Exempt Organizations
Technical Guide

TG 45: Suspension of Tax-Exempt Status of Terrorist Organizations under IRC 501(p)

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I. Overview

(1) This technical guide discusses Section 501(p) of the Internal Revenue Code (Code or IRC) suspension of tax-exempt status of terrorist organizations.

A. Background/History

(1) Prior to the enactment of Section 501(p), there wasn’t a procedure under U.S. law to suspend the tax-exempt status of an organization. Section 501(p) provides for the automatic suspension of the tax-exempt status of an organization upon designation or identification by the federal government of the organization as a terrorist organization.

(2) To revoke an organization’s tax-exempt status, the IRS completes a multi-step process:
   a. Conducting an examination of the organization,
   b. Issuing a letter to the organization proposing revocation, and
   c. Allowing the organization to exhaust the administrative appeal rights that follow the issuance of the proposed revocation letter.

(3) The organization may file a petition challenging a final revocation letter under the declaratory judgment procedures of Section 7428. The organization has an opportunity to establish its tax-exempt status under these declaratory judgment procedures.

(4) In the aftermath of the September 11, 2001, terrorist attacks, uncovering the root of terrorist financing has become one of the biggest challenges facing the United States. One significant source of alleged terrorist support has been the exploitation of charities and nonprofit organizations to raise money, move persons and materials, and provide logistical support for the international operations.

(5) To combat terrorism, the federal government has designated a number of organizations as terrorist organizations under the Immigration and Nationality Act, the International Emergency Economic Powers Act, and the United Nations Participation Act of 1945.

(6) Section 501(p) was enacted as part of the Military Family Tax Relief Act of 2003 and supports the federal government’s efforts to combat terrorism.

B. Relevant Terms

(1) Terrorist organization - An organization designated or identified as supporting or engaging in terrorist activity or supporting terrorism, as provided in Section 501(p)(2).

(2) Terrorism - Terrorism includes the unlawful use of force and violence against persons or property to intimidate or coerce a government, the civilian population, or any segment thereof, in furtherance of political or social objectives. See 28 CFR 0.85(l).
C. Law/Authority
   (1) Section 501(p)

II. Suspension of Tax-Exempt Status of Terrorist Organizations Provisions
   (1) Tax-exempt organizations designated or identified as terrorist organizations are subject to certain restrictions under suspension. Section 501(p) allows for a tax remedy for organizations erroneously designated. Section 501(p) requires the IRS to publish a notice listing each suspended terrorist organization upon its designation as such.

A. Restrictions on Suspended Terrorist Organizations
   (1) Terrorist organizations are automatically subject to the following tax consequences during the period of designation or identification as terrorist:
      a. The organization’s exemption from tax under Section 501(a) is suspended. See Section 501(p)(1).
      b. The organization’s eligibility to apply for recognition of exemption under Section 501(a) is suspended. See Section 501(p)(1).
      c. No deduction for a contribution to the organization is allowed under any provision of the IRC, including Sections 170, 545(b)(2), 642(c), 2055, 2106(a)(2), and 2522. See Section 501(p)(4).
      d. Any administrative or judicial challenge of suspension or denial of deduction is denied to the organization. Notwithstanding Section 7428 or any other provision of law, no organization or other person may challenge a suspension, a designation or identification as a terrorist organization, the period of suspension, or a denial of a deduction in any administrative or judicial proceeding relating to the federal tax liability of such organization or other person. See Section 501(p)(5).

B. Federal Authority that Designates or Identifies an Organization as Terrorist
   (1) A Section 501(p) suspension applies to an organization designated or otherwise individually identified through one of the following means described in Section 501(p)(2):
      b. In or pursuant to an executive order which is related to terrorism and issued under the authority of the International Emergency Economic Powers Act or section 5 of the United Nations Participation Act of 1945 for the purpose of imposing on such organization an economic or other sanction. See Section 501(p)(2)(B).
c. In or pursuant to an executive order issued under the authority of any federal law if:

a. The organization is designated or otherwise individually identified in or pursuant to such executive order as supporting or engaging in terrorist activity (as defined in section 212(a)(3)(B) of the Immigration and Nationality Act) or supporting terrorism (as defined in section 140(d)(2) of the Foreign Relations Authorization Act, Fiscal Years 1988 and 1989). See Section 501(p)(2)(C)(i).

b. Such executive order refers to this subsection. See Section 501(p)(2)(C)(ii).

(2) The above designations aren’t mutually exclusive. For example, some organizations are designated as a foreign terrorist organization under the Immigration and Nationality Act and as a specially designated global terrorist in an executive order under the International Emergency Economic Powers Act.

C. Period of Suspension

(1) For a terrorist organization described in Section 501(p)(2), the period of suspension is established in Section 501(p)(3).

   a. The period begins the later of the date of the first publication of its designation or identification or the date of the enactment of this Section 501(p) on November 11, 2003.

   b. The period ends on the first date that all its designations and identifications described in Section 501(p)(2) are rescinded pursuant to the law or executive order under which such designation or identification was made.

(2) Note that the period of suspension typically begins with the publication of the terrorist designation/identification by the appropriate federal agency (typically Treasury’s Office of Foreign Assets Control or the State Department) and not when the IRS subsequently publishes an announcement of the suspension. The IRS announcement helps publicize the suspension.

D. Tax Remedy for an Erroneous Designation

(1) If a designation and identification described in Section 501(p)(2) is erroneous pursuant to the law or executive order under which such designation or identification was made, and the erroneous designations and identifications result in an overpayment of income tax for any taxable year by such organization, credit, or refund (with interest) with respect to such overpayment shall be made. See Section 501(p)(6)(A).

(2) If the credit or refund of any overpayment of tax from an erroneous designation is prevented at any time by the operation of any law or rule of law (including res judicata, a claim barred because it was already judged), such credit or refund may nevertheless be allowed or made if the claim is filed before the close of the

E. IRS Notice of Suspensions

(1) If the tax exemption of any organization is suspended under Section 501(p), the IRS shall update the listings of tax-exempt organizations and shall publish appropriate notice to taxpayers of such suspension and of the fact that contributions to such organization are not deductible during the period of such suspension. See Section 501(p)(7).


(3) As of this document’s date of publication, nine organizations are suspended under Section 501(p).

III. Other Considerations Regarding Terrorism

(1) The Treasury Department, including the IRS, conducts other efforts to combat terrorism.

(2) The Terrorist Screening Center (TSC), housed within the Federal Bureau of Investigation, resulted out of Homeland Security Presidential Directive-6 (HSPD-6) signed on September 16, 2003. It is intended to consolidate the federal government’s approach to terrorism screening and to provide for the appropriate and lawful use of terrorist information in screening processes. Federal agencies, who participate in the coordination efforts, include the Department of Justice, the Central Intelligence Agency, the Department of State, Department of Homeland Security, Department of Defense, and the Department of Treasury.

(3) The Department of Treasury, Office of Foreign Assets Control (OFAC) administers and implements Executive Orders (E.O.) pursuant to a delegation of authority from the Secretary of the Treasury. OFAC has published comprehensive regulations implementing E.O. 13224 (31 CFR part 594) as amended by E.O. 13886 (84 FR 48041). OFAC acts under presidential national emergency powers as well as authority granted by specific legislation to impose controls on transactions and freeze assets under U.S. jurisdiction.

(4) As part of the comprehensive and sustained campaign against terrorist financing, all U.S. persons, including U.S.-based charities, are prohibited from dealing with persons (individuals and entities) identified as being associated with terrorism on OFAC’s Specially Designated Nationals and Blocked Persons List (OFAC SDN List). The OFAC SDN List is available at www.treasury.gov/ofac.

(5) Exempt Organization (EO) employees consider and address indicators of potential involvement in or a heightened risk of diversion of funds to terrorism in
cases they review. The Internal Revenue Manual (IRM) provides guidance for considering and addressing these indicators.

IV. Application for Recognition of Exemption

(1) IRM 7.20.6, Exempt Organizations Determination Letter Program, Anti-Terrorism and Other Emerging Issues, sets forth procedures for EO Rulings & Agreements (R&A) employees to follow regarding identification of potential terrorism activities.

(2) Procedures specific to Section 501(p) are provided in IRM 7.20.6.3. IRM 7.20.6.1 and 2 provide procedures for more general anti-terrorism considerations.

(3) Employees must review every case for potential indicators of involvement in terrorism and heightened risk of diversion of funds to terrorism. This includes all exemption applications (Form 1023, Form 1023-EZ, Form 1024, Form 1024-A, and letter applications), foundation reclassification requests, and other miscellaneous determination requests.

(4) Indicators of potential involvement in terrorism or heightened risk of diversion of funds to terrorism may include:
   a. Name or address matches against OFAC’s online Sanctions List Search
   b. Foreign grants or activities in a foreign country
   c. Other facts and circumstances

(5) Cases involving grants or activities in foreign countries may present a higher risk of terrorism, especially in countries where there is war and civil unrest. Also, in some foreign countries an organization’s assets are at higher risk for diversion to support terrorism regardless of the organization’s intent.

(6) The US Department of State maintains the official list of state sponsors of terrorism on its website. OFAC administers comprehensive sanctions programs against the State Department’s designated state sponsors of terrorism.
   a. OFAC lists these countries on its website, www.treasury.gov/ofac.
   b. An organization needs to apply to OFAC for a special license to conduct charitable operations in such countries, if OFAC has not granted a general license.

(7) For additional information visit the following websites:
   a. www.treasury.gov/ofac - various sanction programs
   b. www.state.gov/j/ct/rls/crt - US Department of State’s Country Reports on Terrorism - state sponsors of terrorism and safe havens for terrorists,

A. Guidance on Foreign Grants and Activities

(1) For guidance on foreign grants and activities see the following revenue rulings.
d. Rev. Rul. 75-65, 1975-1 C.B. 79  
g. Rev. Rul. 74-229, 1974-1 C.B. 142

(2) The following procedures may be helpful in ensuring an organization’s funds or goods are used for the intended purposes:

a. Requiring written grant agreements that specify how grant funds may be used  
b. Requiring feedback reports from foreign grantees or agents  
c. Employing report verification procedures such as on-site visits (by U.S. personnel or independent persons) or requiring supporting documentation (such as photos or receipts)

(8) In cases where an organization will make foreign grants or conduct activities in foreign countries, request sufficient information (if not included in the taxpayer’s initial submission) to determine:

a. In which countries the organization will operate or make grants  
b. What funds or goods have been or will be distributed, to whom, and for what purpose  
c. The process for grant requests, including application, review, and approval  
d. Whether the organization will check the OFAC SDN List for names of individuals and entities with whom it is dealing  
e. Whether the organization has any other practices to ensure that foreign expenditures or grants are used for intended purposes and not diverted to support terrorism or other non-charitable activities

(9) IRM 7.20.6 contains specific details on conducting an examination of an organization that conducts foreign activities or provides grants to foreign entities.

V. Examination Techniques

(1) In the course of auditing an exempt organization, sometimes known as non-governmental organizations (NGOs) in the international context, the examiner may find evidence of involvement in terrorism, such as dealings with another NGO that is suspected of funding terrorism.
A. General Terrorism Considerations

(1) NGO cases involved in potential terrorism-funding may be subject to a Joint Terrorism Task Force (JTTF) Grand Jury (GJ) investigation. As such, these sensitive cases are subject to additional security measures and may require a top-secret national security clearance.

(2) When an examiner encounters an EO that appears to be potentially involved in funding or supporting terrorism, the examiner should review the Specially Designated Nationals List (SDN List), maintained by the Office of Foreign Asset Control (OFAC). The examiner should determine if the organization or any related entity or key individual is identified on that list and document your findings.

(3) If there is a positive OFAC hit or if the examiner continues to have concerns as to the organization's involvement in supporting terrorism, all examination work should be suspended. Discuss the case with your manager and document the facts and circumstances of the case.

(4) Follow IRM 7.20.6 procedures to contact the Anti-Terrorism Coordinator (ATC).

(5) The ATC:
   - Maintains the Comprehensive List of Terrorists and Groups (CLTG)
   - Coordinates cases identified as having a risk of terrorism
   - Serves as the liaison for this issue with Internal Revenue Service - Criminal Investigation - Narcotics, Counterterrorism and Transnational Organized Crime (IRS-CI-NCT)

(6) Follow IRM 7.20.6.2.2 to complete Form 14503 based on indicators of potential involvement in terrorism or heightened risk of diversion of funds to terrorism.
   - Indicate the reasons for completing the form
   - Enter relevant case details
   - Email Form 14503 and related documents to *TE/GE-EO-Anti Terrorism


B. Procedure if Exemption of Organization Under Examination Is Suspended

(1) When a case is assigned to an agent involving an organization whose tax-exempt status has been suspended under IRC Section 501(p) (Status Code 98 in the EO Business Master File (BMF)), or is suspended under Section 501(p) during the audit, the agent will cease all audit actions and notify his/her manager.

(2) See IRM 4.70.14.4.10 Disposition of Section 501(p) Cases, for specific procedural details.