

## NAAFTF Notice to Applicants Regarding the “Tipping Point”

1. Under the tax law, a section 501(c)(3) organization is presumed to be a private foundation unless it requests, and qualifies for, a ruling or determination as a public charity. Organizations that qualify for public charity status include, among others, schools and “publicly-supported organizations” which are organizations that receive a specified portion of their total support from public sources. See <http://www.irs.gov/Charities-&-Non-Profits/EO-Operational-Requirements:-Private-Foundations-and-Public-Charities>.
2. When an organization has qualified as a “public charity,” it can lose that status and revert to being a private foundation if it receives too large an award from a single source. The size of a grant or other contribution which could change an organization from a public charity to a private foundation is referred to as the “tipping point.” Organizations which have qualified as public charities generally seek to avoid being “tipped” back into the private foundation category, because it subjects them to more burdensome regulations.<sup>1</sup>
3. The “public support test” determines whether a charity is a private foundation or public charity.<sup>2</sup> The test examines the current year and 4 prior years, for total of five years. Where more than 2/3 of an organization’s support comes from a sole source, then the organization is usually deemed a private foundation, rather than a public charity. If at least 1/3 of an organization’s support comes from the general public or government grants, then it establishes “public support.” <http://www.irs.gov/pub/irs-pdf/p557.pdf> at 32
4. An organization will ordinarily lose its public charity status if it cannot pass the public support test for two consecutive years. If the organization cannot meet the public support test for two consecutive years, it will be reclassified as a private foundation as of the start of the second consecutive year (unless it qualifies as another kind of public charity).<sup>3</sup> <http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Exempt-Organizations-Annual-Reporting-Requirements-Form-990,-Schedules-A-and-B:-Maintaining-Public-Charity-Status>.
5. NAAFTF and Class Counsel **cannot** provide you any advice as to whether your organization would be at risk of tipping from a public charity to a private foundation as a

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<sup>1</sup> Because they are less open to public scrutiny, private foundations are subject to various operating restrictions and to excise taxes for failure to comply with those restrictions. <http://www.irs.gov/Charities-&-Non-Profits/EO-Operational-Requirements:-Private-Foundations-and-Public-Charities>.

<sup>2</sup> There are some categories of organizations that are always considered public charities, such as schools, churches and hospitals.

<sup>3</sup> In the case of “unusual” one-time grants the grantee may request a ruling from the IRS that the grant should be set aside for purposes of determining the organization’s public support calculation. There may be other exceptions as well. For example, funds awarded by the government do not count against an organization in applying the public support test.

result of receiving an award from the *cy pres* funds. It is not clear, for example, if funds remaining from a class settlement paid by the U.S. government are funds that are covered as a source that may “tip” an organization. We wanted to alert applicants to this issue and urge that they take it into account in determining the size of the award they apply for. NAAFTF is not responsible for any consequences to an organization of having their application funded, including tipping any public charities to private foundations.

6. To make a rough estimate of the “tipping point” for your organization
  - a. Look at your Form 990 Schedule A.
  - b. Look at total public support in Section A, line 6(f) or Section B, line 11(f) (depending on which section your organization completes).
  - c. Multiply that amount by  $2/3$ .
  - d. If the proposed grant is larger than the amount calculated, there is a tipping risk.