

# 990 HANDBOOK

## Unified Financial Reporting System for Not-for-Profit Organizations

A Comprehensive Guide to Filing IRS Form 990, Part I

**990** Return of Organization Under section 501(c), 527, or 4947(a) benefit to

Department of the Treasury Internal Revenue Service

The organization may have to use a

**A** For the 2007 calendar year, or tax year beginning

**B** Check if applicable:

- Address change
- Name change
- Initial return
- Termination
- Amended return
- Application pending

Please use IRS label or print or type. See Specific Instructions.

**C** Name of organization

Number and street (or P.O. box, if no street address)

City or town, state or country, and ZIP+4

• Section 501(c)(3) organizations and trusts must attach a completed Schedule B

**G** Website: ▶

**J** Organization type (check only one) ▶  501(c) ( ) ▶

**K** Check here ▶  if the organization is not a 509(a)(3) and gross receipts are normally not more than \$25,000. A return is not required to file a return, be sure to file a complete return.

**L** Gross receipts: Add lines 6b, 8b, 9b, and 10b to line 10c

**Part I Revenue, Expenses, and Changes**

**1** Contributions, gifts, grants, and similar amounts received

- a** Contributions to donor advised funds
- b** Direct public support (not included on line 1a)
- c** Indirect public support (not included on line 1a)
- d** Government contributions (grants) (not included on lines 1a through 1c)
- e** Total (add lines 1a through 1d) (cash \$)

**2** Program service revenue including government contracts or grants

**3** Membership dues and assessments

**4** Interest on savings and temporary investments

**5** Dividends and interest from securities

**6a** Gross rents

**b** Less: rental expenses

**c** Net rental income or (loss). Subtract line 6b from line 6a

**7** Other investment income (describe in Part VII)

**8a** Gross amount from sales of assets other than inventory

**b** Less: cost or other basis and sales expenses

**c** Gain or (loss) (attach schedule)

**d** Net gain or (loss). Combine line 8c and line 8b

**9** Special events and activities (attach schedule)

**a** Gross revenue (not including \$500 or less contributions reported on line 1)

**b** Less: direct expenses other than those reported on line 1

**c** Net income or (loss) from special events and activities

**10a** Gross sales of inventory

**b** Less: cost of goods sold

**c** Gross profit or (loss) from sales of inventory

**d** Other revenue (from Part VII, line 10)

**Total revenue.** Add lines 1e, 2, 3, 4, 5, 6c, 7, 9c, 10a, and 10c

Program services (from line 2)

Management and general (from line 3)

Fundraising (from line 4)

Payments to affiliates (attach schedule)

The nonprofit sector's **new report card**

Governance and the revised IRS Form 990: New roles for trustees

by Tom Hyatt

The quest for good governance in the nonprofit sector has received more thoughtful attention in the last five years than ever before. Charity governance standards organizations, watchdog groups, states' attorneys general and Congress all have had their say. Now, the quest has been joined by an unlikely ally that may prove to be the most influential of them all: the Internal Revenue Service.

Most trustees and directors of nonprofit organizations likely do not associate the realization of the core governance principles of accountability, transparency and compliance with the completion of Form 990, the Internal Revenue Service (IRS) information return that is filed each year by most tax-exempt organizations. It is often dismissed by trustees as a tax form, best left to accountants, the chief financial officer and the audit committee. With the introduction in 2008 of the IRS' all-new Form 990, the time has come to discard those notions and to accept and embrace the role that directors must play in enabling their organization to prepare the new 990 in a manner that effectively demonstrates that the organization is well governed. As is often the case, the journey to that result is of greatest importance here. It is an opportunity for the board of trustees to more fully understand and give needed direction to the organization they serve.

In December 2007, the IRS issued its redesigned Form 990. It had previously released a discussion draft, and solicited and incorporated many public comments in a commendably collaborative effort with the nonprofit sector. The use of the form dates back to the 1940s; however, in the view of the IRS, the existing 990 failed to reflect important changes in the law affecting nonprofits and the increasing size, diversity and complexity of the tax-exempt sector. It can fairly be said that the existing Form 990 is inadequate to illuminate the inner workings of exempt organizations or to permit peer comparisons to the extent desired by the IRS, the public and exempt organizations themselves. Accordingly, the IRS launched an

extensive effort to redesign Form 990 to capture relevant information about the modern tax-exempt organization.

Make no mistake about it, this redesign is revolutionary. According to the IRS, it is intended to provide greater transparency, promote compliance and lessen the burden on the filing organization. (Two out of three ain't bad.) Here are eight things nonprofit directors should know now about the new Form 990 and how it will affect their organization.

### 1. This is much more than a tax form.

If you ever were of the mind that the Form 990 was a tax document that didn't require board involvement, it is time to change your point of view. The IRS uses the 990 as its primary tax compliance tool for tax-exempt organizations. It is a public record document, readily available on the Internet. Most states also rely on the form to perform charitable and other regulatory oversight. Moreover, the new Form 990 is so much more than a financial reporting document. It contains questions designed to delve deeply into the governance processes of the organization, its compensation mechanisms and its operating policies. Certainly, the financial disclosures remain a key portion of the form, including all-new disclosures about compensation and endowments. However, it is essential that the board goes through the exercise of answering the governance-related questions and making informed choices about which practices and policies to adopt so as to ensure effective governance.

### 2. This is not your grandfather's Form 990.

The original Form 990 was two pages long. The new Form 990 has a core form that is 11 pages long and may include up to 16 schedules. In its public comments to the IRS on the redesigned 990, the National Association of College and University Business Officers



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(NACUBO) predicted that many large and mid-sized institutions will need to add one full-time administrative position for collecting and reporting data required by the new form. While the burden on filing organizations will surely increase, notwithstanding the IRS' goal to the contrary, that burden is not management's alone. There is meaningful governance work to be done by boards in preparing the responses that are called for in the expanded scope of the form.

### 3. The clock is ticking.

The final redesigned Form 990 is in effect now. It applies to a tax-exempt organization's 2008 tax year, which is the fiscal year of the organization that begins in 2008. Accordingly, organizations with a calendar fiscal year had only until the end of 2008 to implement needed governance policies identified in the form; those with fiscal years ending on June 30 have less than a year. The relevant deadline here is the end of the organization's 2008 fiscal year, not the form's filing deadline. Governance policies inquired about by the IRS include: conflicts of interest, protection of whistleblowers, document retention and destruction, compensation policy and practice, joint ventures, chapters and affiliates, expense payments and reimbursements, gift acceptance, compensation review, and Form 990 review. Adoption, or even review and updating, of these policies is too important to cram into the already full agenda of a year-end board meeting. These deliberations should have taken place by now, and in a thoughtful and thorough manner. More than one board or committee meeting may well be required.

### 4. The board of trustees will be more involved in review of the form.

Typically, Form 990 is prepared by the organization's finance staff or its external accountants. While these professionals will still have the heavy lifting responsibilities for much of the form, it is critical that the organization's board be involved in the process with respect to the governance and operational questions raised by the form. Perhaps the most important governance questions on the new Form 990 are these: Was Form 990 provided to the board before it was filed? What is the process the institution uses to review Form 990?

The IRS does not require prior *approval* of the 990 by the board and there is no legal penalty for the failure of a board to do so. However, these questions point out the need of the board of directors to be conversant in the information presented in the Form 990. While prior review may pose some logistical problems when filing deadlines get tight, this role is vital and a fiduciary duty of the board under its duty of care.

The obligation to describe the organization's Form 990 review process begs the question: Do we even have such a process? If you don't, you're in good company. In a 2007 Grant Thornton survey, *National Board Governance Survey for Not-for-Profit Organizations*, 70 percent of the respondents had not established a policy for board members to review the organization's Form 990. Clearly, this is a new role for nonprofit boards and some trial and error will no doubt be necessary as the board and management work through what such a review should entail.

Many of those commenting to the IRS suggested that this duty could be fulfilled through review by a board committee, such as the audit committee. And, indeed, the IRS alludes to the acceptability of this practice in the new form's instructions. But, to

consign review of the governance-related responses solely to a board committee is to miss an important opportunity for the organization to receive essential, hands-on leadership from all of its trustees or directors.

### 5. The new Form 990 may elevate some governance best practices to de facto requirements.

Throughout the form, questions are asked with respect to whether the organization has various governance policies in place or whether it follows particular "good governance" practices. For example, Part VI of the core form is entirely dedicated to statements regarding governance, management and disclosure. It asks the following questions:

- How many voting members are on the governing body? How many of them are independent?
- Does the organization have a written conflict of interest policy?
- Does the organization have a written whistleblower policy?
- Does the organization have a written document retention and destruction policy?
- Does the organization contemporaneously document the meetings of the governing body and its committees?
- If the organization has local chapters, branches or affiliates, does it have written policies and procedures governing their activities to ensure that their operations are consistent with the organization's?
- How do you make the following available to the public: governing documents, conflict of interest policy, Forms 1023, 990 and 990-T, and financial statements?

The IRS has stated in Form 990 that the governance policies addressed are not required by the Internal Revenue Code. While most of the best practices suggested by the new form have found widespread acceptance in recent years, there is not universal agreement on the need for these practices for all nonprofit organizations or on how they should be implemented. What are the consequences of answering “no” to whether the organization has adopted these policies? Trustees should be prepared to explain the governance choices they have made in such cases and should avoid allowing the 990’s default choices to establish best practices without careful deliberation regarding what works best in their own organization.

## 6. Be ready to discuss your endowment funds.

A new Schedule D, Supplemental Financial Statements, has been included in the new Form 990. The schedule calls for disclosure of certain financial information regarding the endowment funds of exempt organizations, including the amount of contributions, earnings and losses, expenditures for facilities and programs, and administrative expenses, both for the current year and a four-year look-back period.

The value of requiring such disclosures in the absence of a meaningful basis for comparing the reported amounts between institutions is questionable. This issue is likely more germane to higher education organizations than to any other member of the exempt community. Institutions of higher education vary greatly in the size of their endowments, and the rate of spending of investment earnings on such funds varies for a multitude of reasons unique to each institution. These include building new facilities, recruitment of faculty, student financial aid, increases or decreases in enrollment, and investment return. Also, based on higher education surveys, over 90 percent of endowment funds are donor-restricted.

Again, this imposes spending constraints that are unique to each institution; valid comparisons of institutions based on a general expenditures disclosure are elusive.

Nevertheless, educational institutions operate in a time of increasing scrutiny of their endowments and Congress is weighing new restrictions, taxes and mandatory payouts. Trustees should be prepared to answer public questions that will arise from these disclosures and to have a dialogue with their institution’s administration regarding the significance of the variance in results among higher education institutions.

## 7. Be ready to discuss executive compensation.

It is now clear to trustees of tax-exempt organizations that the compensation of the president and senior leadership has been the subject of increasing scrutiny by regulators, Congress and charity watchdog groups. With the advent of the new Form 990, we will surely see that trend continue; however, it should lead to a more informed and reasoned discussion of compensation and a more legitimate comparison between institutions.

Part VII of the core form requires disclosure of compensation to officers, directors, trustees and key employees from the organization and its related organizations. The new Schedule J, Supplemental Compensation Information, requires disclosure of compensation for these individuals that is broken down in greater detail than ever before required of tax-exempt organizations. Disclosure is mandated not only for base compensation, but also for bonuses and incentives, severance and change in control payments, first-class travel, spousal travel, club fees, housing allowances, supplemental nonqualified retirement plans, and equity-based compensation.

With this level of disclosure, all trustees and directors, not just those who serve on the compensation committee, will need to more fully understand the compensation mechanisms of the institution and be prepared to respond to questions that result from these disclosures.

## 8. The ascendancy of the independent trustee or director.

No doubt drawing from the reforms instituted for publicly traded firms in the wake of the Sarbanes-Oxley Act of 2002, the new Form 990 shines the spotlight on the presence of independent trustees or directors serving on the board. The first page of the new form, intended to act as a snapshot of critical data that can easily be compared between institutions, specifically asks how many independent voting members serve on the governing body. This answer is drawn from Part VI of the form, which also inquires about family and business relationships between directors, officers and key employees. Independence in this context is generally defined as not receiving compensation from or doing business with the organization or related organizations beyond a specified threshold.

The IRS has long required that tax-exempt healthcare organizations have “community boards” with independent directors in the majority. Clearly, the new 990 reveals the IRS’ view of the importance of independent board members in securing compliance with tax exemption rules for all tax-exempts.

The implementation of the new Form 990 should be embraced by all tax-exempt organizations as an opportunity to improve transparency and achieve greater accountability. Those that do so will strengthen their ability to achieve their missions and sustain the public’s support. More than ever, Form 990 will serve not as a tax form but as a report card. Trustees and directors should ensure that they are proud to show it off. |

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