



Understanding the Revised Form 990 and Governance Disclosures – Enhancing Transparency and Compliance

March 20, 2009

9:30 am – 11:15 am

North County Philanthropy Council

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Background and Overview

- No major revisions since 1979
- Needed to address changes in tax law and increasing size, diversity and complexity of nonprofit sector
- Goals:
 - Increase transparency
 - Increase compliance and accountability (IRS/States/public)
- No relief of burden with regard to governance
- Format: Reference to Core Form/Part/Line = CF_/P_/L_

Background

- States (AG) govern most board behaviors
 - California: AG Registry of Charitable Trusts
- Many feel the IRS has gone too far
 - IRS shining light on governance practices
 - Not required for federal income tax exemption
 - But may create basis for an examination
- IRS position: A well-governed charity is more likely to obey tax laws, safeguard charitable assets and serve charitable interests and its constituents

Background

- Sources for redesign
 - Sarbanes Oxley (governance, whistleblower, etc.)
 - Independent Sector: 33 Principals for Good Governance
 - State regulators
 - Public comments (focus on privacy and minimizing compliance burden)

www.independentsector.org

Effective Date; Phase-In

- New Form 990 effective for 2008 tax year (2009 filings)
- Phase-in for smaller organizations satisfying both gross receipts and assets tests:

| <i>May file 990-EZ for:</i> | <i>If gross receipts are:</i> | <i>If assets are:</i> |
|-------------------------------|-------------------------------|-----------------------|
| 2008 tax year (filed in 2009) | > \$25,000 and < \$1 million | < \$2.5 million |
| 2009 tax year (filed in 2010) | > \$25,000 and < \$500,000 | < \$1.25 million |
| 2010 and later tax years | > \$50,000 and < \$200,000 | < \$500,000 |

- Filing Thresholds will be set permanently beginning with 2010 year at \$200,000 in gross receipts or \$500,000 in total assets

Legal Compliance – Requirements for Tax Exemption

- IRC Section 501(c)(3):

Corporations and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Legal Compliance – Requirements for Tax Exemption

- “Organizational Test” – Articles and Bylaws
- “Operational Test” – Operations and Activities
- No Private Benefit
- No Lobbying or Candidate Endorsement (certain exceptions)

=> New Form 990 elicits information for IRS to better evaluate compliance

Legal Compliance – Organizational Test

- Must be organized exclusively for charitable purposes
- Assets irrevocably dedicated to charity
- Articles and Bylaws (or Trust Document)
 - Satisfy requirements of IRC Section 501(c)(3)
 - Filed with Form 1023 exemption application
- Report significant changes or amendments of organizational documents (CF6/PVI/L4 and Schedule O)

Legal Compliance – Operational Test

- Must be operated “exclusively” for charitable purposes
- Cannot engage in non-charitable and non-incidental activities except to an “insubstantial” degree
 - UBTI and filing Form 990-T
- “Incidental” activities (e.g., hospital restaurant)
- Activities must further charitable purpose/mission as stated in Form 1023 exemption application
 - Advance approval for new activities
- CF1/PI/L1 and CF2/PIII: Description of mission and activities, and accomplishments of charitable goals
- CF3/PIV: Questions and required schedules for more information on specific activities

Redesign of Form 990 – What are the Changes?

- 990 Core Form: All Filers
- 16 Schedules (based on “trigger questions” in the Core Form)

Plan is to eliminate problems where “attach schedule” resulted in incomplete disclosure

- A Pubic Support
- B Contributors (no change)
- C Campaign & Lobbying Activity
- D Supplemental Financial Statement Detail
- E Private Schools (“Education?”)

Redesign of Form 990 – What are the Changes?

- F Foreign Activities & Grants
- G Gaming & Fundraising
- H Hospitals
- I Grants (in U.S.)
- J Compensation
- K Bonds
- L Loans
- M Non-Cash Contributions
- N Termination/Disposition of Assets
- O Open for additional info
- R Related Organizations

Redesign of Form 990 – What are the Changes?

- Form 990, Page 3 & 4, Parts IV: Checklist of Required Schedules (A thru O & R)
- Form 990, Page 5, Part V: Statements Regarding other IRS Filings and Tax Compliance
 - Other forms filed, 990-T, W-3, 1096, 8282
- Form 990, Page 6, Part VI: Governance Management & Disclosure (Not Required?)
 - Even though certain governance, management and disclosure policies and procedures may not be required under the Internal Revenue Code, the IRS considers such policies and procedures to generally improve tax compliance

Redesign of Form 990 – What are the Changes?

- Form 990, Page 7, Parts VII: Compensation Overview
 - List all current officers, directors
 - High 5 current compensated employees > \$100k
 - Former officers, key employees > \$10k
 - Includes from the Organization and any related organization
 - Calendar wages total to agree to W-2 filed
 - Must also complete Schedule J Compensation Information if Part VII discloses:
 - Any Former's (to provide more detail on the Former)
 - Any >\$150,000 (to provide ore detail on the individual)
 - Any person in Part VII perform services for pay to an unrelated organization

Redesign of Form 990 – What are the Changes?

- Form 990, Page 9, Part VIII: Statement of Revenue
 - Provides more detail to break out revenue than in previous form
- Form 990, Page 10, Part IX: Statement of Functional Expenses
 - Still required for only 501(c)(3)'s & (c)(4)'s
- Form 990, Page 11, Part X & XI: Balance Sheet & Financial Statements and Reporting
 - Organization must answer specific questions about financial statement preparation

Core Form Record Keeping Highlights

Mission

- Should address why Org. exist
- What it hopes to accomplish
- What activities it will undertake, where and for whom

Core Form Record Keeping Highlights

Ensure all proper forms are being filed

1. Information returns (1099's, W-2's, etc)
2. Form 8899 (receipt of contributed intellectual property)
3. Form 8282 (disposition of donated property within 3 years of donation)
4. Form 990-W (\$500 or more tax liability)

Process for Board review of 990 before filing

Core Form Record Keeping Highlights

Volunteers

- Page 1 – Number of Volunteers reported

Lobbying

- Sch. C – Hours spent on lobbying

Identify former officers, key employees, and highest compensated employees

Core Form Record Keeping Highlights

Donation Categories (Core Form, Pg. 5, Pt. IV, Lines 1a-f):

- Federated campaigns
- Fundraising events
- Related organizations
- Government grants
- All other contributions

Core Form Record Keeping Highlights

Fees for Services (non-employees)

- Management
- Legal
- Accounting
- Lobbying
- Fundraising
- Investment Management
- Other

Core Form Record Keeping Highlights

Audit committee

- “Assumes responsibility for oversight of the audit, review or compilation of its financial statements and selection of an independent accountant?”
- Must check the box yes or no

Endowment Funds

- Detail changes in balances
- Balances held as:
 - Quasi or Board designated
 - Permanent
 - Term

Sch. C – Record Keeping Highlights

Political Campaign and Lobbying

1. Educate board, officers, staff to understand:
 - a. Political Campaign Activities
 - Political Campaign Intervention
 - Voter Education, Voter Registration Drives – conduct in a non-partisan manner
 - Individual Activity by Organization Leaders – cannot make partisan comments while acting as official
 - Candidate appearances at event
 - Advocacy vs. Political Campaign Intervention
 - Business Activity of the Organization
 - Websites

Sch. C – Record Keeping Highlights

Political Campaign and Lobbying – Con't.

b. Lobbying Activities

- Activities attempt to influence legislation
- Can conduct education meetings, prepare and distribute materials, or consider public policy issues in an education manner

Sch. D – Record Keeping Highlights

Supplemental Financial Statement

1. Conservation Easements
2. Trust, Escrow, Custodial Arrangements
3. Endowment Funds – detail balance changes
4. Investments – Real Property, Securities

Sch. E – Record Keeping Highlights

Schools

1. Radical Composition Records:
 - a. Student Body
 - b. Faculty
 - c. Administrative Staff
2. Scholarship and Financial Aid Records:
 - a. Rewarded on a nondiscriminatory basis

Sch. E – Record Keeping Highlights

3. Collateral Material for Student Admissions, Programs, and Scholarship.
4. Collateral Material for Donations and Contributions

Sch. F – Record Keeping Highlights

1. Grant Amounts
2. Grantee Information
3. Criteria used for selection
4. Procedures for monitoring the use of grant funds
5. Procedures for the responsible expenditure

Sch. G – Record Keeping Highlights

Fundraising or Gaming Activities

1. Fundraising Activities

- a. Records for fees for services paid to non-employees for professional fundraising activities
 - Contract agreements
 - Payment Records
 - Materials and methods for solicitation campaigns

Sch. G – Record Keeping Highlights

Fundraising or Gaming Activities – Con't.

2. Fundraising Events

- a. Maintain separate accounting records for each event to provide gross revenue and expenses by event. (Major 2 events disclosed in detail)
- b. Contributions generated by event as separate revenue from admissions, ticket revenue, etc.
- c. Non-financial information such as attendance totals and volunteers.
- d. Auction items (published value providing good faith estimate)

Sch. G – Record Keeping Highlights

Fundraising or Gaming Activities – Con't.

3. Gaming Activities

- a. Separate records for each gaming activity to provide gross revenue and expenses by gaming category
- b. Record volunteer labor used

Sch. H – Record Keeping Highlights

Hospitals

1. Charitable care policy
2. Annual community benefit report prepared
3. Detailed financial data regarding charity care and other community benefits
4. Bad debt expense detail
5. Medicare detail
6. Collection practices policy regarding charitable care?
7. Management companies and joint ventures
 - Ownership % for organization, key employees, directors and physicians
8. Facility Information – Name, address, type of facility

Sch. I – Record Keeping Highlights

Grants and Other Assistance

1. Grant Making Policy and update annually for procedures used to monitor the use of grant funds
2. Maintain Grantee Information to include:
 - a. Name, Address, EIN #, IRC Code Section
 - b. Total amounts awarded, cash and non-cash
 - c. Purpose of grant, charitable category

Sch. J – Record Keeping Highlights

Compensation

1. Compensation for Officers, Directors, and Key Employees:

Required information includes:

- a. Reportable base compensation
- b. Bonus and incentives
- c. Deferred compensation
- d. Non-taxable benefits
- e. Severance payments

Sch. J – Record Keeping Highlights

Compensation – Continued

2. Review Compensation Policies
 - a. Approved by independent persons
 - b. Use comparability data
 - c. Contemporaneous substantiation
3. Travel and Reimbursement Policies

Sch. K – Record Keeping Highlights

Tax Exempt Bonds

1. Maintain detail information of bond issues Include:
issuer name, date issue, issue price, activity of bonds
and private business use
2. Same information provided to independent auditors to
show financial activity and other information required to
be disclosed as part of the audited financial statements

Sch. L – Record Keeping Highlights

Transactions with Interested Persons

1. Record keeping required on any transactions, loans, grants, and business transactions with interested persons
2. Policy regarding defining and labeling disqualified officers
 - a. Disqualified = Any person in a position to exercise substantial influence over the affairs of the organization
 - b. Excess benefit and intermediate sanctions

Sch. M – Record Keeping Highlights

Noncash Contributions

1. Record the number of contributions of noncash gifts – define contribution
2. Form 8283 – Noncash Charitable Contributions (# received)
3. Gift acceptance policy
4. Descriptions of gifts received including monetary value

Sch. N – Record Keeping Highlights

Liquidation, Termination, Dissolution or Significant Distribution of Assets

1. Description of asset, distribution date, Fair Market Value
2. Recipient information – name, address, EIN

Sch. O – Record Keeping Highlights

Supplemental Information

1. Narratives by organization to support Core Form 990 and schedules in correct order and structure
2. Include Policies (to be discussed in next segment):
 - a. Conflict of Interest Policy
 - b. Whistleblower Policy
 - c. Document Retention Policy
 - d. Investment Policy

Sch. R – Record Keeping Highlights

Related Organizations and Partnerships

1. Identification information of the entities and basic financial information (gross income, assets, and transactions for the reporting period)

Legal Compliance – Private Benefit

- Organization's assets cannot benefit of private parties
- Reasonable salary and market value payments for goods or services
- Detailed compensation reporting for officers, directors, trustees, key employees, and independent contractors
 - Review and approval by independent persons
 - Comparability data
 - Contemporaneous substantiation

Legal Compliance – Interested Person Transactions

- Must report direct and indirect transactions (e.g., loans, business transactions, assistance) between an organization and “interested persons”:
 - Officers, directors, trustees (“o/d/t”)
 - Key employees, defined as:
 - Paid greater than \$150,000;
 - Had or shared organization-wide authority similar to a o/d/t, or responsible for >10% of organization’s activities; AND
 - One of the top 20 highest compensated.
 - Substantial contributor
 - Certain persons and entities related to the foregoing

CF3/PIV/L25-28 and Schedule L

Legal Compliance – Excess Benefit Transactions

- Must report “excess benefit transactions” (“EBT”) with “disqualified persons”
- EBT is a transaction in which economic benefit is directly or indirectly provided by an applicable tax-exempt organization to or for the use of a disqualified person, and the value of the benefit exceeds the value of the consideration provided by the disqualified person (e.g., excessive salary, free use of organization assets)
- PIV/L25a – Current EBT
- PIV/L25b – Become aware of prior EBT

Legal Compliance – Excess Benefit Transactions

- “Disqualified person” is any person who was in a position to exercise substantial influence over the affairs of the organization at any time during a 5-year period ending on the date of the transaction (including officers, directors, trustees), and:
 - Certain family members of a disqualified person
 - 35% controlled entities of a disqualified person
- Rebuttable presumption of reasonableness
 - Approved by non-conflicted authorized body
 - Decision based on appropriate comparable data
 - Concurrent adequate documentation of decision

Legal Compliance – Excess Benefit Transactions

- EBT must be corrected by disqualified person (payment)
- IRC Section 4958 Intermediate Sanctions:
 - Excise tax equal to 25% of excess benefit imposed on disqualified person
 - Additional 200% excise tax if not timely corrected (prior to statutory notice of deficiency; 90-day cure for abatement)
 - 10% excise tax on organization managers who knowingly participate in transaction
- EBT may also lead to loss of exempt status in certain circumstances

Board Structure and Relationships

- Number of voting members of the governing body (CF/PI/Q3 and PVI/L1a) as of year end
- Disclose any special or limited voting rights (Schedule O)
- Number of independent voting members (CF/PI/L4 and PVI/L1b)
- Board relationships (CF/PVI/L2)
- California “interested director” rule: no more than 49% of directors may be compensated

Conflict of Interest

- Written policy (CF/PVI/L12a)
- More than Form 1023 policy
- Annual disclosure (CF/PVI/L12b)
- Regularly and consistently monitor and enforce compliance (CF/PVI/L12c)
- Document in board minutes

Public Disclosure and Procedures

- Sharing with the states (CF/PVI/L17)
 - E.g., California requires with Form RRF-1
- Informs IRS of states in which organization operates or solicits donations
- Form 990, 990-T and 1023 (CF/PVI/L18)
- Describe how made available to public (CF/PVI/L19 and Schedule O)
 - Governing documents (Form 1023, Articles, Bylaws)
 - Financial Statements
 - Conflict of Interest Policy

Public Disclosure and Procedures

- Need not comply with written request for documents if already made “widely available” (internet posting)
 - Web page must inform readers that documents available for downloading
 - Any individual with access to the internet can download, view and print the documents in exact reproductions without special formatting hardware or software
- Intent is to improve accountability and transparency

Document Retention Policy

- Policy should include:
 - Specific types of documents
 - Length of time to retain
 - When permissible or required to destroy
 - Paper and electronic documents
 - Archiving of documents
 - Backup procedures and regular check-ups of the reliability of the system
 - Ensure destruction halted if official investigation

Document Retention Policy

- Must retain permanently
 - Organization documents
 - Board minutes
 - Documents related to State and Federal Tax Exemption

Public Charity vs. Private Foundation – Support Tests

- 33 1/3% Public Support Test
- 10% Public Support Test; Facts and Circumstances
 - Continuous and bona-fide public support program
 - Sources of funding
 - Board represents broad interest of public; public served
- 5-Year computation period
- No more advanced ruling period

- CF3/PIV/L1 and Schedule A
- Schedule B (large contributors)

990 Review Process

- Can use a committee
- CF/PVI/L10 – “Was a copy of Form 990 provided to the governing body before it was filed?”
- Describe the process the organization uses to review the Form 990 on Schedule O

Board Member Roles & Responsibilities

- Legal Responsibilities
- Leadership Responsibilities
- Stewardship Responsibilities

Legal Responsibilities

- Duty of Loyalty
- Duty of Obedience
- Duty of Care

Duty of Loyalty

Key Duties

- Decisions benefit the organization
- Disclose potential conflicts
- Avoid compensation with the organization

Duty of Loyalty

Important Items to Accomplish

- Be UNSELFISH in doing your duty
- Disclose CONFLICTS OF INTEREST
- Create a POLICY for how to address C.o.I.
- Keep board business CONFIDENTIAL
- Be INFORMED of current laws and statutes

Duty of Loyalty

Recommendations

1. **Review Status of Conflicts Policy** – Evaluate scope, sufficiency and compliance
2. **Outside Board Service** – Set a Policy for service on other boards
3. **Confidentiality** – Use a Confidentiality Agreement
4. **Nominating Committee** – Review nominating standards to avoid people with conflicts of interest

Duty of Obedience

Key Duties

- Follow charter, bylaws and articles
- Comply with federal and state laws
- Faithful to the mission and goals
- Ensure financial records and procedures to safeguard assets

Duty of Obedience

Important Items to Accomplish

1. Make sure the organization is obedient to its **CENTRAL PURPOSE**

Duty of Obedience

Recommendations

1. Review the “statement of charitable purposes”
2. Adopt decision-making processes for decisions that affect this mission

Duty of Care

Key Points

- Members should gather all information before decision making
- Board members need not always be right, but must act with common sense and good judgment
- Requires active participation
 - Meetings and activities
 - Read minutes and reports
 - Review performance of E.D. and organization

Duty of Care

Important Items to Accomplish

1. Know the CIRCUMSTANCES of the Situation
2. Act with CARE and PRUDENCE
3. Have DIRECTION and Responding to Conflicts
4. Keep good records and be TRANSPARENT

Duty of Care

Recommendations

1. Review how decisions are brought to the board for approval
2. Adopt clear, concise governance policies
3. Review the manner in which board oversees management activities
4. Review management of funds.

Top 10 Things to Do Now

1. Checklist of policies
2. Fill any gaps or document reasons for not having a policy (i.e., no payment to officers, so no compensation review)
3. Review existing policies for compliance
4. Review procedures
5. Review record keeping
6. Board compliance calendar
7. Board committees and reports
8. Schedule regular board education
9. Schedule regular compliance checks and reporting out on high risk areas
10. Contact tax and legal advisor as needed

Resources

- www.boardsource.org
- www.independentsector.org
- www.stayexempt.org
- www.smithsonian.org
- www.ncna.org
- www.irs.gov