and~~

~~(C)~~ (B) The Franchise Tax Board issues a determination exempting the organization from tax.

(2) The exemption ~~provided~~ does not extend to the unrelated business taxable income of such organization. ~~(See Revenue and Taxation Code section 23731.)~~ Also, the exemption is not applicable to an organization determined to be a feeder organization under Revenue and Taxation Code section 23702. An organization which has been determined to be exempt by the Franchise Tax Board can rely upon such determination so long as there are no substantial changes in the law or the organization's charter, purposes or method of operation. However, to retain exempt status the organization must elect an annual accounting period, ~~must~~ submit an exempt organization annual information return or annual statement, and pay ~~applicable~~appropriate filing fees.

(3) Notwithstanding anything to the contrary in this regulation, ~~for requests filed on or after January 1, 2008,~~ an organization that is exempt from federal income tax under Internal Revenue Code section 501(c)(3), (c)(4), (c)(5), (c)(6), (c)(7), or (c)(19) shall, upon submission of a copy of its federal determination letter to the Franchise Tax Board, be exempt from corporate franchise tax and ~~or corporate income tax~~ under Part 11 of

Division 2 of the Revenue and Taxation Code, except to the extent noted in the preceding paragraph, ~~under the authority of Revenue and Taxation Code section 23701d, subdivision (e).~~ The additional filing requirements specified in subsection (b) shall not apply to any organization described in this paragraph.

(b) Proof of Exemption. An organization must be organized (chartered, incorporated) and operated (conducting activities) primarily (in some cases exclusively) for one or more of the purposes specified in the particular section describing the exempt organization. If the organization fails to meet the organizational or operational test for the particular section describing the exempt organization, it is not entitled to exemption.

(1) Except as provided in subsection (a)(3), an organization claiming exemption under Revenue and Taxation Code section 23701 and described in Revenue and Taxation Code sections 23701a through 23701z shall file with the Franchise Tax Board an exemption application (~~Form 3500~~) ~~filled out~~ completed in accordance with the instructions on the form or issued therewith. The exemption application and the attachments thereto shall show the character of the organization, the purpose for which it was organized, its actual and proposed activities, the sources of its income and the receipts and disposition thereof, whether or not any of its income or receipts is credited to surplus or may inure to the benefit of any private shareholder or individual, and in general all facts relating to its operations which may affect its right to exemption. To each application there shall be attached a copy of the articles of incorporation, declaration of trust or other organizational document, the bylaws or other code of regulations, and financial statements showing assets, liabilities, receipts and disbursements (actual or as proposed) of the organization. The organizational document must meet the organizational test set out below and the activities or proposed activities must meet the operational test.

(A) Inurement of Income to ~~Member~~ Private Shareholder or Individual. Sufficient information must be furnished about benefits and compensation to be received by a private shareholder or individual ~~members, officers, directors and employees to insure that it can be said demonstrate that~~ they will not receive personal or private inurement. An organization is not operated for one or more exempt purposes contained in Revenue and Taxation Code sections 23701a through 23701z (with some exceptions discussed below) if net earnings inure directly or indirectly, in whole or in part, to the personal or private benefit of a private shareholder or individual ~~member, officer, director, employee or individual~~.

Inurement means that an individual receives some special benefit which is unreasonable under the circumstances because of the individual's ~~his~~ membership or relationship to the organization. Where organizations, exempt under Revenue and Taxation Code sections 23701d or 23701n are involved, the activity that leads to inurement may also be a prohibited transaction under Revenue and Taxation Code section 23736.1. If the organization is a private foundation, the violation of the prohibitions against ~~upon~~ self-dealing set forth in the Internal Revenue Code would normally constitute inurement if not corrected.

1. Under Revenue and Taxation Code sections 23701a, 23701b, 23701i, 23701j, 23701n and 23701s the payment of sick, accident, death, unemployment or retirement benefits out of employer, employee or member contributions does not result in personal or private inurement. In most cases, a limited amount of income, which may be taxable as unrelated business taxable income (see Revenue and Taxation Code section 23731), may be used for the payment of permitted benefits. Local associations of employees may receive contributions from employers that benefit employees without loss of exempt status. Payments of profits to participants of exempt diversified management corporations are also permissible benefits.

2. Examples of inurement include ~~Inurement has been held to have occurred in many situations, including~~ the following:

(I) Unreasonable compensation for services. The facts and circumstances of each case must be examined to determine if the compensation is unreasonable.

(II) Unreasonable rental charges.

(III) Unsecured loans of doubtful safety.

(IV) Deferred or retained interest in the assets of an organization claiming exemption under Revenue and Taxation Code sections 23701c, 23701d, 23701f, or 23701r.

(V) Operation of an organization to serve private interests.

(VI) Self-dealing with the organization; such as, making sales to or purchases from the organization which are not reasonable on their face.

(VII) Lack of a reasonable return on the capital of an organization exempt under Revenue and Taxation Code section 23701d.

(VIII) Use of the organization's property without adequate payment.

(IX) Reduction of dues, increase in assets, or provision of more services to members for the same dues which occurs as a result of a social and recreational organization's receiving income from the general public may be inurement to members. Use of limited income received from the general public for the above purposes may be permissible if it is taxable as unrelated business taxable income. (See Revenue and Taxation Code section 23731.)

(X) Reimbursement of founder for expenses incurred in connection with organization before it was exempt.

(XI) Payment of part of the general operating expenses of a membership organization out of income received from the general public normally results in inurement.

(B) Change of exempt classification.

1. An organization requesting a change of exempt status more than one year after exemption has been granted must submit a new exemption application, unless clause 2. is applicable. However, supporting information that is still current need not be resubmitted.

2. If an initial federal exemption application is timely filed and the exempt classification when received is different than that issued by the Franchise Tax Board, a change of classification will be considered without a formal application if the request for reclassification is submitted within ninety days after issuance of the federal determination exemption-letter. The request shall be accompanied by a copy of the federal determination letter and any supporting information not previously furnished to the Franchise Tax Board.

(2) In addition to the information specifically required under this regulation, the Franchise Tax Board may require additional information as deemed necessary to determine whether an organization is entitled to exemption under Revenue and Taxation Code section 23701, including evidence that the organization has established exempt status with the Internal Revenue Service.

~~(3) An organization applying for exemption from tax or for a change (reclassification) of exempt status must pay an application fee of \$ 25 with the exemption application. However, exceptions to the payment of the fee may be made for subordinates (processed on a group basis) and for unincorporated associations or trusts operating in California which were exempt from federal taxation prior to January 1, 1970. A copy of the Internal Revenue Service exempt determination letter should be furnished with the application.~~

~~(4)~~(3) Retroactivity of Exemption. Exempt status may be granted for years prior to approval of the exemption application but only to the extent the organization establishes it satisfied the exemption requirements during each of such prior years. In no event shall a claim for refund be allowed unless timely filed under Revenue and Taxation Code section 19306. In the case of exemptions granted under subsection (a)(3), the effective date of an organization's tax-exempt status for California franchise or income tax purposes shall be no later than the effective date of the organization's tax-exempt status, ~~under Section 501(c)(3) of the Internal Revenue Code,~~ for federal income tax purposes.

(c) Organizational Test.

(1) In General.

(A) An organization is organized primarily (in some cases exclusively) for one or more exempt purposes only if its articles of organization ("articles") as defined in paragraph (2) of this subsection:

1. Expressly set out an exempt purpose consistent with the purposes stated in the section which describes the exempt organization; and
2. Limit any other purposes or powers of the organization, except to an insubstantial degree, to those in furtherance of the purpose.
3. In the case of an unincorporated association (that is not a trust), expressly state that the organization is organized for nonprofit purposes and that individuals will not profit therefrom. However, associations described in Revenue and Taxation Code sections 23701h or 23701x (relating to certain title-holding companies) are not subject to this requirement.
4. In the case of a domestic corporation, incorporate the organization under Division 2, Parts 1, 2, 3, 4 or 6, of the California Corporations Code. However, incorporation under other provisions of the Corporations Code is permitted to the extent provided in Revenue and Taxation Code sections 23701h and 23701x (relating to certain title-holding companies).

(B) In meeting the organizational test, the organization's specific purpose may be as broad as, or more specific than, the purposes stated in the section which describes the exempt organization. The purpose should normally be accomplished by the primary activity of the organization.

(C) An organization is not organized primarily for one or more exempt purposes if its articles expressly empower it to carry on, other than as an insubstantial part of its activities, activities which are not in furtherance of one or more exempt purposes, even though such organization is, by the terms of such articles, created for a purpose that is no broader than the purposes specified in a section describing an exempt organization. Thus, an organization that is empowered by its articles "to engage in a manufacturing business," or "to engage in the operation of a social club" does not meet the organizational test of an organization desiring exemption under Revenue and Taxation Code section 23701d regardless of the fact that its articles may state that such organization is created "for charitable purposes" within the meaning of Revenue and Taxation Code section 23701d.

(2) Articles of Organization. For the purposes of this section, the term "articles of organization" or "articles" includes the trust instrument, the corporate charter, the articles of incorporation, the articles of association, or any other written instrument by which the organization is created.

(3) If before January 1, 1970, an organization has been determined to be an exempt organization by the Franchise Tax Board, the fact that such organization does not meet

the organizational test prescribed by this paragraph shall not be a basis for revoking such determination.

(d) Operational Test.

(1) Primary Activities. An organization will be regarded as "operated primarily" or "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in the section (Revenue and Taxation Code sections 23701a through 23701z) which describes the exempt organization. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

(2) Exempt status will be recognized in advance of operations ~~(or incorporation)~~, where proposed operations are planned to begin within one year and can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere restatement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy these requirements. The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures, or other means adopted or planned for carrying out the activities; the anticipated source of receipts, and the nature of contemplated expenditures. Where the Franchise Tax Board considers it warranted, a record of actual operations may be required before a determination letter will be issued.

(A) Where exempt operations do not actually begin within the year, an attachment should be added to the exempt organization annual information return report or annual statement (see Revenue and Taxation Code sections 23772 and 23774) to explain the delay and to outline plans for conducting activities during the next year. Failure to explain such inactivity will be cause for revocation of the organization's exempt status because since an inactive organization is not operated for exempt purposes and therefore is not entitled to exemption from tax.

(B) Organizations that commence exempt operations and later become inactive are subject to loss of their exempt status unless they include an attachment on their exempt organization annual information return report or annual statement to explain that their inactivity is temporary and to outline their plans for becoming active in the near future.

(e) The words "private shareholder or individual" in Revenue and Taxation Code sections 23701a through 23701z refer to persons having a personal or private interest in the activities of the organization.

(f) Every organization which has established its right to exemption shall submit an exempt organization annual information return report or annual statement as required by Revenue and Taxation Code sections 23772 and 23774. Also, the organization shall maintain adequate operational and financial records to show that its operations are conducted in an exempt manner. Changes in the character, operations or purposes of an exempt

organization shall be reported in writing to the Franchise Tax Board for evaluation as to whether the organization's exempt status is affected. In cases where the organization ~~organization's is suspended or its~~ exempt status is revoked, ~~either by suspension of corporate powers, for failure to elect an accounting period, or to file an annual return or statement, then~~ Revenue and Taxation Code sections 23776 and 23778 are applicable for reinstatement provisions.

(g) Every exempt organization shall make its records available or shall submit, in addition to its exempt organization annual information return or annual statement, such additional information as may be required by the Franchise Tax Board for the purpose of enabling it to inquire further into the organization's exempt status and to administer the provisions of Chapter 4 (Exempt Corporations) of Part 11 ~~(the Corporation Tax Law)~~.

(h) Withdrawal of Applications. ~~Applications for e~~Exemption applications may be withdrawn, upon the written request of one of the principal organizers or the his/her authorized representative ~~attorney of one of the principal organizers~~, at any time prior to the issuance of a determination letter. However, even though the application is withdrawn, the application, and supporting documents ~~and the application fee~~ will be retained by the Franchise Tax Board and will not be returned to the organization.

(i) Group Exemptions for Subordinates.

(1) A central organization (one which has one or more California subordinates under its general supervision or control) may apply for exemption for itself and its subordinates (chapter, local, post or unit). A central organization may be a subordinate itself; for example, a state organization which has subordinate units and may itself be affiliated with a national organization or a district of a state organization. This procedure will relieve each of the subordinates from applying separately for exemption.

(2) The organization applying for a group exemption letter must establish its own exempt status. It must also establish that the subordinates to be included in the group are:

(A) Affiliated with it;

(B) Subject to its general supervision and control; and

(C) Exempt under the same lettered section under Revenue and Taxation Code section 23701, including organizations exempt under subsection (a)(3), although not necessarily exempt under the same section as the national, state or parent (central) organization.

(3) Each subordinate to be included in the exempt determination must be formed under a standard constitution, articles of association, articles of incorporation or bylaws, and must authorize the central organization in writing to include it in the group exemption letter.

(4) A central organization seeking a group exemption letter for its subordinates must establish its own exemption separately by filing an exemption application form. In

addition to the information required to establish its own exemption or information not previously furnished, if it is already exempt, it must include in the application for group exemption:

(A) Information verifying the existence of the relationships set out in subsection 2(A) and (B) above.

(B) A description of the principal purposes and activities of subordinates.

(C) A sample copy of the uniform governing instrument for subordinates.

(D) An affirmation to the effect that, to the best of the central organization's knowledge, the subordinates are operating in accordance with the stated purposes.

(E) A statement that each subordinate to be included in the group exemption letter has furnished written authorization to the parent organization.

(F) A list of all California subordinates, mailing addresses and corporation numbers or Franchise Tax Board organization numbers if assigned. If an annual group report will be submitted, the organizations to be included in the report should be identified.

(5) Information required annually to maintain a group exemption letter. The national, central or state organization must submit to the Franchise Tax Board annually within 45 days after the close of the annual accounting period of its subordinates:

(A) Information regarding all changes in the purpose, character, or method of operation of subordinates included in the group exemption letter.

(B) A complete listing, with addresses, of all active California subordinates, showing the corporation or organization number assigned by the Franchise Tax Board (when one has been assigned). If a group report will be submitted, the listings should indicate all subordinates that are authorized to and will be included in the group report. The list should be marked to indicate which subordinates have changed their names or addresses during the year. Any new subordinate formed during the year shall be clearly identified.

(C) A separate listing should show all subordinates that have ceased to exist since the last report and those that have disaffiliated from the central organization.

(D) Each subordinate must be included in an exempt organization annual information return or annual statement (see Revenue and Taxation Code sections 23772 and 23774) submitted annually. Subordinates that meet the requirements may be included in a group return~~report~~, while any subordinate not authorized and not included in the group return must submit an individual annual information return or annual statement.

(E) Submission of the above information does not relieve the central organization or any of its subordinates of the duty to submit such additional information as the Franchise Tax Board may require to permit it to determine whether the conditions for continued exemption are met.

(6) Termination of a group exemption letter.

(A) Termination of a group exemption letter will result in non-recognition of the exempt status of all included subordinates. To reestablish an exempt status in such cases, each subordinate must file an exemption application or a new group exemption must be applied for and secured.

(B) If a central or state organization covered by a group exemption letter ceases to exist, the group exemption letter will be terminated.

(C) Failure of the central or state organization to submit an annual listing or exempt organization annual information return for itself (where required) and for its subordinates which are included in the group letter and designated to be included in a group report may result in termination of the group exemption letter.

(D) If a subordinate which is covered by the group exemption letter and which is required to report separately to the Franchise Tax Board does not submit an exempt organization annual report information return or annual statement (see Revenue and Taxation Code sections 23772 and 23774), its exempt status may be terminated on an individual basis. The group exemption letter will no longer be applicable to such subordinate, but will otherwise remain in effect. Where a subordinate's exemption is terminated on an individual basis, it must reapply for exemption on an individual basis.

NOTE: Authority cited: Section 19503, Revenue and Taxation Code. Reference: Section 23701, Revenue and Taxation Code.

CALIFORNIA CODE OF REGULATIONS, TITLE 18, DIVISION 3, CHAPTER 3.5, SUBCHAPTER 4 – EXEMPT ORGANIZATIONS, ARTICLE 5 – RETURNS, REVOCATION AND SUSPENSION OF EXEMPT ORGANIZATIONS, AMEND SECTIONS 23772, 23775, 23776, 23777, AND 23778.

Text of Proposed Regulations

Section 23772 is amended to read:

§ 23772. Information Returns and Statements.

Exempt Organizations.

(a) For income years ending December 31, 1971, and subsequent years, all exempt organizations or trusts and nonexempt trusts treated as a private foundation because of

Internal Revenue Code section 4947(a)(1) must file an exempt organization annual information return Form 199 (Exempt Organization Annual Information Return).

(1) A completed exempt organization annual information return Form 199 is required from any organization, except:

(A) A church, an interchurch organization of local units of a church, a convention or association of churches, or an integrated auxiliary of a church such as a men's or women's organization, religious school, mission society, or youth group;

(B) An exclusively religious activity of any religious order;

(C) For taxable years beginning before January 1, 2012, Aan organization (other than a private foundation) the gross receipts of which in each taxable year are normally not more than \$25,000 (as described in subsection (i)(1));

(D) For taxable years beginning on or after January 1, 2012, an organization (other than a private foundation) the gross receipts of which in each taxable year are normally not more than \$50,000 (as described in subsection (i)(2));

(DE) A mission society sponsored by or affiliated with one or more churches or church denominations, more than one-half of the activities of which society are conducted in, or directed at persons in, foreign countries;

(EF) Nonprofit exempt quasi-governmental organizations formed to carry out a function of the State or a public body, that are carrying out that function and are controlled by the State or a public body. Such an organization must have been formed to support a function of the State, county, city or other political body, it must be operating for this purpose, and the majority of the directors must be under the control of the State or appropriate political body. Upon dissolution, the assets must be turned over to the State, county, city, or other political body.

(G) A political organization exempt under Revenue and Taxation Code section 23701r.

NOTE: A stock bonus, pension or profit-sharing trust exempt under Revenue and Taxation Code section 17631 is not required to file an exempt organization annual information return or submit annually, in electronic form, in the manner as may be prescribed by the Franchise Tax Board, the information listed in Revenue and Taxation Code section 23772(b)(13)(A)(i) Form 199. However, a stock bonus, pension or profit-sharing trust exempt under Revenue and Taxation Code section 17631 with unrelated business taxable income of \$1,000 or more is required to file the filing of Form 109- a California exempt organization business income tax return (Form 109). (See Revenue and Taxation Code section 18506.)

(2)(A) The information required to be furnished by each organization required to file an exempt organization annual information return Form 199 is:

~~1. Its-g~~ Gross sales and receipts from all sources during the year, except dues and contributions set out in clauses 2. and 3. below. For this purpose, gross receipts includes tax exempt income. The cost of goods sold and the cost or other basis and sales expenses of assets will be shown and subtracted from the above to arrive at gross income.

2. Gross dues and assessments from members and affiliates for the year. Social or recreational clubs must furnish additional information on source of receipts.

~~3. The-t~~ Total of the contributions, gifts, grants and similar amounts received during the taxable year.

4. Gross receipts for filing requirements.

~~5. Its-e~~ Expenses incurred within the year attributable to gross income.

~~6. Its-d~~ Disbursements (including prior years' accumulations) made within the year for the purposes for which it is exempt.

7. Increase or decrease in net worth.

~~8. The-t~~ Total assets and liabilities at the beginning and end of the year.

9. Information on legislative and political activities.

10. If a private foundation, the names and addresses of foundation managers within the meaning of Internal Revenue Code section 4946(b)(1).

11. Information with respect to qualified disaster relief activities.

12. Each controlling organization within the meaning of Internal Revenue Code section 512(b)(13), which is subject to the requirements of subdivision (a), must include on its return all of the following information:

(I) Interest, royalties, annuities, and rents received from a controlled entity, within the meaning of section 512(b)(13) of the Internal Revenue Code.

(II) Loans made to a controlled entity.

(III) Any other transfers of funds between itself and a controlled entity.

~~10~~13. Other information that may be found necessary to ~~insure~~ensure that the organization is operating in an exempt manner.

~~11~~14. For additional information required to be furnished by private foundations, see subparagraphs (B) and (C) below.

(B) Alternative detailed reporting requirements.

1. Any organization, including a private foundation, that is required to complete Part II of an exempt organization annual information return Form 199 can comply fully with its reporting requirements by completing Part I page 1 of an exempt organization annual information return the Form 199 and paying \$ ~~10.00~~ filing fee, if required, and:

(I) Attaching a completed copy of the current annual registration renewal fee report to the Attorney General of California Registry of Charitable Trusts Report CT-2; or

(II) Attaching a completed copy of the federal return from organization exempt from income tax Federal Form 990 which includes Part I, II, and any required schedules. In the case of private foundations, attach a completed copy of the federal report of the private foundation, including all required schedules, filed with the Internal Revenue Service with assets of \$ 5,000 or more, at any time during its accounting period, must furnish a copy of the annual report of private foundation (Federal Form 990A-R or substitute report) filed with the Internal Revenue Services; or

(III) In case of a labor organization, a copy of federal labor organization annual report Labor Department Form LM-3 may be attached.

(C) Special rules for organizations which are required to complete Part II of an exempt organization annual information return Form 199 but which do not use alternative detailed reporting requirements permitted in subparagraph (B) above.

1. An itemized schedule must be attached to an exempt organization annual information return Form 199 if money, securities or other property of \$5,000 or more is received as a contribution, gift or grant directly or indirectly from one person during the year showing name, address, date received and total amount received from such person. In the case of a private foundation (as defined in Internal Revenue Code Section 509(a)), the names and addresses of all persons who became substantial contributors (as defined in Internal Revenue Code section 507(d)(2)) during the taxable year shall be furnished.

(I) An organization described in Revenue and Taxation Code section 23701d which meets the 33 1/3 percent-of-support test of the regulations under Internal Revenue Code section 170(b)(1)(A)(vi) (without regard to whether such organization otherwise qualifies as an organization described in Internal Revenue Code section 170(b)(1)(A) ~~I.R.C.~~) is required to provide the name and address of a person who contributed, bequeathed or devised \$5,000 or more during the year only if this amount is in excess of 2 percent of the total contributions, bequests and devises received by the organization during the year.

(II) An organization other than a private foundation is required to report only the names and addresses of contributors of whom it has actual knowledge. For instance, an organization need not require an employer who withholds contributions from the compensation of employees and pays over to the organization periodically the total amounts withheld, to specify the amounts paid over with respect to a particular employee. In such case, unless the organization has actual knowledge that a particular employee gave more than \$5,000 (and in excess of 2 percent if 1. of this ~~subdivision~~ subsection is applicable), the organization need report only the name and address of the employer, and the total amount paid over by the employer~~him~~.

(III) Separate and independent gifts made by one person in a particular year need to be aggregated to determine if the ~~his~~ contributions and bequests exceed \$5,000 (and in excess of 2 percent if 1. of this subsection is applicable), only if such gifts are of \$1,000 or more.

(IV) Organizations described in Revenue and Taxation Code sections 23701b or 23701l and organizations described in Revenue and Taxation Code section 23701g that receive contributions or bequests to be used exclusively for purposes described in Revenue and Taxation Code section 17214(d) must attach a schedule with respect to all gifts which aggregate more than \$1,000 from any one person, showing the name of the donor, the amount of the contribution or bequest, the specific purpose for which such amount was received, and the specific use to which such amount was put. In the case of an amount set aside for such purposes, the organization shall indicate the manner in which such amount is held (for instance, whether such amount is commingled with amounts held for other purposes). If the contribution or bequest was transferred to another organization, the schedule must include the name of the transferee organization, a description of the nature of such organization, and a description of the relationship between the transferee and transferor organizations. Such organizations must also attach a statement showing the total dollar amount of contributions and bequests which are \$1,000 or less received for such purposes.

2. Attach a schedule detailing the gross amount received from the sale of assets, including inventory items.

3. Attach a schedule itemizing other income, except contributions, gifts and grants.

4. Attach a schedule showing amount of:

(I) Death, sickness, hospitalization or disability benefits;

(II) Unemployment compensation benefits; and

(III) Other benefits (state nature) paid out.

5. Attach schedule for officers, directors, trustees or individuals having similar responsibilities, showing name, address, social security number, title, compensation and time devoted to position, and in the case of a private foundation, all persons who are foundation managers, within the meaning of Internal Revenue Code section 4946(b)(1). Organizations described in Revenue and Taxation Code section 23701d must also attach a schedule showing the names and addresses of the five employees (if any) who received the greatest amount of annual compensation in excess of \$30,000 and amounts received; the total number of other employees who received annual compensation in excess of \$30,000; the names and addresses of the five independent contractors (if any) who performed personal services of a professional nature for the organization (such as attorneys, accountants, and doctors, whether such services are performed by such persons in their individual capacity or as employees of a professional service corporation) and who received in excess of \$30,000, from the organization for the year for the performance of such services; and the total number of other such independent contractors who received in excess of \$30,000 for the year for the performance of such services.

6. Attach schedules to explain depreciation (or depletion), other expenses, and to explain items on balance sheet where requested in Part II of an exempt organization annual information return ~~Form 199~~.

(b) For taxable years beginning on or after January 1, 2010, any organization that does not file an exempt organization annual information return because such organization falls within the exceptions under (a)(1)(C) or (D) above must submit, annually, in electronic form, in the manner as may be prescribed by the Franchise Tax Board, the information listed in Revenue and Taxation Code section 23772(b)(13)(A)(i).

(b)(c) Accounting Period for Filing Information Return or Annual Statement, or Submitting Information Electronically. An exempt organization annual information return ~~on Form 199~~ or annual statement (see Revenue and Taxation Code sections 23772 and 23774) shall be filed, or the information listed in Revenue and Taxation Code section 23772(b)(13)(A)(i) shall be submitted electronically, in the manner as may be prescribed by the Franchise Tax Board, on the basis of the established annual accounting period of the organization. If the organization has no established accounting period, the exempt organization annual information return or annual statement shall be filed, or the information listed in Revenue and Taxation Code section 23772(b)(13)(A)(i) shall be submitted electronically, in the manner as may be prescribed by the Franchise Tax Board, on the basis of the calendar year.

(e)(d) Returns When Exempt Status Not Established. Where an organization has a reasonable claim for exemption and submits an exemption application request prior to the time a taxable return is due, if it does not appear that the exemption will be denied, an exempt organization annual information return ~~may shall~~ be submitted, or the information

listed in Revenue and Taxation Code section 23772(b)(13)(A)(i) shall be submitted electronically in the manner as may be prescribed by the Franchise Tax Board, within ten days of the due date even if the Franchise Tax Board has not yet issued an exemption determination letter. If the exemption should be denied at a later time, the above action should be reasonable grounds for filing a late taxable return. In other cases, a taxable return should be submitted on or before the due date with a payment for any tax that is due.

~~(d)~~(e) Group Returns.

(1) A group return may be filed by a central organization (for the purposes of this subsection, this includes a parent, state, district, or similar type organization) for its subordinate organizations (for the purposes of this subsection, this includes a branch, local or similar organization) none of which are private foundations, provided the subordinate organizations:

(A) are affiliated with the central organization at the close of the central organization's annual accounting period;

(B) are subject to the general supervision and control of the central organization; and

(C) do not have unrelated ~~trade or business~~ taxable income in excess of \$1,000.

1. The group return shall consist of the following:

(I) a completed exempt organization annual information return or annual statement for the central organization;

(II) a list of names, current addresses, employer identification numbers, and corporate or association numbers of the ~~qualified subordinates~~ organizations which are to be included in the group return; and

(III) any additional information which may be required by the Franchise Tax Board.

2. After the initial group return is filed, Item 1.(II) above may be replaced by a list to include only:

(I) subordinates organizations that were added;

(II) subordinates organizations deleted; or

(III) a statement of no change from the previous year's group return~~report~~.

3. ~~If the central organization has not been issued a group exemption letter, it must secure an~~ group exemption or group exemption determination from the Franchise Tax Board ~~to cover its subordinates~~ before a group return may

be filed. ~~The Franchise Tax Board may determine the requirements for a group exemption. Subordinate organizations must be covered by a group exemption, or have obtained exempt status on their own basis, before they can be included in a group return.~~

4. If the central organization has previously been issued a group exemption letter, all new subordinate organizations formed during the year must be identified on the list of subordinates~~roster~~.

5. A group statement return~~return~~ may be submitted by central church associations for subordinate churches or church associated groups that are permitted to file the exempt organization annual information statement. Schedules required in 1.(II) above must be attached to the information statement submitted by the parent church. Any subordinate organizations having more than \$1,000 of unrelated ~~trade or business~~ taxable income may not be included in the group return report.

~~(e)~~(f) Time and Place for Filing. The exempt organization annual information return ~~on Form 199~~ shall be filed, or the information listed in Revenue and Taxation Code section 23772(b)(13)(A)(i) shall be submitted electronically in the manner as may be prescribed by the Franchise Tax Board, on or before the 15th day of the fifth month (4 1/2 months) following the close of the annual accounting period for which the return is required to be filed. The annual partnership return of income~~return on Form 565~~ required to be filed by a religious or apostolic association or corporation shall be attached to an exempt organization annual information return Form 199. Each such return shall be filed in accordance with the instructions applicable thereto.

~~(f) Payment of Filing Fee. All organizations required to file Form 199 (including group returns), except those described below, must pay a \$ 10.00 filing fee with Form 199. If payment is not made on or before the due date (or extended due date), the fee is \$ 25.00 unless there is reasonable cause for late payment. Organizations required to file Form 199 but not required to pay the filing fee should check the appropriate box on Form 199. Organizations exempt under Revenue and Taxation Code section 23701d which are not required to pay a filing fee are described as follows:~~

~~(1) Exclusively religious organizations.~~

~~(2) An exclusively educational organization exempt under Revenue and Taxation Code section 23701d, if the organization normally maintains a regular faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on.~~

~~(3) An exclusively charitable organization, or an organization for the prevention of cruelty to children or animals, exempt as provided under Revenue and Taxation Code section 23701d, if the organization is supported, in whole or in part, by funds contributed by the United States or any state or political subdivision thereof, or is primarily supported by contributions of the general public.~~

~~(4) An organization exempt under Revenue and Taxation Code section 23701d, if the organization is operated, supervised, or controlled by or in connection with a religious organization.~~

(g) Penalties for Failure to File a Return. If an organization or trust required to file an exempt organization annual information return ~~a Form 199~~ fails to file the return on or before the due date, it ~~shall will have to~~ pay \$5.00 for each month, or part thereof, after the due date, not to exceed \$40.00, until the form is filed, unless it can be shown that the failure was due to reasonable cause. In the case of a private foundation, the Franchise Tax Board may make written demand that such delinquent return or foundation report be filed within a reasonable time after notice of mailing such demand. The person failing to file (unless it can be shown to be due to reasonable cause) ~~shall will have to~~ pay \$5.00 for each month, or part thereof, (not to exceed \$25.00) after the period expires.

(h) Records, Statements, and Other Returns of Tax-Exempt Organizations. Every organization which is exempt from tax, whether or not it is required to file an exempt organization annual information return or annual statement, shall submit such additional information as may be required by the Franchise Tax Board for the purpose of inquiring into its exempt status and administering the provisions of Chapter 4 of the Corporation Tax Law. (See Revenue and Taxation Code section 23701 and the regulations thereunder with respect to the authority of the Franchise Tax Board to require such additional information, and with respect to the books of account or records to be kept by such organizations.)

(i) Definitions. For the purposes of this regulation, the following definitions are applicable:

(1) For taxable years beginning before January 1, 2012, g~~G~~ross receipts of an organization are normally not more than \$25,000 if—

(A) In the case of an organization which has been in existence for 1 year or less, the organization has received, or donors have pledged to give, gross receipts of \$ 37,500 or less during the first taxable year of the organization,

(B) In the case of an organization which has been in existence for more than one but less than 3 years, the average of the gross receipts received by the organization in its first 2 taxable years is \$30,000 or less, and

(C) In the case of an organization which has been in existence for 3 years or more, the average of the gross receipts received by the organization in the immediately preceding 3 taxable years, including the year for which the return would be required to be filed, is \$25,000 or less.

(2) For taxable years beginning on or after January 1, 2012, gross receipts of an organization are normally not more than \$50,000 if—

(A) In the case of an organization which has been in existence for 1 year or less, the organization has received, or donors have pledged to give, gross receipts of \$75,500 or less during the first taxable year of the organization.

(B) In the case of an organization which has been in existence for more than one but less than 3 years, the average of the gross receipts received by the organization in its first 2 taxable years is \$60,000 or less, and

(C) In the case of an organization which has been in existence for 3 years or more, the average of the gross receipts received by the organization in the immediately preceding 3 taxable years, including the year for which the return would be required to be filed, is \$50,000 or less.

~~(2)~~(3) "Gross Receipts" means the gross amount received by the organization during its annual accounting period from all sources, without reduction for any costs or expenses. Gross receipts include, for example, cost of goods or assets sold, cost of operations, and expenses of earning, raising, or collecting such amounts. Thus "gross receipts" includes, but is not limited to:

(A) the gross amount received as contributions, gifts, grants, and similar amounts without reduction for the expenses of raising and collecting such amounts,

(B) the gross amount received as dues or assessments from members or affiliated organizations without reduction for expenses attributable to the receipt of such amounts,

(C) gross sales or receipts from business activities (including business activities unrelated to the purpose for which the organization qualified for exemption), the net income or ~~less~~ loss from which may be required to be reported on a California exempt organization business income tax return ~~Form 109~~,

(D) the gross amount received from the sale of assets without reduction for cost or other basis and expenses of sale, and

(E) the gross amount received as investment income, such as interest, dividends, rents, and royalties.

NOTE: Gross receipts of local lodges do not include funds collected for insurance premiums of members by local lodges and thereafter remitted to the home or parent office in connection with benefit contracts issued by the home office.

(j) Unrelated Business Income Tax Returns. In addition to the foregoing requirements of this section, most organizations otherwise exempt from tax under Revenue and Taxation Code section 23701 are subject to tax on unrelated business taxable income and are also required to file ~~returns on a California exempt organization business income tax return~~ Form 109 if they receive such income. (See Revenue and Taxation Code section 23731 and the regulations thereunder.)

(k) This regulation shall be applied to income years beginning on or after January 1, 1986, except that paragraph (1) of subsection (i) and subparagraph (C) of paragraph (1) of subsection (a) shall be applied to income years beginning on or after January 1, 1982; ~~subsection (f) and clause (i) of subparagraph (B) of paragraph (3) of subsection (a) shall be applied with respect to fees imposed on or after July 1, 1983;~~ and subparagraph (A) of paragraph (1) of subsection (a) shall be applicable to filings made on or after January 1, 1984.

NOTE: Authority cited: Section 19503, Revenue and Taxation Code. Reference: Section 23772, Revenue and Taxation Code.

Section 23775 is amended to read:

§ 23775. Suspension of Exempt Corporate Status.

(a) The corporate powers, rights and privileges of an exempt domestic corporation may be suspended and the exercise of corporate powers, rights and privileges of a foreign exempt corporation in this state may be forfeited if the organization fails to-

(1) File an exempt organization annual information return ~~(Form 199)~~ required under Revenue and Taxation Code sSection 23772 on or before the close of the last day of the 12th month following the close of the income year.

(2) Pay any amount due under Revenue and Taxation Code sSection 23703 or 23772 on or before the close of the last day of the 12th month following the close of the income year.

~~(3) File a return or notify the Franchise Tax Board of its annual accounting period within nine months after its date of incorporation or qualification.~~

(b) Corporations will normally receive at least one notice of their delinquency before suspension or forfeiture is effected. However, there is no legal requirement that such notice be sent to or received by the organization.

(c) A suspended or forfeited corporation cannot exercise any of the corporate powers, other than to set forth a new name by amending its articles of incorporation. Thus, a suspended or forfeited corporation may not prosecute or defend an action at law or in equity; but may obtain a continuance to permit revivor to be accomplished. The exemption of a suspended corporation that continues to operate (other than for winding up) may be revoked and, pursuant to Revenue and Taxation Code section 23303, the organization will be subject to at least the minimum franchise tax ~~under Section 23303.~~

(d) Evidence of suspension or forfeiture is in the form of a list issued by the Franchise Tax Board and transmitted to the Secretary of State. The suspension or forfeiture is effective upon transmittal of said list to the Secretary of State. Also, a notice of suspension or forfeiture is normally mailed to the last known address of the corporation by the Franchise Tax Board.

NOTE: Authority cited: Section ~~1950326422~~, Revenue and Taxation Code. Reference: Sections 23775, 23301.5 and 23302, Revenue and Taxation Code.

Section 23776 is amended to read:

§ 23776. Relief from Suspension Imposed Under Section 23775.

(a) Any corporation that was suspended or forfeited under the provisions of Revenue and Taxation Code ~~s~~Section 23775 may be relieved therefrom upon the filing of all of the following:

(1) ~~A complete new application for exemption application and applicable schedule(s) and payment of the ten dollar (\$10) application fee; and.~~

(2) ~~An application for revivor; and.~~

(3) Any annual information returns, notifications, or amounts due under Revenue and Taxation Code ~~s~~Sections 23772 or 23775 which ~~was~~ were not previously submitted or paid and which resulted in the suspension or forfeiture; ~~and.~~

(4) Any annual information return and amounts specified under Revenue and Taxation Code ~~s~~Section 23772 for each year or part thereof during the period of suspension or forfeiture in which the organization conducted any activities or received income, grants, gifts, or other assets. ~~Where the exemption of the corporation was also revoked the minimum franchise tax will be due under Section 23303, unless there was reasonable cause for the deficiency which resulted in the revocation.~~

~~(b) Any corporation that was suspended or forfeited under Section 23775 may be revived as indicated in (a) above:~~

~~(1) For corporations formed in the last year and suspended for failure to elect an accounting period only a certificate of revivor, the front page of the exemption application (FTB 3500) with the \$10.00 revivor fee is normally required. However, if a return or statement is overdue or will be due within two weeks, it must be enclosed, with appropriate filing fee and penalties.~~

~~(b2) For other corporations formed or granted exemption in 1968 or subsequent years, abbreviated information may be furnished to support the exemption application. (Include application for revivor.)~~

~~(1A) A c~~Complete page one of the exemption application and applicable schedule(s) ~~the appropriate question number 11 through 21.~~

~~(2B)~~ Do not include a copy of the articles of incorporation, but include any amendments made after the exemption letter was issued. A ~~xerox~~ copy is satisfactory so long as the Secretary of State's endorsed stamp is shown.

~~(3C) Include a A copy of current bylawsby laws.~~

~~(4D) Furnish a A statement of all significant activities conducted by the organization during the last three years.~~

~~(5E) Submit a Any annual information returns, reports, or statements for accounting periods ending in 1970 and subsequent years that have not previously been filed, in addition to any applicable penalties and fees. Also include filing fees or fees resulting from Registrar of Charitable Trusts actions that have not previously been paid.~~

~~(i) Any time a Form 199 is submitted late or was submitted on time without filing fees the filing fee is increased from \$10.00 to \$25.00. Therefore, any old returns or reports submitted should normally include a \$25.00 fee. If a return or report was submitted without a fee or a minimum tax assessment was made under Section 23703, the organization should have notice of the amount due.~~

~~(ii) Where a Form 199 is due for December, 1971, or subsequent, a penalty of \$5.00 a month not exceeding \$40.00 is due unless there is reasonable cause for the late filing of the report.~~

~~(3) Corporations formed or granted an exemption prior to 1968 must furnish any additional information required by page two of the exemption application in addition to a copy of the articles of incorporation. An exception can be made to submission of articles of incorporation if they have been furnished to the Franchise Tax Board subsequent to the granting of exemption.~~

NOTE: Authority cited: Section ~~1950326422~~, Revenue and Taxation Code. Reference: Section 23776, Revenue and Taxation Code.

Section 23777 is amended to read:

§ 23777. Revocation of Exempt Status.

(a) The exemption granted to any organization or trust under Revenue and Taxation Code ~~s~~Section 23701 may be revoked if the organization fails to:

(1) File an exempt organization annual information return ~~(Form 199)~~ required under Revenue and Taxation Code ~~s~~Section 23772 on or before the close of the last day of the 12th month following the close of the income year.

(2) Pay any amount due under Revenue and Taxation Code ~~s~~Section 23703 or 23772 on or before the close of the last day of the 12th month following the close of the income year.

(3) Confine its activities to those permitted by the section under which the exemption was granted.

~~(b) Corporations that fail to elect an accounting period, to file returns or statements on time or pay amounts due on time will normally be suspended under the provisions of Section 23775.~~

(be) Unincorporated associations or trusts that are believed to be active that fail to file returns or statements on time or pay amounts due on time will have their exemptions revoked under Revenue and Taxation Code section 23777.

(cd) Where unincorporated associations or trusts become inactive or terminated prior to the due date of an exempt organization annual information return ~~report or a filing fee~~, the organization will normally be made inactive on the Franchise Tax Board files rather than being revoked and made a taxable organization. The organization or its parent (if there is one) must submit a notice of inactivity of the organization prior to the date the revocation is authorized.

(de) Any organization that is revoked for the conduct of improper activities will be taxable as a taxable corporation or trust so long as exempt status is not reestablished.

NOTE: Authority cited: Section ~~1950326422~~, Revenue and Taxation Code. Reference: Section 23777, Revenue and Taxation Code.

Section 23778 is amended to read:

§ 23778. Relief from Revocation of Exempt Status.

(a) An organization whose exemption was revoked under Revenue and Taxation Code sSection 23703 or 23777 may reestablish itself as an exempt organization upon the filing of all of the following:

(1) A new ~~application for exemption application and payment of the twenty five dollar (\$25) filing fee required under Section 23701; and.~~

(2) Any annual information returns, statements, notifications, or amounts due under Revenue and Taxation Code sSection 23772, 23774 or 23775 ~~which that~~ were not previously submitted or paid which resulted in the revocation; ~~and.~~

(3) When revocation occurred because of the conduct of improper activities of the organization, satisfactory proof must be furnished that the improper activities have ceased and that the organization will operate in an exempt manner in the future and the payment of any tax due for the period it operated as a taxable organization.

(b) Where the organization or trust was granted an exemption in 1968 or subsequent years, abbreviated information may be furnished to support the exemption application if the revocation occurred for failure to submit a return or statement or to pay an annual filing fee.

(1) Complete ~~page one of the application for exemption. and the appropriate question number 11 through 21.~~

(2) Do not furnish a copy of the constitution or bylaws or trust document unless they have been revised after exemption was granted.

(3) Furnish a statement of all significant activities conducted during the last three years.

(4) Submit any exempt organization annual information returns or annual statements that have not previously been filed, in addition to any applicable penalties and fees, or statements, or filing fees, or assessments made under Section 23703 that have not been submitted that resulted in the revocation. ~~Any time a \$10.00 filing fee is due and it will be paid late, it is automatically increased to \$25.00.~~

(5) ~~Where a Form 199 must be submitted for December, 1971, or later, a penalty of \$5.00 a month not exceeding \$40.00 is due unless there is a reasonable cause for the late filing of the report.~~

~~(c) Organizations or trusts which were granted an exemption prior to 1968 should furnish all the information required on page two of the exemption application, including the information requested in subdivision (b) above.~~

(cd) Organizations whose exemption was revoked for improper activities must include a copy of the revocation letter, a detailed statement as to the change of activities, and a description of action that has been taken to prevent the reoccurrence of the improper activities in addition to all the information required on the exemption application. Copies of any income tax returns submitted during the period the organization was taxable (not to exceed the three latest years) must be submitted.

NOTE: Authority cited: Section 1950326422, Revenue and Taxation Code. Reference: Section 23778, Revenue and Taxation Code.