

Corporate Advisory - Tax Exempt Organizations Practice Group

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NEW IRS FORM 990 -- Where is Your Board's Compliance Plan?

The IRS Form 990 is the annual information return that must be filed by most nonprofit organizations, including charities, trade associations and other tax exempt organizations. For tax years beginning in 2008, many tax exempt organizations will be required to prepare and file a newly redesigned IRS Form 990. For others, the new Form 990 will be phased in over a three-year period.

Of immediate and critical importance is a new series of questions, which ask whether your organization's governing board has adopted certain governance and management policies and disclosure practices by December 31 (or the end of the organization's fiscal year beginning in 2008). For many questions, the preferred response will be YES. For other questions, it may be more appropriate for an organization to answer NO and be prepared to explain the reason for its response.

The biggest challenge will be to get your governing board to consider these important issues as soon as possible in light of your organization's particular operational and legal requirements.

Background

The redesigned Form 990 is the biggest project the IRS has undertaken relating to the tax exempt community in the last quarter century. The redesigned Form 990 has been described by many as an extension of Sarbanes-Oxley principles to the nonprofit sector. It also is a reaction to specific scandals and questionable practices involving prominent tax exempt organizations such as the United Way, American University and the Smithsonian Institution.

As the IRS notes in its background documents, the redesign of the Form 990 is intended to: (1) enhance the Form 990 as the key transparency and disclosure tool relied on by the public, state regulators, the media, researchers, and policymakers to obtain information about a tax exempt organization; (2) strengthen the disclosures required by the Form 990 to promote accountability by tax exempt organizations; and (3) bolster and add new disclosures to position the redesigned Form 990 as the IRS' primary tax compliance tool for tax exempt organizations.

A New Core Form and 16 Schedules

The redesigned Form 990 consists of a new core form, that must be completed by all organizations required to file the new form. There are also 16 schedules that organizations must complete to the extent they are applicable.

Among other things, the new Governance section in the core form asks whether your organization has a conflict of interest policy, a whistle blower policy, and a document retention/destruction policy. If nothing else, the governing body of every tax exempt organization should adopt these three basic policies as soon as possible, since they represent and incorporate good governance practices, and help guard against Sarbanes Oxley liability.

The new Form 990 also inquires about the independence of the board; the outside relationships of board members to one another (about which the organization must carefully inquire); the authority of members to elect the governance body and approve board decisions; whether the board and board committees keep minutes; and if there are written policies and procedures for chapters, branches and affiliates.

The new Form 990 asks whether an organization discloses its governing documents, conflicts policy and financial statements to the public. Another question asks if there is a committee that assumes responsibility for oversight of the outside accountant. There is also a question whether the governing board is provided a copy of the Form 990 before it is filed (and a requirement to describe the organization's Form 990 review process).

The new Form 990 also asks whether an organization's process for determining compensation for top management includes review and approval by "independent persons," the use of comparability data, and contemporaneous substantiation of the deliberation and decision. Public disclosure of the compensation of many senior exempt organization employees will be required for the first time. For organizations required to file Schedule J, there is a series of check boxes regarding certain fringe benefits provided to highly compensated individuals such as first class and companion travel, tax indemnification and gross ups, health and social clubs, discretionary spending accounts, housing, business use of a residence, and the provision of personal services (e.g., maid, chauffeur, chef). Although these fringe benefits are not unlawful, such expenditures should be appropriate for your organization and you should make sure your organization is properly reporting them for tax purposes.

Other parts and schedules of the new Form 990 inquire about contributions, fundraising, gaming, lobbying/political activities, gift acceptance policies for those organizations that accept non-cash contributions, policies for organizations that enter into joint ventures, limited liability companies and partnerships with others, and grant-making record-keeping procedures and criteria for organizations that make both foreign and domestic grants. There are also special schedules for schools and hospitals (which include questions about their anti-discrimination policies and charity care and debt collection policies).

How Should Your Organization Respond?

How will your organization respond to the questions posed by the new Form 990? Will and should your organization answer YES to all of these questions? Is your organization prepared to provide an adequate explanation if it decides it is more appropriate to answer NO to some of these questions?

CONTACTS

If you would like more information, please contact any of the McKenna Long & Aldridge attorneys or public policy advisors with whom you regularly work. You may also contact the following members of the Tax Exempt Organizations Practice Group:

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The introduction to the new Governance section states that the information required to be disclosed is NOT required by the Internal Revenue Code (and also may not be required by any state authority). Even though these policies and procedures are not required under the Internal Revenue Code, the IRS is alerting the tax exempt community that it considers such policies and procedures important for tax compliance.

The policies that each organization adopts must be appropriate to its particular circumstances and legal requirements. Some of the questioned practices, like the public disclosure of financial statements, seem more appropriate on their face for charities than trade associations, so that also is a factor to consider.

It is also important to note that the redesigned Form 990 is no longer merely a financial document or tax return. The IRS redesign has transformed the Form 990 into a public disclosure tool that many, including the IRS, Congress, state regulatory authorities, potential contributors, members, the media and bloggers, may use to evaluate the efficiency, effectiveness and merit of your organization.

Although your accountant or tax advisor will remain critical in preparing the financial sections of the Form 990 and compiling the entire document, responding to the new Form 990 will require involvement by your board or a board committee, legal advisers, fundraisers and perhaps others in your organization who are responsible for the public image of your organization.

If you have not already done so, now is the time to assemble your team and develop a plan to review your governance and management policies, and to prepare for and respond to the redesigned Form 990.

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