

# Why Is Nonprofit Tax Exemption Essential for North Carolina?

## 1. It protects taxpayers.

- Nonprofits provide essential services that government would have to provide otherwise. Tax exemption costs much less than the cost of government having to provide the services itself.
- Nonprofits provide public benefits in exchange for tax exemption.
- Organizations may choose not to locate in counties or states that do not grant tax exemption. This is a potential loss for the people and economy in those locations.

## 2. It fuels North Carolina's economy.

- Nonprofits provide more than 400,000 jobs in North Carolina. These 400,000 employees pay income, sales, and property taxes.
- Nonprofits are essential to create the quality of life that attracts and keeps jobs in North Carolina. They are a vital part of thriving communities and a thriving state.
- Three-fifths of North Carolina's nonprofits lack the resources to fully meet demands for their services. If nonprofits had to pay taxes, North Carolina communities would lose more essential public services and jobs.

## 3. It leverages new resources for community services.

- Nonprofits are uniquely positioned to leverage private contributions and donated volunteer time for the public benefit. Tax exemption is a small price to pay for the value that nonprofits add to the life of every North Carolinian.

## 4. It avoids raising taxes.

- Taxing nonprofits would reduce what they can spend on essential program services in communities across the state.
- When government contracts with nonprofits to provide essential public services, government funds would be used to pay government taxes if nonprofits were not tax-exempt.
- Nonprofits operate on a thin financial margin. Boards and volunteers need reliability and consistency in their tax status in order to make the best use of their resources and plan well for the future. It is important that eligibility standards for charitable tax exemptions are applied consistently across all levels of government.

## 5. It respects what taxpayers want.

- The public supports tax exemptions for nonprofit organizations. Recent polls show that nearly 8 of 10 North Carolinians think nonprofits should **not** pay taxes.
- Donors want the dollars they contribute to nonprofits to be used to provide services and accomplish missions, not to pay taxes. If contributions decreased, our government and communities would suffer from the loss of services.

## What are 501(c)(3) nonprofits?

Nonprofits that are tax-exempt under Section 501(c)(3) of the Internal Revenue Code must **operate for the public benefit**. They must be organized to achieve specific charitable, religious, educational, scientific, or literary purposes. They are required to operate very differently from for-profit businesses (see box). They agree to **give up three fundamental rights** that for-profit businesses have:

1. **Profits.** No one “owns” a nonprofit. They are required by federal law to reinvest all of their net earnings back into their missions. By contrast, for-profit businesses distribute their profits to shareholders or owners. Financially sound nonprofits do, in fact, need more revenue than expenses in order to continue their work from month to month. To be sustainable, it is important for them to maintain financial reserves as a “rainy day fund” that can cover several months of operations.
2. **Privacy.** Many documents of 501(c)(3) nonprofits are available to the public. They are required to provide their applications for tax-exempt status, which includes their basic governing documents. Those with annual budgets over \$50,000 are required to make public the Form 990 that they file every year with the IRS. The 990 includes information on their programs, revenue and expenses, key employees’ salaries, governance, and the identity of directors and officers. Smaller nonprofits are also required to identify their board officers and attest to their budget size.
3. **Politics.** Engaging in partisan politics is absolutely prohibited for 501(c)(3) nonprofits. They can lose their tax-exempt status if they make political contributions or coordinate activities with political parties or candidates for office. Very importantly, 501(c)(3) *are* allowed and encouraged to take positions on policy issues, educate elected officials about their issues, and lobby.

### How Do Nonprofits Differ from For-Profit Businesses?

**Both are private organizations, but they have these fundamental differences.**

#### Nonprofits with 501(c)(3) status:

- Primary objective is public benefit.
- Must be organized and operated for charitable, educational, religious, scientific, or literary purposes.
- Must reinvest net earnings back into the mission (but do need net earnings to be able to continue their work).
- In exchange for this public benefit, they are exempt from federal and state income taxes, most are eligible to request refunds of sales taxes they pay, and most are exempt from property tax on land and buildings they own and operate.
- Donors may deduct some of their contributions from the federal and state income taxes.
- Financial data on IRS forms is public information.
- Allowed to advocate and lobby, but prohibited from partisan politics.

#### For-profit businesses:

- Primary objective is profit.
- Net earnings may be distributed to shareholders, employees, owners, and other private individuals.
- Pay taxes on income, purchases, and property owned.
- Financial data is private except for publicly-traded corporations
- May engage in partisan politics.