**From:** Michele Wales
**To:** *TE/GE-EO-F990-Revision;
**CC:** Mike Batts;
**Subject:** Comments regarding draft Form 990
**Date:** Friday, September 14, 2007 1:32:14 AM
**Attachments:** comment letter to IRS re 990 revision.pdf

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Please find attached a PDF file containing our firm's comments regarding the draft Form 990.

We appreciate the opportunity to provide this input.

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MICHAEL E. BATTS, CPA
MANAGING SHAREHOLDER

September 14, 2007

Internal Revenue Service
Tax-Exempt & Government Entities Division
Office of Exempt Organizations
Form 990 Redesign
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Washington, DC 20224

VIA EMAIL TRANSMITTAL: form990revision@irs.gov

Dear Sir or Madam:

We are writing in response to your request for comments concerning the draft Form 990 revision. We applaud the Service's stated principles of enhancing transparency, promoting compliance and minimizing the burden on filing organizations. We believe that the following comments may be useful to the Service in accomplishing these objectives.

General Comments

1. We believe that the "core form" approach with accompanying schedules requiring more detailed information for certain transactions/activities may serve to enhance transparency and promote greater uniformity in the way such information is reported on the Form 990 and accompanying schedules. However, in order to minimize the burden on filing organizations while still promoting transparency and compliance, we suggest that the IRS consider increasing the filing and reporting thresholds for the Form 990, accompanying schedules, and certain information contained in those documents. For example the IRS might consider:

   a. Increasing the filing threshold for use of the Form 990-EZ (currently available for organizations whose gross receipts are less than $100,000 and whose total assets are less than $250,000 at the end of the year),

   b. Increasing the reporting threshold for business relationships between officers, directors and key employees (see draft Form 990, Part II, Section B, line 5b), currently set at $5,000,

   c. Establishing a threshold for the filing of items listed in Parts I through VII of Schedule D (Supplemental Financial Information), and/or allowing the filing organization to file schedules printed or uploaded from its internal tracking software (such as depreciation schedules maintained in Excel),

   d. Increasing the filing threshold for Schedule G (Supplemental Information Regarding Fundraising Activities), currently set at $10,000,

e. Increasing the reporting threshold for grants and other assistance to governments and organizations in the United States (see Schedule I, Part II), currently set at $5,000 per recipient, and

f. Increasing the filing threshold for Schedule M (Non-Cash Contributions), currently set at $5,000.

Comments Regarding Specific Forms/Schedules

2. Form 990, Part IV – business codes – We suggest that, if the IRS intends for filing organizations to use such codes to describe its exempt revenue-generating activities as well as its taxable activities, the list of businesses found in the current Form 990-T instructions should be significantly expanded to include a comprehensive listing of exempt revenue-generating activities normally carried on by nonprofit organizations.

3. Form 990, Part IX, lines 2 and 3 – the determination of the "most significant" program service accomplishment during the year is ambiguous and overly subjective. We suggest that the IRS consider rewording this question to request a short summary of the filing organization's primary exempt purposes. The information requested in item 3 should then elicit information regarding the most significant activities (measured in terms of expenditures devoted to each specific activity) carried on in furtherance of the organization's exempt purposes as delineated in item 2. In addition, no "total" for direct revenue requested on line 3e should be required to be reported, since this total will generally not coincide with total revenues for those filing organizations whose revenues in include direct public support for its overall mission.

4. Schedule A, Part I, line 11f – determination letters of supporting organizations dated prior to the enactment of the Pension Protection Act of 2006 do not generally indicate whether the organization has been classified by the IRS as a Type I, Type II or Type III supporting organization. The instructions to the Schedule A should indicate the process whereby a supporting organization can request a written determination of its status from the IRS, as well as how a filing organization should address the question if it has not received such a determination.

5. Schedule A, Part II, lines 9 and 10 – the delineation between the types of income that are required to be reported on line 9 (net income from unrelated trade or business activities, whether or not the business is regularly carried on) and line 10 (gross receipts from activities that are not an unrelated trade or business under section 513) should be further clarified in the instructions. The instructions as currently written may cause confusion as to the proper line on which to report (and therefore whether to report gross receipts or net income) revenues from fundraising events and other activities that do not meet the section 513 criteria for exclusion from unrelated business income, but are nevertheless excluded from unrelated business income because they are not regularly carried on. We believe that the schedule and instructions as currently written are self-contradictory, since, as defined in the Internal Revenue Code, an activity must be regularly carried on in order to be an "unrelated trade or business activity."

6. Schedule F – the instructions as currently written would require that Schedule F be completed by organizations whose sole foreign activity consists of grants made to recipients located in foreign countries, including the making of grants to a U.S. organization if more than one-half of that organization's activities are conducted in a foreign country or directed to persons in a foreign country. In many cases, a grantor organization may not know in which countries the grantee organization specifically operates, or the extent to which the granted funds were expended within the U.S. or within a foreign country. The IRS should consider excluding from Schedule F grants made by one U.S. charity to another U.S. charity, since the grantee organization would be required to report the expenditure of those grant funds on its own Schedule F filed with its Form 990.

7. Schedule J – we believe that the requirement that nontaxable expense reimbursements for meals, travel and entertainment paid to officers, directors, key and highly compensated employees under an accountable plan be reported as compensation on Schedule J would create a significant and unreasonable additional recordkeeping burden on reporting organizations, and would also create confusion to users of the Form 990. Such payments are generally not compensatory in nature, but rather represent a business expense related to the conduct of an organization's exempt activities. An officer employed by an exempt organization which serves a large geographic area might incur significant travel-related expenses in carrying out his duties, while an officer of an

organization serving a small geographic area might not. To require disclosure as "compensation" the amounts paid by the first organization to its officers for travel-related reimbursements under an accountable plan is not only incorrect (since such amounts are generally not compensatory in nature), but also serves to falsely inflate the reported compensation figures of individuals employed by such organizations. The IRS should consider excluding these types of reimbursements from the amounts reportable on Schedule J.

We also believe that similar issues arise from the proposed requirement that excludible fringe benefits under IRC §132 paid to officers, directors, key and highly compensated employees be reported as compensation on Schedule J. Reporting such amounts would create a significant and unreasonable additional recordkeeping burden on reporting organizations, and would create confusion to users of the Form 990. To require disclosure of such amounts as "compensation" serves to falsely inflate the reported compensation figures of individuals employed by such organizations. The IRS should consider excluding these types of benefits from the amounts reportable on Schedule J.

We hope you find these comments helpful and look forward to reviewing further revisions to the draft Form 990. If you have any questions concerning the above, please feel free to contact me accordingly.

Sincerely,

Michael E. Batts, CPA

MEB:mw

**From:** James R. King
**To:** *TE/GE-EO-F990-Revision;
**CC:** Schultz Ronald J; Pattara Theresa; Gerald Griffith;
**Subject:** Comments on Independence of Board Members and Conflict of Interest
**Date:** Friday, September 14, 2007 7:39:01 AM
**Attachments:** JD_1381588_2 - King-Griffith Redesigned Form 990 Comment Ltr 14 Sep 07.pdf

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Dear Director Lerner,

My partner, Gerry Griffith, and I would like to submit the attached comments regarding board independence and conflicts of interest. As we develop in more detail in the attached letter, we respectfully request that, in finalizing the redesign of the Form 990, the Service take into account our comments that:

- The Glossary and/or Instructions to the Redesigned Form 990 should make clear that there is no substantive law requirement for any particular percentage of independent directors;
- The Glossary definition and/or Instructions to the Redesigned Form 990 should be expanded to give guidance as to what constitutes a "material benefit" and/or that any future IRS guidance address this issue as well;
- That "materiality" should be judged by the "close and continuous connection" standard set forth in the Service's FY 1997 Continuing Professional Education Text article, "Tax-Exempt Health Care Organizations Community Board and Conflicts of Interest Policy," by Lawrence M. Brauer and Charles F. Kaiser;
- That independence of board members should be assessed by applying general rules, illustrated with multiple, detailed examples, and that the IRS defer to the business judgment of a board as to what is a "material interest" for that board in cases where the board has in good faith, and exercising ordinary care and business prudence, established reasonable materiality standards for that board; and
- That the definition of "conflict of interest" for exempt organizations be limited to financial conflicts of interest and not extend to nonfinancial conflicts.

Thank you for your consideration.

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JP174285:tj September 14, 2007

VIA E-MAIL

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Director of the Exempt Organizations Division
Internal Revenue Service
Form 990 Redesign, SE:T:EO
1111 Constitution Ave., N.W.
Washington, DC 20224

Re: Comments on the Draft Redesigned Form 990

Dear Director. Lerner:

We appreciate the significant effort that the IRS has invested in the draft redesigned Form 990 ("Discussion Draft") released on June 14, 2007, and we believe that, if finalized, the Discussion Draft will enhance transparency and promote accountability among exempt organizations. In that regard, we note that the IRS already has received hundreds of pages of excellent comments about a wide variety of concerns and requests for clarification. However, we believe that two areas of concern exist with the Discussion Draft that have not been adequately addressed in the prior comments we reviewed. Accordingly, we are submitting these supplemental comments regarding the Discussion Draft's definition of "independence" for an exempt organization's governing board and the scope of "conflicts of interest" for Form 990 reporting purposes.

## "Independent Member" of the Governing Board.

### Glossary Definition of Independence

The Discussion Draft's core form refers to the concept of "independent member" of a governing body three times.[1] Citing both the work product of the Panel on the Nonprofit Sector Revised Principles – Draft for Public Comment (the "Revised Principles")[2] and the Intermediate Sanctions Regulations criteria for conflicts of interest,[3] the Glossary accompanying the Discussion Draft defines an "independent member of [a] governing body" as follows:

[1] Part I, Line 4; Part II, Section B, Line 3; and Part III, Line 1b.

[2] See Revised Principles at p. 13. The Revised Principles are available online at www.nonprofitpanel.org/selfreg/Effective_Governance_Revised.pdfTreas.

[3] Reg. 53.4958-6(c)(1)(iii).


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> A person: [i] Who is not compensated as an employee of the organization; [ii] Who does not receive compensation or other payments from the organization as an independent contractor (other than reimbursement of expenses or reasonable compensation for services provided in the capacity of serving as a member of the governing body); [iii] Who does not receive, directly or indirectly, ***material financial benefits***[4] from the organization except, if applicable, as a member of the charitable class served by the organization; and [iv]Who is not a spouse, sibling, parent, or child of any individual who is employed by, or receives compensation or other ***material benefits*** from, the organization.

(Emphasis added).

**Concept of Board Member Independence**

"Independence" in this context is an entity-level concept. That is, it looks at an individual's overall relationship with an organization to determine whether he or she is sufficiently independent of the organization from a financial standpoint to serve as an "independent" board member. As the Revised Principles note, under state charitable organization and state nonprofit law, directors of a tax-exempt organization owe that organization a "duty of loyalty" that requires them to put the interests of the organization above their personal interests and to make decisions they believe are in the best interests of the organization. The Revised Principles then note that individuals who have a personal, financial interest in the affairs of the organization may not generally be as likely to question the decisions of those in management who determine their compensation or fees or to consider changes in management or program activities that might advance the mission and improve the services of the organization. As a result, again as noted in the Revised Principles, when a majority of the board members are free of the conflicts of interest that can arise from having a personal interest in the financial transactions of the organization, the board as a whole may be more likely to

[4] The term, "material financial interest," not "material financial benefits," is used in Treas. Reg. 53.4958-6(c)(iii). However, the term is not defined, and the only other place the term appears in the Intermediate Sanctions Regulations is § 53.4958-3, which defines a disqualified person. There, the term is used in § 53.4958-3(g), Examples 10 and 11, in reference to "material financial interest" in a "provider-sponsored organization (as defined in section 1855(e) of the Social Security Act [42 U.S.C. § 1395w-25(d)]])." The term also appears in § 501(o) of the Code, again in reference to "provider-sponsored organization (as defined in section 1855(e) of the Social Security Act)." However, neither the regulations under the Social Security Act nor § 501(o) of the Code define the term "material financial interest." The Social Security Act, however, does define a "provider sponsored organization" as, *inter alia*, one "with respect to which the affiliated providers share, directly or indirectly, substantial financial risk with the respect to provision of [the contracted] items and services and have ***at least a majority financial interest in the entity***." 42 U.S.C. § 1395w-25(d)(1)(C) (emphasis added).

exercise its responsibility to review and take action on materials and information independent of the staff and management.[5]

**No Current Substantive Law Requirement for Majority Independence**

We endorse the general approach taken in the definition of independence set forth in the Glossary and the approach taken in the Revised Principles. We note, however, that under current law, there is no substantive law requirement that any particular percentage of a governing board be made up of independent board members.[6] Even the majority of independent members required under the community board criterion of Revenue Ruling 69-545,[7] which applies only to health care organizations, is only one factor (though an important factor) that is part of a larger facts-and-circumstances test and is not an absolute requirement for tax-exempt status.[8]

**Form 990 Glossary Does Not Impose a Substantive Law Requirement**

Therefore, as we understand it, the definition of independence in the Glossary has no substantive law impact. In that regard, we believe it would be confusing and misleading, and, therefore, contrary to the IRS's transparency goal, to require organizations to provide information about the percentage of independent board members without making it clear that this is a transparency function only, not a substantive law requirement.

Furthermore, it is not clear whether the definition of independence is one of the areas contemplated by Item 7 of the joint Department of Treasury/Internal Revenue Service Priority Guidance Plan for 2007-2008 regarding regulations that will be needed to implement the Redesigned Form 990. As a result, until such time as the IRS both adopts a substantive definition of independence and mandates a specific percentage of independent directors via regulation (following the required notice and comment period under the Administrative Procedures Act), we believe that the definition in the Glossary should make clear that independence is not a substantive law requirement.

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[5] Revised Principles at p. 14.

[6] The closest provision of the Code or Regulations requiring specific board composition is found in Treas. Reg. § 1.170A-9(e)(3)(v), defining a § 170(b)(1)(A)(vi) organization under the 10% facts and circumstances test. This regulation provides that a "representative governing body" that "represents the broad interests of the public, rather than the personal or private interests of a limited number of donors . . . will be taken into account in determining whether an organization is 'publicly supported.'"

[7] 1969-2 C.B. 117.

[8] St. David's Health Care System v. United States, 349 F.3d 232, 236 (5th Cir. 2003), footnote 4; IHC Health Plans, Inc. v. Commissioner, 91 AFTR 2d 2003-1767, 2003-1776 – 2003-1777, 325 F.3d 1188 (10th Cir. 2003).

**Definition of Materiality – "Close and Continuous Connection Standard"**

In addition, we believe that a key component of the foregoing definition, that of "material financial benefit," needs to be clarified. We urge that the Glossary definition be expanded to include a discussion of what constitutes a "material benefit" and/or that any future regulation project address this issue as well. In that regard, we endorse the approach to materiality taken by the IRS in its FY 1997 Continuing Professional Education Text article, "Tax-Exempt Health Care Organizations Community Board and Conflicts of Interest Policy," by Lawrence M. Brauer and Charles F. Kaiser (the "1997 CPE Text").

In the 1997 CPE Text, Messrs. Brauer and Kaiser note that practicing physicians affiliated with the hospital, officers, department heads, and other employees of the hospital are not independent "due to their close and continuing connection with the hospital." On the other hand, other persons, who may have some business dealings with the hospital, but who do not, as a result, have a "close and continuing connection with the hospital" are usually considered to be independent.[9] We believe that this "close and continuous connection" standard should be the cornerstone of determining what constitutes a material financial benefit.

**Materiality is a Facts-and Circumstances Analysis**

In that regard, we believe that determining what is material is necessarily a facts and circumstances analysis because what is material will vary from organization to organization, from board member to board member, and even with the same board and the same institution, the relationship may change over time as circumstances of the institution and the board member change. From the institution's perspective, the ultimate goal should be to draw a "materiality" line at the place where, given the facts and circumstances of the institution in question and the board member's economic relationship with the institution, a person could reasonably conclude that a board member is more likely than not to (or at least reasonably likely to) be inclined to "go along" or otherwise not challenge management in order to preserve a revenue stream or other economic benefit that the director, a member of the director's family or 35%-controlled entity,[10] directly or indirectly, receives from the institution.

**Role of the Board in Determining Materiality**

In any effort to define a materiality standard for board independence and its application, we recommend that the IRS adopt the approach taken in the Proposed Regulations on exempt

[9] 1997 CPE Text p.p. 18-19.

[10] We suggest using the definitions of "family" and "35%-controlled entity" found in IRC § 4958(f)(4) and (f)(3) and in Treas. Reg. § 53-4958-3(b)(1) and (b)(2).

status released by the IRS on September 8, 2005.[11] The Proposed Regulations set forth a series of five factors, followed by a series of examples indicating how the factors should be applied in different facts and circumstances. As those factors are applied in each of the examples in the Proposed Regulations, the IRS made clear that there was a direct connection between responsible corporate governance and compliance practices and continued tax exemption. This approach is similar to the one followed by the IRS in various Revenue Rulings in the health care industry, most notably the physician recruitment revenue ruling.[12] In that ruling too there is a significant emphasis on board oversight in the multiple favorable examples – oversight which is a hallmark of good governance processes. In effect, both the Proposed Regulations and Rev. Rul. 97-21 recognize the importance of board oversight and an unstated deference to the reasonable business judgment of nonprofit boards. That reliance is particularly justified where the board has adopted a substantial conflicts of interest policy (discussed below).

**IRS Deference To Reasonable Business Judgment of the Board on Materiality**

We believe that same approach of general rules illustrated by multiple, detailed examples will work well in assessing independent of board members and the materiality of their economic relationships with the organizations they serve. However that approach is implemented, whether through expansion of the Glossary, in new Regulations, or other form of guidance such as a Revenue Ruling, we believe the IRS needs to endorse the "close and continuing connection" standard from the 1997 CPE Text as the general rule or "benchmark" for materiality, to illustrate the operation of that standard though a series of detailed examples, to require boards to adopt policies that define independence for their board members consistent with that definition of materiality, and to require that those standards be reviewed periodically by the board (similar to the review of overall activities already contemplated in the IRS model conflicts of interest policy referenced below). Moreover, we urge that any final guidance in this area indicate that, in general, the IRS will defer to a board's business judgment on materiality where the board has, in good faith, exercised ordinary business care and prudence in following the process and standards set forth in the guidance regarding board member independence in general and materiality in particular.

[11] 70 Fed. Reg. 53599-53604 (Sept. 9, 2005). The Proposed Regulations describe the standards that the IRS will use to determine whether to revoke the § 501(c)(3) status of an organization that has engaged in a transaction that constitutes both (i) traditional private inurement under IRC § 501(c)(3), and (ii) an excess benefit transaction under the intermediate sanctions rules of IRC § 4958.

[12] Rev. Rul. 97-21, 1997-1 C.B. 121.

**Scope of "Conflict of Interest" for Form 990 Reporting Purposes.**

**Benefits of a Conflict of Interest Policy**

While "independence" is an overall, entity level concept, "conflict of interest" is a transactional concept. That is, even an individual who is "independent" on an overall relationship basis may from time to time have a "conflict of interest" with respect to a particular transaction. There is nothing illegal or unethical about having a conflict of interest. Everyone at some time can find himself or herself in a conflict of interest position. The important issue is not whether a conflict exists but how the individual and the institution deal with conflicts and potential conflicts. In that regard, we agree with Messrs. Brauer and Kaiser's assessment in the 1997 CPE Text that the role of a conflict of interest policy is to " . . . protect the exempt organization's interest in transactions or arrangements that may also benefit an officer's or director's private interest."[13]

**Glossary's Definition of a Conflict of Policy Interest for Tax Purposes**

The definition of "Conflict of Interest Policy" in the Glossary is based on the definition of that term set forth by the Panel on the Nonprofit Sector in Strengthening Transparency, Governance, Accountability of Charitable Organizations: A Final Report to Congress (June 2005) (the "Final Report").[14] In relevant part, the Final Report states that "A conflict of interest policy helps protect the organization by defining conflict of interest, identifying the classes of individuals within the organization covered by the policy, facilitating disclosure of information that may help identify conflicts of interest, and specifying procedures to be followed in managing conflicts of interest." Consistent with the Final Report, the first sentence of the Glossary's definition of a Conflict of Interest Policy, provides that a Conflict of Interest Policy is "A policy that defines conflict of interest, identifies the classes of individuals within the organization covered by the policy, facilitates disclosure of information that may help identify conflicts of interest, and specifies procedures to be followed in managing conflicts of interest."[15]

The Panel's position is consistent with the view articulated by Messrs. Brauer and Kaiser in the 1997 CPE Text, and we endorse the Panel's position that each organization should have a conflict of interest policy to ensure that all members of its governing body are aware of their duty of loyalty and take reasonable steps to ensure that the board conducts its affairs subject to

[13] The 1997 CPE Text goes on to state: "The primary benefit of a conflicts of interest policy is that the board can make decisions in an objective manner without undue influence by persons with a private interest. The presence and enforcement of a conflicts of interest policy can also help assure that an exempt health care organization fulfills its charitable purposes, properly oversees the activities of its directors and principal officers, and pays no more than reasonable compensation to physicians and other highly compensated employees." 1997 CPE Text at pp. 18-19.

[14] Final Report at p. 93. The final Report is available online at http://www.nonprofitpanel.org/final/.

[15] Glossary definition of Conflict of interest Policy, first sentence.

the terms and conditions of a "substantial" conflicts of interest policy. In that regard, many exempt organizations have adopted a "substantial" conflict of interest policy for their boards based on the IRS Sample Policy prescribed for tax-exempt health care organizations in the 1997 CPE Text and now included as an Appendix for potential use by organizations filing Form 1023.

**Glossary's Definition of a Conflict of Interest**

While the first sentence of the Glossary definition captures, correctly we think, the proper role for a conflicts policy within an exempt organization, we think the second sentence, which defines the term, "conflict of interest," is too broad. According to the Glossary, "A ***conflict of interest*** arises when a person [who[16]] is in a position of authority over an organization, such as an officer, director or manager, ***may benefit personally*** from a decision he or she could make." (Emphasis added.)

As the emphasized language indicates, the Glossary definition extends to all transactions in which a fiduciary "may benefit personally," whether in an economic sense or in a non-economic sense. On the other hand, as we understand it, the tax law principles relevant to conflicts of interest for exempt organizations involve private inurement under IRC § 501(c)(3) and economic benefit under IRC § 4958. In that regard, we note that these tax law concepts involve financial conflicts only, not those related to non-financial benefits. Consistent with that limitation, the IRS Sample Conflicts Policy and the Intermediate Sanctions Regulations address financial conflicts only.[17]

As a result, we believe that the definition in the Glossary is beyond the scope of the IRS Sample Policy and beyond the scope of the conflicts addressed under either IRC § 501(c)(3) or IRC § 4958. Therefore, we would recommend that the second sentence in the Glossary definition of a "Conflict of Interest Policy" be changed to read as follows: "A conflict of interest arises when a person who is in a position of authority over an organization (such as an officer, director or manager), or such person's family members or 35% controlled entities (as defined in the regulations under Section 4958), may derive a personal economic benefit from a decision he or she could make in that position."

**Summary and Conclusions**

As noted above, we appreciate the time and effort that the IRS has invested in developing the Discussion Draft, and we believe that it will further transparency and accountability among

[16] On a technical note, we assume the omission of "who" in the actual text of the Glossary was a typographical error.

[17] See Definition of "Interested Person" and "Financial Interest" in Article II of the IRS Sample Conflicts of Interest Policy and see Treas. Reg. § 53.4958-6(c)(iii) under the Intermediate Sanctions Regulations.

exempt organizations. In finalizing the Discussion Draft, we respectfully request that you take into account our comments that:

- The Glossary and/or Instructions to the Redesigned Form 990 should make clear that there is no substantive law requirement for any particular percentage of independent directors;

- The Glossary definition and/or Instructions to the Redesigned Form 990 should be expanded to give guidance as to what constitutes a "material benefit" and/or that any future IRS guidance address this issue as well;

- That "materiality" should be judged by the "close and continuous connection" standard set forth in the 1997 CPE Text;

- That independence of board members should be assessed by applying general rules, illustrated with multiple, detailed examples, and that the IRS defer to the business judgment of a board as to what is a "material interest" for that board in cases where the board has in good faith, and exercising ordinary care and business prudence, established reasonable materiality standards for that board; and

- That the definition of "conflict of interest" for exempt organizations be limited to financial conflicts of interest and not extend to non-financial conflicts.

If you have any questions regarding these comments, please contact us at the numbers listed below.

Very truly yours,

James R. King
614-281-3928

Gerald M. Griffith
312-269-1507

cc: Ronald J. Schultz, JD, Senior Technical Advisor to the Commissioner of TE/GE
Theresa Pattara, JD, CPA, IRS Project Manager for Form 990 Redesign

**From:** Markezin, Ernest
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**CC:** "dlifson"; "sfierstein"; "Edward Torres"; "Schoenfeld, Susan"; "Paul Hammerschmidt"; mcanto; "sonja. lepkowski"; Grumet, Louis;
**Subject:** NYSSCPA Comments on IRS Draft of a Redesigned Form 990
**Date:** Friday, September 14, 2007 9:31:00 AM
**Attachments:** NYSSCPA Comments on Proposed Form 990 final 07.09.14. pdf

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To: Form 990 Redesign, ATTN: SE:T:EO

Please find attached the New York State Society of CPAs comments on the discussion draft of a redesigned Form 990, *Return of Organization Exempt from Income.*

If you have any problems in opening the attachment, please contact me at 212-719-8303.

Sincerely,
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September 14, 2007

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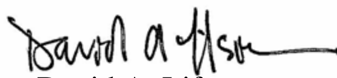
By e-mail: ______________________

**Re: IR-2007-117 – Redesigned Draft Form 990**

The New York State Society of Certified Public Accountants, representing 30,000 CPAs in public practice, industry, government and education, submits the following comments to you regarding the above captioned release. NYSSCPA thanks the Internal Revenue Service for the opportunity to comment on this release.

The NYSSCPA Exempt Organizations Committee deliberated the draft Form 990 for tax-exempt organizations and prepared the attached comments. If you would like additional discussion with the committee, please contact Paul E. Hammerschmidt, chair of the Exempt Organizations Committee, at (212) 885-8321, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,



David A. Lifson
President

Attachment

new york state society of
NYSSCPA
certified public accountants

Home of the Trusted Professional
3 park avenue, at 34th street, new york, ny 10016-5991
212.719.8300 • fax 212.719.3364
www.nysscpa.org

# COMMENTS ON IR-2007-117 – REDESIGNED DRAFT FORM 990

# FOR TAX-EXEMPT ORGANIZATIONS

**September 14, 2007**

<u>**Principal Drafters**</u>

**Martin S. Cantor**
**Sonja Lepkowski**
**Paul E. Hammerschmidt**

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**NEW YORK STATE SOCIETY OF**
**CERTIFIED PUBLIC ACCOUNTANTS**

**EXEMPT ORGANIZATIONS COMMITTEE**

**COMMENTS ON IR-2007-117**

**Redesigned Draft Form 990 for Tax-Exempt Organizations**

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## GENERAL COMMENTS

CPAs working with nonprofit clients bring a unique perspective on financial reporting by nonprofit organizations that has evolved from our historic roles of preparing or reviewing their information returns and tax returns, auditing their financial statements, and advising on their operations.

The IRS has recently made a bold revision of the form, the first since 1979. The goal is to implement these changes for the 2008 form, that is, in January 2009 for the 2009 filing season.

While we have found that much of the redesigned Form 990 is a welcome improvement over the old form, we have some general concerns as well as some specific suggestions for improvement. It is our hope that the revised Form 990 will provide the IRS, state charity officials and the public with a more realistic picture of organizations and will more accurately reflect their operations.

In several instances, we recommend that the threshold requirement be raised in connection with Form 990-EZ filers as well as for reporting separate schedules. We make these recommendations with consideration of the three guiding principles of the redesign of Form 990: (1) enhancing transparency, (2) promoting tax compliance, and (3) minimizing the burden on the filing organization.

## SPECIFIC COMMENTS AND RECOMMENDATIONS FOR IMPROVEMENT

### Continuance of Group Returns

The IRS indicated in the "Phone Forum" held on July 18 and 19, 2007, that it is considering the elimination of group returns for several reasons including a "lack of transparency" as well as a process that is "administratively burdensome." This is consistent with the elimination of boxes H and I on page 1 of the current Form 990.

In the interest of transparency and reducing the administrative burdens on the IRS and many organizations, we recommend that group returns, currently permitted under Reg. 1.6033-2(d)(2)(i), continue to be allowed.

The relationship that is required for a central organization to obtain a group ruling to include its subordinates, which are subject to the central organization's general supervision or control, insures that the group return will provide transparency and be a meaningful report of operations of the subordinates. Group returns often include local chapters of a larger organization. Sometimes these chapters are unsophisticated and do not have the resources to provide accurate and detailed financial information, and they rely on the central organization for proper reporting to the IRS. The administrative burden on both the IRS and these organizations would be increased siginificantly by requiring each chapter to prepare and file returns on their own, and having the IRS process them.

**State Filings**

Many states require the attachment of audited, reviewed or compiled financial statements to Form 990 as part of the organization's state filings, and these financial statements may only be available electronically in the protected ".pdf" format. There is a need for the redesigned Form 990 to accommodate attachments in ".pdf" format as well as explanations and other notes.

**Comments on Glossary**

The definition of "audit of financial statement" does not agree with the professional literature, and should be changed to the following sentence from Section AU 110.01 of the U.S. Auditing Standards chapter of AICPA *Professional Standards*:

> "The objective of the ordinary audit of financial statements by the independent auditor is the expression of an opinion on the fairness with which they present, in all material respects, financial position, results of operations, and its cash flows in conformity with generally accepted accounting principles."

The definition of a "compilation" does not agree with the professional literature, and should be changed to the following sentence from Section AR 100.04 of the Accounting and Review chapter of AICPA *Professional Standards*:

> "Presenting in the form of financial statements information that is the representation of management (owners) without undertaking to express any assurance on the statements."

The definition of a "review of financial statement" does not agree with the professional literature, and should be changed to the following sentence from Section AR 100.04 of the Accounting and Review chapter of AICPA *Professional Standards*:

"Performing inquiry and analytical procedures that provide the accountant with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the statements for them to be in conformity with GAAP [generally accepted accounting principles] or, if applicable with another comprehensive basis of accounting (OCBOA)."

## CORE FORM

### Part I – Summary

Form 990 Instructions do not provide program service activity codes. Rather, they refer the preparer to the Form 990-T Instructions. We suggest that program activity codes also be provided in Form 990 Instructions.

We suggest that percentages, ratios and other statistical information not be deemed automatic "red flags" (with IRS establishing minimums or maximums for inquiries). We suggest that Form 990, as redesigned, allow room for organizations to provide a narrative to assist the reader to understand the financial information reported.

### Part III – Statements Regarding Governance, Management, and Financial Reporting

We agree that tax-exempt organizations should maintain strong governance standards. However, the revision added sections concerning governance even though the IRS currently has no statutory authority to regulate the governance of exempt organizations (including mandating best practices such as "Voluntary Best Practices" for U.S.-Based Charities[1] and "Sarbanes-Oxley" provisions). These governance areas include the following parts of the redesigned Form 990:

(1) Percentage of board members who are independent
(2) Relationships of board members, officers and key employees (page 3 of the core form)
(3) Written conflict of interest policy (and its availability to the public) and number of related transactions reviewed, written "whistleblower" policy, written document retention and destruction policies, and written policy safeguarding exempt status concerning transactions and arrangements with related organizations
(4) Financial statements and independent accountant's compilation, review or audit services, along with the availability to the public of financial statements and audit reports

[1] U.S. Department of The Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities

(5) Review of Form 990 by the organization's governing body before it is filed.

We suggest that the IRS indicate to the public the purpose of this new section and whether particular responses to these matters are indicators of inquiry or examination. We recommend that the IRS expand its outreach efforts to increase the quality of governance maintained by exempt organizations.

In addition, we suggest that the IRS include a statement on Form 990, Part III, indicating that compliance with these governance standards is not mandatory. Rather, they are recommended to achieve good governance that is part of the process of decision-making and the process by which decisions are implemented (or not implemented).

**Part VII – Statements Regarding General Activities**

Line 8a – We recommend that additional guidance of "conduct all or a substantial part of its exempt activities through or using a partnership, LLC or corporation" be provided that would assist the preparer to properly respond to this question.

**Part IX – Statement of Program Service Accomplishments**

The addition of Line 3 to Part IX will require organizations to report their program service revenue in two different ways on the core form: by source (but excluding government grants) in Line 2 of Part IV and by activity in Line 3 of Part IX. The instructions to the core form should include a worksheet (that is not included in the return) that reconciles the program service revenue reported in these two parts.

The IRS is proposing to require organizations to report direct revenue (*i.e.*, program service revenue; not contributions) for programs along with the related program service expenses (required for 501(c)(3) and (4) organizations and 4947(a)(1) trusts; optional for others) in part IX. The instructions do not provide adequate guidance, and it is not clear how direct revenue reported here would reconcile with program service revenue reported on Part IV, Line 2.

Organizations may not report amounts of direct revenue (by program) in their financial statements and these amounts may not be easily calculated. Further, disclosure of amounts of direct revenue would marginally enhance transparency and promote tax compliance while adding to the burden on the filing organization. Charitable organizations often provide a benefit or service to a charitable class in fulfillment of their exempt purpose. Programs are typically funded from a combination of different revenue streams including government grants and program service revenue. For these reasons, we recommend that IRS eliminate the requirement to report direct revenue associated with program services.

## SPECIALIZED SCHEDULES

### Schedule A – Supplementary Information for Organizations Exempt Under Section 501(c)(3)

Line 11f – This question asks whether the organization has a written determination from the IRS that it is a Type I, Type II or Type III supporting organization. We recommend that the IRS suspend the request for written determination of the Type I, II or III status of supporting organizations until the IRS establishes a procedure to enable Section 501(c)(3) organizations (that already have determination letters that did not list their type of supporting organization) to receive such Type I, II, or III determinations.

Part II – We are pleased to see that the IRS has eliminated the need to require most publicly supported organizations described in IRC §§ 509(a)(1) and 170(b)(1)(A)(vi) (*i.e.*, organizations preparing Form 990 under the accrual method of accounting, required under generally accepted accounting procedures, often referred to as donative public charities) to convert various revenue amounts from the accrual method of accounting to the cash method of accounting for purposes of the support schedule. The IRS should seriously consider using the information provided in this schedule in lieu of the current requirement of organizations having to complete and file Form 8734 within 90 days after the end of their advance ruling period in order to obtain their definitive ruling. To effectuate this change, the Treasury Department would need to modify the requirements of Reg. § 1.170A-9(e)(5).

Part III – We believe that the requirement to use the cash method of accounting should be eliminated for supported organizations described in IRC § 509(a)(2) (often referred to as service provider entities), similar to donative public charities described above. Once again, the IRS should seriously consider using the information provided in this schedule in lieu of the current requirement of organizations having to complete and file Form 8734 within 90 days after the end of their advance-ruling period in order to obtain their definitive ruling. To effect this change, the Treasury Department would need to modify the requirements of Reg. § 1.509(a)-3(d).

### Schedule C – Political Campaign and Lobbying Activities

We suggest that further consideration be given to the need and the benefits expected to be derived from Part I-A as organizations that conduct direct and indirect political campaign activities will likely face difficulties in accumulating the number of volunteer hours to report in Part I-A.

**Schedule D – Supplemental Financial Statements**

Part VI – There appears to be a typographical error in the heading. It most likely should read, "…for assets not reportable on lines 1-15 (Form 990, Part VI, Line 16)."

Because the amount of support and contribution revenue for many organizations can vary widely from year to year or may not cover an organization's financial needs, many organizations rely on endowment investments to supplement their other sources of cash for either short or long periods. Readers should appreciate the reporting of the accumulation of assets in endowment funds as a requirement of the donor (*e.g.*, restricted contributions) or as responsible financial planning. In addition, the size of an organization's endowment fund in relation to its overall expenditures should also be evaluated in terms of each organization's own reasonably anticipated future needs. For example, an organization may have a multi-year capital campaign that may not be reported in the financial information but may be described by the organization in a narrative.

We suggest that a comment section be provided to Schedule D, Part XII, "Endowment Funds," as well as to Schedule M, Line 29 (property held for the three years from the date of initial contribution) to provide an opportunity for organizations to furnish explanations of their reasonably anticipated future needs and their policies and practices.

**Schedule F – Statement of Activities Outside the U.S. and Schedule I – Supplemental Information on Grants and Other Assistance to Organizations, Governments and Individuals in the U.S.**

Grants made to domestic organizations, when a majority of their activities are either in foreign countries or primarily benefit people in foreign countries, would be reported as foreign grants on Schedule F. Currently, makers of grants to domestic organization grantees having a majority of their activities either in foreign countries or primarily benefiting people in foreign countries rely on their American public charity status, and do not perform the additional grant recipient selection or monitoring procedures that they would do for foreign organizations doing the same humanitarian work. We suggest that the IRS require these organizations to advise their contributors of the foreign grant status in the contribution acknowledgement letters, and provide a transition period for the grant-making organizations to accumulate this information prior to requiring this disclosure on the new Form 990.

Schedule F, Part I, Line 2, requires makers of foreign grants to have formal procedures for selecting grant recipients and monitoring the use of grant funds. Many grant-making organizations with a small staff that make separate grants in excess of $5,000 to U.S. public charities conducting their activities abroad rely on the recipient US public charities to select the programs abroad to be financed and to monitor those programs' effectiveness. A provision should be made to exempt U.S. grant-making organizations

that rely on these recipient U.S. public charities for the selection and monitoring functions from having to complete Line 2 of Part 1 of Schedule F.

**Schedule G – Supplemental Information Regarding Fundraising Activities**

Reporting requirements have been expanded from the current (2006) Form 990, Line 9 (including the required schedule listing the two largest fundraising events and an aggregate reporting of other events as measured by gross receipts).

IRS Instructions regarding who must file Schedule G do not appear to be consistent with Part IV, Line 11 that indicates, "Attach schedule G if 'total' exceeds $10,000." It appears, from the instructions, that the IRS is referring to Part IV, Line 11a. If so, we suggest that the word "total" be replaced with "Line 11a." In addition, there is an inconsistency in the guidance of Part IV, Line 11a, that indicates that Schedule G is required when the total "*exceeds $10,000*," while the Schedule G instructions indicate that the schedule is required when Part IV, Line 11a, is "*$10,000 or more*." We recommend that the threshold be consistent between the guidance and the instructions and suggest using *"$10,000 or more."*

There is an additional inconsistency in guidance of Part V, Line 11e, that indicates that Schedule G is required when the total "*exceeds $10,000*," while the Schedule G instructions indicate that the schedule is required when Part IV, Line 11a, is "*$10,000 or more*." Again, we recommend that the threshold be consistent and we suggest *"$10,000 or more."*

**Schedule I – Supplemental Information on Grants and Other Assistance to Organizations, Governments and Individuals in the U.S.**

We support the requirement to furnish employer identification numbers, however we suggest a delay or transition period for implementation to allow U.S. grant-making organizations time to accumulate the employer identification numbers of domestic and foreign grantees in Schedules F and I.

**Schedule M – Non-Cash Contributions**

Schedule B, "Schedule of Contributions," has not been revised. Schedule M (to provide details for non-cash contributions) will be burdensome for organizations to prepare. Schedule B reports both cash and/or non-cash contributions of $5,000 or more (unless special rules apply) while Schedule M reports non-cash contributions in excess of $5,000. We recommend that the threshold be consistent between these two schedules.

**CONCLUSION**

The redesigned Draft Form 990 is a significant enhancement in the objectives of improving transparency and promoting tax compliance. We support attaining these goals as long as the cost is reasonable and in line with the benefits that the IRS seeks to attain.

We believe professional fees in connection with the preparation of the revised Form 990 are likely to increase significantly. Also, organizations that prepare Form 990 in-house are likely to experience additional and considerable administrative burdens to gather, process and report the additional information required to file the new Form 990.

Under current provisions, for tax periods beginning after December 31, 2006, small tax-exempt organizations whose gross receipts are normally $25,000 or less may be required to file an annual electronic notice, Form 990-N, “Electronic Notice” (e-Postcard). We believe that this filing threshold is appropriate.

Under current provisions, Form 990-EZ is available for organizations (other than supporting organizations) whose gross receipts during the year are less than $100,000 and total assets at the end of the year are less than $250,000. Recognizing the additional burden of having to gather, process and report information, as well as the third key principle to reduce the filing burden, we recommend that the gross receipts threshold be increased to $200,000, and that the current asset level of $250,000 be retained.

A cost/benefit analysis should be made that considers the balance between the enhanced information made available to the public and the significantly increased costs to exempt organizations as they pursue their missions and goals.

**From:** Lynda S. Ramirez-Blust
**To:** *TE/GE-EO-F990-Revision;
**CC:**
**Subject:** Revised IRS Form 990 Comments
**Date:** Friday, September 14, 2007 11:07:18 AM
**Attachments:** IRS Form 990 Comments.pdf

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Lynda S. Ramirez-Blust
LSRB Consulting LLC
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Arlington, VA 22205
O:  703-465-4999
C:  414-793-6622
Email:

**LSRB Consulting LLC**
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September 12, 2007

Form 990 Redesign
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Washington, DC 20224

Dear Sir or Madam:

I would like to thank the Exempt Organizations division of the Internal Revenue Service for its efforts in revising the IRS form 990. This is a significant undertaking and the diligence with which it is being executed is applauded. While I understand the technological and budgetary considerations driving the current deadlines, I hope that they do not get in the way of thoughtful consideration for the comments received not only from myself but also from the thousands of others around the country working with and for tax exempt organizations that will be impact by the proposed changes.

In general, I am supportive of the changes being made to the form. I have two primary concerns. My first concern is with the duality of purpose in the IRS Form 990. It is at once supposed to be both a document used by the IRS to fulfill its enforcement responsibilities and a public disclosure document much like those filed by public companies with the SEC. As a result, certain items included in the form while intended to improve disclosures to the public set arbitrary thresholds of appropriateness and perpetuate the use of metrics that are limited at best in communicating the effectiveness and efficiency with which reporting organizations meet their missions.

My second concern has to do with the short timetable for tax exempt organizations to be prepared to comply. It is expected that the new form will be required for tax year ending 2008. That means that at the beginning of the tax year, tax exempt organizations have to have the systems and processes in place to capture all of the information necessary to prepare the IRS Form 990. Some organizations will have only a year between the time the form is finalized and is required for use to implement in necessary changes in their own accounting and governance systems and processes. Based on my nearly 13 years of experience working with nonprofit organizations this is not enough time.

Following are my specific comments:

- ***Form 990 Core Form Part I, lines 3 and 4 and Part III, lines 1a and 1b.*** These items should be removed from the IRS Form 990. They are not relevant to the enforcement activities of the IRS. While the size and independence of the board is often evaluated to assess the effectiveness of organizational governance, there is no definitive evidential matter that supports an ideal board size or degree of independence. Inclusion of these metrics perpetuates an unfounded expectation that the size of the governing body or the degree of independence of its members is an indicator of effective governance.

- ***Form 990 Core Form Part I, line 6 and Part II, line 2.*** This item should be removed from the IRS Form 990. While it is necessary for the IRS to identify potential instances of excessive compensation, it is not appropriate to establish an arbitrary threshold of $100,000 to determine how many individuals to disclose. In a small organization there may be no one receiving $100,000 and yet there still be an instance of excessive compensation because the compensation represents an excessive percentage of the organization's total revenues. Conversely, there may be many individuals receiving compensation in excess of $100,000 which is warranted given the size of the organization, the nature of its operations, and the skills required of the personnel. The utilization of a threshold creates a de facto limit on compensation which is completely inappropriate.

- ***Form 990 Core Form Part I, line 8b.*** Please clarify the relevance of officer, director, trustee, and other key employee compensation allocated to program expenses as a % of total program expenses. This is not an effective indicator of operational efficiency or effectiveness or good governance.

- ***Form 990 Core Form Part I, lines 11-21.*** While the % of Total calculation is performed by most charity watchdog organizations and are the most commonly used metrics used to evaluate organizational performance, they should not be presented on a summary page without adequate space for the reporting organization to provide additional metrics and explanations to provide a more comprehensive and often more accurate basis for readers to evaluate organizational performance. These calculations should either be removed from Part I or space should be added for additional metrics.

- ***Form 990 Core Form Part I, lines 25-26.*** Please clarify the relevance of presenting gaming and fundraising information in the summary section as opposed to other sources of revenue.

- ***Form 990 Core Form Part II, Section A, line 1A.*** The arbitrary threshold of $100,000 for reporting highly compensated present and past officers, employees, etc. should be removed from the definitions of individuals requiring disclosure. While it is necessary for the IRS to identify potential instances of excessive compensation, it is not appropriate to establish an arbitrary threshold of $100,000 to determine how many individuals to disclose. In a small organization there may be no one receiving $100,000 and yet there still be an instance of excessive compensation because the compensation represents an excessive percentage of the organization's total revenues. Conversely, there may be many individuals receiving compensation in excess of $100,000 which is warranted given the size of the organization, the nature of its operations, and the skills required of the personnel. The utilization of a threshold creates a de facto limit on compensation which is completely inappropriate.

- ***Form 990 Core Form Part II, Section A, line 1A.*** Clarify that former officers, key employees, highest compensated employees, directors or trustees require disclosure only if they received compensation in excess of limits in the period being reported.

- ***Form 990 Core Form Part II, Section A, Column (A).*** Why is the individual's city and state of residence required for disclosure?

- ***Form 990 Core Form Part II, Section B, line 4.*** This item should be removed from the IRS Form 990. While it is necessary for the IRS to identify potential instances of excessive compensation, it is not appropriate to establish an arbitrary threshold of $100,000 for disclosure. The utilization of a threshold creates a de facto limit on compensation which is completely inappropriate.

- ***Form 990 Core Form, Part II, Section B, lines 5a-5f.*** While most nonprofit organizations have conflict of interest policies in place, based on my experience many do not have effective processes in place to capture the information required for disclosure. There may be an unreasonable burden placed on nonprofits trying to comply for the 2008 tax year.

- ***Form 990 Core Form, Part II, Section B, line 6.*** Please clarify why Schedule J is required if a former officer, director, trustee, key employee, or highest compensated employee is listed in Section A. Does Schedule J only have to be completed for the former individual or all individuals?

- ***Form 990 Core Form, Part II, Section B, lines 7-9.*** Does Schedule J only have to be completed for the individual listed in Section A or all individuals?

- ***Form 990 Core Form, Part II, Section B, line 5a-5f.*** This section should be moved and combined with Part III, lines 3a and 3b.

- ***Form 990 Core Form, Part III.*** This section should be retained as they encourage improved governance and transparency of nonprofits and this is the only way to establish a national standard at present.

- ***Form 990 Core Form, Part IV and Part I.*** While the breaking out of selected revenue and expense line items is appropriate, organizations may not have adequate time or resources to implement changes to their accounting systems to effectively capture and report this information for the 2008 tax year.

- ***Form 990 Schedule G.*** I think far more than the estimated 25% of nonprofits will need to prepare this schedule.

Respectfully submitted,
Lynda S. Ramirez-Blust
Owner

**From:** JWilson
**To:** *TE/GE-EO-F990-Revision;
**CC:** jwright; lharris;
JMcDowell;
**Subject:** Comments Regarding Proposed Form 990
**Date:** Friday, September 14, 2007 11:34:18 AM
**Attachments:** Comments on Proposed Form 9900000.pdf

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Please find attached, a letter containing our comments regarding the
proposed form 990.

(See attached file: Comments on Proposed Form 9900000.pdf)

R. Jeremy Wilson

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Albany, Georgia 31702

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***********************
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Draffin & Tucker, LLP
CERTIFIED PUBLIC ACCOUNTANTS

September 14, 2007

Mr. Ronald J. Schultz
Senior Technical Advisor
Tax-Exempt and Government Entities
Internal Revenue Service
Form 990 Redesign, SE:T:EO
1111 Constitution Avenue, NW
Washington, D.C. 20224-0002

Dear Mr. Schultz:

We address you as a public accounting firm, whose practice includes a significant niche in the healthcare market, including a considerable number of not-for-profit hospitals. Our firm is very familiar with all aspects of reporting for such entities, including Medicaid and Medicare reporting, audits of financial statements, and tax reporting. Accordingly, our perspective is focused on the reporting requirements of the hospital community, particularly on Schedule H.

Having extensively reviewed the proposed revisions for the Form 990, several items have been brought to our attention. In an effort to relay these items to you and your committee, we have prepared the following letter.

To begin, the stated goal of these changes is to provide greater transparency. There is obviously a significant portion of this goal that includes transparency of operations to the community. However, whether intentional or otherwise, an apparent perception is that these changes will allow for comparability between proprietary and not-for-profit hospitals. Based on the current structure of the form, we do not feel that this perception is realized by the resulting form. In fact, it is our opinion that the information provided does not necessarily allow for the comparability between two different hospitals.

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MEMBERS:
THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

THE GEORGIA SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS

The first hurdle that hinders comparability between various hospitals is the degree to which narratives are utilized throughout Schedule H. Narratives, by nature, are very subjective and not quantifiable. To be fair, the committee has added substantial charts and questions requesting quantifiable data. However, we still feel that excessive narrative disclosures exist. An example of such a narrative is Line 13b, which asks the organization to describe its charity care policy. Some parameters are set in the question; however, there is still a substantial opportunity to provide the Service with a voluminous answer of little or no substance. Instead, we would suggest a series of "Yes/No" questions, aimed at discovering the substance of the charity care policy of the organization. Such questions might include asking the organization if it provides free or discounted services to individuals at or below 100% / 150% / 200% / 300% / 400% of the Federal Poverty Level.

The second hurdle we see with respect to comparability among hospitals is that there is not a single, required method for reporting the quantifiable data; that is to say that hospitals may choose how to report certain items. An example of such a choice is the costs of charity care. Under the proposed form, a hospital may report such information either by using the hospital's internal cost accounting method or by using program cost reports and calculating a cost-to-charge ratio. Obviously, the result would be different depending upon which method was used. Furthermore, there is nothing to preclude an organization from switching methods between years. The result is that an organization would not have comparable results from one year to the next. In addition, comparability between providers would also be jeopardized. Our remedy would be that the Service dictates the single method by which a hospital should report the information requested. Furthermore, we feel that appropriate measures should be in place to insure that reporting for a particular entity should be consistent from one year to the next.

Continuing with this idea of consistency and transparency, we would like to discuss the issue of bad debts versus charity care. Financial reporting guidelines allow charity care to be defined by the individual organization. While we appreciate that the definition for charity care is not defined in any part of the hospital reporting universe, it would be helpful for the Service to set some parameters. This goes to the issue of comparability among hospital entities.

Another issue of charity care is that, typically, in order for an individual to qualify for charity care, he or she must provide the hospital with certain information and support. Oftentimes, such support might include a pay stub or a tax return. However, failure to provide such requested information does not relieve the hospital of its duty to provide services to an individual. The result is that the hospital provides the services free-of-charge, but the account does not qualify as charity care, since the patient did not provide the appropriate information. In absence of other alternatives, the account must be classified as a bad debt. This is a very common example of how a hospital can provide charity care and receive no credit for such services. The reality is that a significant component of the patient-related bad debt expense reported by hospitals would be classified as charity care, if the requested information could be obtained.

Accordingly, we feel that Schedule H should include prominent reporting of bad debt expense, particularly the patient-related amount, as part of the community benefit matrix. One alternative that would achieve comparability with taxable entities would be the requirement that the amount reported should be limited to the actual write-offs for the year. We understand that the position of the Service is one of strong opposition against reporting bad debts; however, we ask that you reconsider your position. The result is that you are penalizing the hospitals for not meeting some theoretical benchmark of charity care, but the attainment of that benchmark rests largely on the shoulders of the patients. A hospital may have the most generous charity care policy, but if there is no patient compliance, the hospital would not be able to document charity care for that year, according to the revised 990. Additionally, there is a correlation between the demographics of a patient-base and the level of patient compliance with such charity care policies. Under this revised Form 990, the hospitals in those communities where charity care is needed the most are likely to be penalized to the greatest extent. Again, our suggestion would be that the Service allow hospitals to report their patient bad debt write-offs for the year.

Continuing our discussion of the Community Benefit Report, we believe that the unreimbursed costs from Medicare should be included in the chart. This is another example, like Medicaid, where the hospital may provide services at rates which do not cover the cost of the services. If the Service takes the position that the unreimbursed Medicaid amount is community benefit, then we see no reason that the unreimbursed Medicare amount should not be included, as well.

The "Billing and Collections" matrix is another part of Schedule H about which we have several comments. To begin, the State of Georgia attempted to collect data akin to that of the "Billings and Collections" section via matrix very similar to the one in Part II of Schedule H. The result was that the matrix was eliminated within two years of implementation. The reason for elimination was that the information was too voluminous to effectively be audited. It is our opinion that the proposed "Billings and Collections Chart" will suffer a similar fate. Our concern is that the Service does not appreciate the difficulty in auditing such numbers, and as a result, may abandon any efforts to review this matrix. Accordingly, the reporting organizations would be forced to spend significant hours reporting the requested information, resulting in an ineffective compilation of data which would not provide for meaningful comparability.

Continuing with the "Billings and Collections" matrix, we would also like to discuss the difficulty in completing the chart. The difficulty is that there is not a single location to find all of the requested data. While this issue presents a time burden on the hospital, the greater issue is that it will be nearly impossible for the information requested to correspond correctly. Specifically, the "Gross Charges" on Line 1 and the "Fees Collected" on Line 4 will likely not correlate properly. The reason for the discrepancy, like the issue of charity care reporting, relates to patient responsibility. For example, the initial revenue may be recorded as revenue from an "Insured Patient," since the patient presents an insurance card. However, when the hospital attempts to bill the insurance company, it is discovered that the policy is no longer in effect. At this point, the resulting accounts receivable and any corresponding write-offs or collections would be classified as uninsured. The result would be that the "Gross Charges" would be recorded in Column (e), Insured, while the "Fees Collected" would be reported in Column (f), Uninsured.

As it relates to Line 4, we do not see the reasoning for such a figure to be reported. In several conference calls, the Service has admitted that the amount on Line 4 will not relate to the amount on Line 1, for the same time period. That is to say, that a significant lag can exist between the time an amount is billed and the time when fees are collected. Accordingly, there seems to be no information garnered by including this entry. Accordingly, we feel that this line should be eliminated.

Finally, Part IV, General Information, provides another example of a previously listed issue. That issue relates to the extensive use of narrative disclosures. Question 1 of this section will likely be several pages in length for many reporting entities, and it is unlikely that the Service will gain any additional insight into whether or not an entity meets its exempt purpose. Question 2 relates to how a hospital educates its patients on eligibility for financial assistance. As we previously noted, a charity care policy precludes documented charity care services unless the patients take the necessary steps. Furthermore, while this question includes government sponsored assistance, this question is essentially a repeat of Question 13(b) from Part I. Though the Service may intend for the answers to each of these questions to be different, the reality is that the answers are likely to be the same.

In conclusion, we appreciate the effort put forth by the Service to increase comparability among reporting organizations. Furthermore, we agree that this project was long overdue. From the standpoint of the hospitals, a substantial modification was necessary to provide a true and accurate picture to the Service and to the communities they serve. We believe that this proposed form achieves this goal to some degree. The addition of charts and tables will be of great benefit over the former method of reporting via narratives. However, as previously mentioned, we feel there are still areas to improve this proposed form, and we ask that you consider additional ways to minimize the reporting via narrative disclosures.

Should you have questions on any of these items, do not hesitate to contact either Mr. Linton A. Harris or Mr. R. Jeremy Wilson of our firm.

Sincerely,

DRAFFIN & TUCKER, LLP

**From:** Chip M. Watkins
**To:** *TE/GE-EO-F990-Revision;
**CC:**
**Subject:** Attached Comments
**Date:** Friday, September 14, 2007 12:41:15 PM
**Attachments:** Form 990 Comments.pdf

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Attached are comments on the proposed revision to Form 990.

<<Form 990 Comments.pdf>>

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# COMMENTS ON THE "REDESIGNED" FORM 990

## FORM 990

**Item H** – For clarity, this item (or the instructions) should instruct the EO to add Part IV, lines 1h, 2g, 3-8, 9a, 10a, 11a, 12a, and 13a.

## Part I – SUMMARY

Line 8b – The percentage to be calculated here is meaningless in the absence of other information. By itself, it has no relevance to tax-exempt status, or liability for any tax. A small EO whose employees are mostly officers, directors, or key employees may have a very high percentage, but still be effective. In 25 years of experience, I have never seen this ratio even referred to, let alone analyzed, by any group of state regulators, charity evaluators, or other observers.

**Lines 11-21 – Delete the columns requesting percentage calculations.** These calculations give undue prominence and weight to percentages that bear no correlation to an organization's qualification for exemption, and that bear little relevance to an organization's effectiveness, except when reviewed on a year-to-year basis by the organization, or when compared with other organizations with similar programs, of similar age, and having similar operational operational characteristics. Those Form 990 users who want to calculate the percentages for their own purposes will have the data to do so.

Line 11 – The instruction should refer to "line 1h", not "line 1g".

Line 15 – Delete the reference to line "3". (This is "membership dues".)

Line 24b – This percentage is also meaningless, and should be deleted.

If the IRS believes that more information is required, then it would be more useful to require EOs to report the prior year information in each row. This would give readers a sense of the trends in the organization's finances.

**Lines 25 and 26 should be deleted.** First, the information required by these lines is not "summary information," but details about the financial results of two particular aspects of the EO's activities, fundraising (if any) and gaming (if any). By highlighting this information on page 1 of the "core" Form 990, the information is given undue prominence.

Equally important, many EOs do not engage in any fundraising or gaming, and the fact that either or both of these two prominent lines are blank may lead some readers to believe that the EO has not properly completed Form 990.

Finally, should these lines remain in Form 990, the percentages called for in column (iv) also do not provide any meaningful information about the EO's qualification for exemption or its liability for any other tax, and column (iv) should be deleted.

## PART II – COMPENSATION, ETC.

**Section A, Column (B)** – The sixth column should be titled "Highly compensated employees" instead of "Other".

### Section B

**Line 4** – "Non-qualified deferred compensation" should be defined in the Glossary

**Line 5** requires substantial information that individuals, especially volunteers, may not be willing to provide, or even know (line 5c). Will the form accept the EO's best efforts to acquire and report this information? Otherwise, many individuals may elect not to serve, *e.g.*, as directors, to avoid these disclosure requirements.

**Line 5f** – The space allowed to describe the transaction is too small.

**Line 9** – The reporting EO many not be aware of payments to any individual from a third party.

**Line 10a** – This question will not pick up payments in the form of royalties or rents.

## PART III – GOVERNANCE

**Line 2** – Form 990 currently requires copies of amendments to the articles of incorporation or bylaws, or trust instrument, to be submitted for review. By doing so, the reporting EO generally acquires protection from retroactive revocation if the IRS does not then object to the changes. What effect will not requiring copies have on this retroactive protection?

Neither the form, nor the instructions, nor the Glossary defines "organizing or governing documents." I recommend the following definition:

The "Organizing or Governing Documents" of an organization are:

--In the case of a corporation, its Articles of Incorporation and Bylaws;

--In the case of a trust, the trust agreement and any bylaws or similar documents that have been adopted as internal rules by the trustee(s);

In the case of a limited liability company, its Articles of Organization and Operating Agreement; and

In the case of an unincorporated association, its articles of organization (if any), constitution (if any), and bylaws.

The requirement (in the instructions) to report "any change" in the six items listed in the instructions will result in the IRS receiving a lot of insignificant information. For example, given that all officers and directors are otherwise listed in Part II, why is it necessary to separately report changes in the number of officers or directors?

Are the policies listed in the instructions *necessarily* "governing documents" for purposes of this line? (I would ordinarily assume that only the articles of incorporation and bylaws are "organizing or governing documents.") If so, what other policies are also "governing documents"?

Line 7a – The Glossary should describe "local chapters, branches or affiliates." There are many different kinds of "chapter, branch, or affiliate" relationships, ranging from internal operating centers, to parent-subsidiary, to licensor-licensee.

For example, some national charities have local operations that are merely internal operating centers, all being part of one corporation. Other national charities and associations also have "chapters" that are subsidiaries of the national organization. Still other "chapters" are merely licensees of the "national's" name and trademarks, and share its purposes.

Line 7b – If the "chapters, branches, or affiliates" are internal operating centers, or perhaps effectively subsidiaries of the reporting EO, this question may be appropriate. However, if the "chapter, branch, or affiliate" is a licensee that shares common purposes with the reporting EO, it may be more appropriate to ask about a written affiliation agreement.

What is meant by "ensure"? Even in a group exemption, the central organization is not responsible for the "sins" of its subordinate units.

What is meant by "consistent" with the reporting EO's operations?

Line 10 – In most organizations, the members of the governing body are not competent to review Form 990, and its review would occupy valuable time that would better be spent on more important matters. The IRS would do better to ask if the Form 990 was prepared or reviewed by its auditor, or reviewed by its lawyer, before it was filed.

Line 11 – This question should also list Form 1023 or 1024. The instructions should remind EOs that §6104(d) requires them to make Form 1023 (or 1024) and the last three Forms 990 (and, for §501(c)(3) EOs, Forms 990-T) available for public inspection.

An EO's failure to make its organizing/governing documents, conflict of interest policy, financial statements, and audit report public should not be taken into account in determining whether an examination is warranted.

Again, "Organizing/Governing Documents" should be defined.

Line 12 – Since space is available, it may be desirable to list all states and the District of Columbia, and require the EO to check a box to indicate each state with which a copy of the Form 990 is listed. This would help the programmers, I would think.

## PART IV – STATEMENT OF REVENUE

Lines 1a-1g – The spaces for reporting these amounts should be moved into column A.

Line 1a – The instructions should also refer to contributions from the Combined Federal Campaign.

Line 1g – This line should read, "Attach Schedule M if total exceeds $5,000." (Compare with line 11a, re: Schedule G.)

That having been said, the $5,000 threshold is too low. This should be increased to $25,000.

Line 2c should read "Revenue from program-related investments".

**Line 13d** should be labeled as "All other".

**Line 14** should refer to "line 1h" and line "13c". The instructions should refer to lines "1h" and "2g".

## PART V – STATEMENT OF FUNCTIONAL EXPENSE

**Column (C)** – Line 4 of the instructions should refer to "supervising or conducting program services or fundraising activities."

**Column (D)** – Although the instructions (at the bottom of page 29) cite the Glossary, the Glossary does not define "joint costs" or "SOP 98-2."

**Lines 1-4** – Columns (C) and (D) should be shaded to preclude any reporting in those columns.

## PART VII – STATEMENT REGARDING GENERAL ACTIVITIES

Line 1 – The instructions should clarify that the conduct of or attendance at occasional meetings outside the U.S. do not require filing of Schedule F.

Line 6b – The instructions should describe the "temporary period exceptions."

Line 9 – The instructions should clarify that an EO not described in §170(b)(1)(A)(iii) that operates one or more hospitals outside the United States that are not supported primarily by fees paid by or for patients may answer this question "no," and is not required to file Schedule H.

Line 10 – The instructions should clarify that an EO not described in §170(b)(1)(A)(ii) that operates one or more schools outside the U.S., all of which are not primarily supported by fees paid by or for students, may answer this question "no," and is not required to file Schedule E.

Line 11 – What is an "affiliated organization"? Should this refer to "related organizations"?

Line 13 – Very few EOs will understand the meaning of this question.

**Part VIII – STATEMENTS REGARDING OTHER IRS FILINGS**

Line 5c should read, "If 'yes' to 5c or 5b, complete the table below."

Line 10 – The instructions should describe the requirements for filing Form 1099-MISC and Form 1099-INT in more detail.

Line 13a should ask about dispositions of any personal property (including nonpublicly traded securities) for which it "was required to file" Form 8282. (Compare Line 14.)

It would seem appropriate to add a question inquiring about whether the EO received any vehicles, boats, or airplanes for which it was required to file Form 1098-C, and how many Forms 1098-C it filed.

**Part IX – STATEMENT OF PROGRAM SERVICE ACCOMPLISHMENTS**

Page 47 of the instructions refers the user to "the instructions for Part IV, Line 1, "Donated Services or Facilities." There are no such instructions.

**SCHEDULE A – SUPPLEMENTARY INFORMATION FOR ORGANIZATIONS EXEMPT UNDER SECTION 501(c)(3)**

**The title** should be changed to "Public Charity Status."

**PART II – SUPPORT SCHEDULE, ETC.**

The IRS is to be commended for using Schedule A in lieu of Form 8734.

**Line 5** should refer to "Excess amounts included on line 1…"

## SCHEDULE E – SCHOOLS

The instructions should clarify that an organization that is not required to file Form 990, but that operates a school in the United States, is required to file Form 5578, *Annual Certification of Racial Nondiscrimination for a Private School Exempt from Federal Income Tax.*

The instructions should also clarify that an EO that is not classified under §170(b)(1)(A)(ii), and that operates a school outside the United States that is not primarily supported by fees paid by or for students is not required to file Schedule E.

## SCHEDULE F – STATEMENT OF ACTIVITIES OUTSIDE THE U.S.

**The title** should be changed to "Activities Outside the U.S."

The instructions should clarify that the mere occasional conduct of, or attendance at, meetings outside the U.S. does not require the EO to file Schedule E.

Public disclosure: Many charitable, educational, and religious EOs conduct activities in foreign countries (including, but not limited to, distribution of charitable assistance; provision of medical care, supplies, and equipment; operation of schools; and conduct of religious worship, education, and evangelism) that would be hostile to, and/or attempt to disrupt and suppress, these activities if they knew about them. For this reason, while disclosure of these activities to the IRS is appropriate to enable to IRS to assess the EO's continuing qualification for exemption, etc., the ITS should enable these §501(c)(3) EOs that wish to maintain confidentiality regarding their non-U.S. activities to do so. If necessary, the IRS should support any required amendments to I.R.C. §6104(d), and adopt any required amendments to Treas.Reg. §3.01.6104(d)-1 *et seq.* EOs should not have to conduct their activities in taxable entities to obtain the confidentiality required to successfully conduct these types of activities.

## SCHEDULE H – HOSPITALS

The instructions to Schedule H should clarify that an EO (not described in §170(b)(1)(A)(iii) or (iv) that operates one or more hospitals outside the United States, all of which are not primarily supported by fees paid by or for patients.

## SCHEDULE I – SUPPLEMENTAL INFORMATION ON GRANTS AND OTHER ASSISTANCE TO ORGANIZATIONS, GOVERNMENTS AND INDIVIDUALS IN THE U.S.

**The title should be shortened "Grants and Other Assistance in the U.S.".**

The "to be completed" instruction just below the title should be changed by changing "lines 1 and 2," to "line 1 or 2."

**Question 2a is very confusing:** The multiple uses of "organization" should be changed by referring to "grantee-organization" and "grantor-organization." The instructions are equally unclear.

This question should also exclude reporting of grants to other nonprofit organizations that share common officers, directors, donors, creators, or highly compensated employees with the grantor.

**Part III:** The instructions for the table should refer to "Form 990, Part V, line 2," not line 2, Form 990, Part V."

**Column (a)** does not have sufficient space for the detailed description of the purpose of the grant required by the instructions.

**Column (c)** requires reporting of the "amount of cash grant" even though there might be *multiple* recipients (see column (b)) of the type of grant or assistance being reported. Is this to be the total amount of the kind of assistance under consideration?

**Columns (d), (e), and (f) share the same problem.** They appear to request "singular" information, even though multiple grants may have been made, and multiple methods of valuation (for gifts of different kinds of non-cash grants) might have been used.

## SCHEDULE J – SUPPLEMENTAL COMPENSATION INFORMATION

**The title should be shortened to "Compensation Information."**

The instructions do not give adequate guidance for determining the value of Nontaxable Benefits when one or more plans provide for a defined benefit for a large number of participants, but no part of the premium paid for the benefit can be identified to specific employee.

**Question 3** suggests that payment or reimbursement of first-class airfare, club dues, or use of a personal residence is evidence of some problem in the organization. In fact, many exempt organizations, including both charities and trade associations, do so for proper business purposes, and properly report any taxable compensation resulting from such payments. For example, both businesses and tax-exempt organizations often pay for first-class airfare on transcontinental or international flights, both to enable the traveler to work while on the plane or to enable him or her to be rested and ready to work the next day. The inclusion of this question turns what is an internal policy matter into a topic of public discussion and gossip. **It should be deleted.**

## SCHEDULE L – SUPPLEMENTAL INFORMATION ON LOANS

**The title should be shortened to "Loans."**

The instructions for Part I should clarify that the EO should not report travel and other expense advances made in the ordinary course of business and within 60 days before the end of the year pursuant to an accountable business expense reimbursement arrangement described in Treas. Reg. §1.62-2

## SCHEDULE M – NON-CASH CONTRIBUTIONS

The threshold for filing Schedule M should be increased to $25,000. A $5,000 threshold will require reporting of too many inconsequential and infrequent transactions. For example, a charity might receive one used vehicle a year, worth, e.g., $6,000, and then be required to file Schedule M.

One of the "other" lines should be labeled for "medical equipment."

## SCHEDULE N – LIQUIDATION, ETC.

The "To be completed" phrase under the title should refer to "Line 10," not "Line 11."

The instructions to Schedule N should clarify that it is not required to be filed with respect to asset dispositions made in the ordinary course of the EO's activities.

| | |
|---|---|
| **From:** | michael |
| **To:** | *TE/GE-EO-F990-Revision; |
| **CC:** | mmalamut; mmalamut; |
| **Subject:** | A practitioner"s comments on the draft Form 990 |
| **Date:** | Friday, September 14, 2007 1:06:12 PM |
| **Attachments:** | IRS 990 comments _Malamut_.pdf<br>IRS Governance comments Malamut.pdf |

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Dear Sir or Madam,

Attached, for your consideration, is a letter written in response to the request for comments on the draft re-designed IRS Form 990, together with an attached letter commenting on the draft IRS Good Governance Practices for 501 (c) (3)s.

I am forwarding this letter from several email addresses because of concerns with potential blckage by spamfilters. Hard copy to follow by US Mail.

Thank you for consideration of practitioners' experience in your redesign of the Form 990.

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September 13, 2007

Lois G. Lerner, Director of the Exempt Organizations Division of the IRS
Ronald J. Schultz, Senior Technical Advisor to the Commissioner of TE/GE
Catherine E. Livingston, Deputy Associate Chief Counsel (Exempt Organizations)
Internal Revenue Service
Form 990 Redesign
ATTN: SE:T:EO
1111 Constitution Avenue, NW
Washington, DC 20224

Form990Revision@irs.gov

Re: Comments on Draft Redesigned IRS Form 990 (Core), Part III, Governance

Dear Ms. Lerner, Mr. Schultz, and Ms. Livingston:

The following comments on the Draft Redesigned IRS Form 990 follow up on comments I previously submitted on the IRS Draft Good Governance Practices for 501 (c) (3) Organizations. My previous comments are attached. The comments in this letter are based on the professional experiences of the author of this letter as an attorney and professional parliamentarian working with many nonprofit membership organizations.

The author of this letter serves as a member of the Board of Editors of Massachusetts Lawyers Weekly; Adjunct Professor at Suffolk University Law School; Chair of the Joint Parliamentary Committee of the National Association of Parliamentarians, American Institute of Parliamentarians, and Robert's Rules Association on Comments to the Revised Model Nonprofit Corporations Act; a member of the Opinions Committee of the American Institute of Parliamentarians; Chair of the Task Force on Governance Forms and Practices of the Nonprofit Governance Subcommittee of the Corporate Governance and Nonprofit Corporations Committees of the Business Section of the American Bar Association; Clerk of the American College of Parliamentary Lawyers; and a Commissioner of Trust Funds for the Town of Dedham, Massachusetts. The comments made in this letter are those of the author solely in his personal capacity and do not represent the official positions of any of the above-listed entities.

In the author's practice, the author works with a number of charitable membership organizations, including local, state, and national governing bodies for sports; international governing bodies for twelve-step organizations; private schools; and religious institutions. He also works with a large number of non-charitable nonprofit membership organizations qualified for tax-exempt status as 501 (c) (4), 501 (c) (5), 501 (c) (6), and 501 (c) (7) entities.

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* Admitted to practice in Massachusetts, New York, and the District of Columbia.

The author of this letter applauds the principles of transparency, compliance, and minimizing the filing burden utilized by the drafters to redesign the Form 990. The comments below are arranged under headings indicating which provision of the draft form and its instructions the comments relate to.

*Glossary, Conflict of Interest Policy*

As worded, the definition of conflict of interest policy applies only when an individual "may benefit personally from a decision he or she could make." This definition does not take into account family relations. Another significant concern in the nonprofit sector is dual loyalty situations, where an individual may owe a fiduciary obligation to more than one nonprofit organization. The draft should consider adding, after "may benefit personally," something along the lines of the following: "or may provide a benefit to another entity to which such person may simultaneously owe a fiduciary obligation."

Dual loyalty situations may come up in large membership organizations (superior organizations, also called "central organizations" in Publications 557 and 4573 and Rev. Proc. 80-27, 1980-1 C.B. 677) affiliated with constituent units (subordinate organizations). The details of the relationships within these types of organizations vary tremendously. While somewhat analogous to the relationship between parent and subsidiary corporations, the relationships among affiliated organizations are not identical to the parent-subsidiary relationship and the interests of the subordinate units (which typically are composed of a subset of the members of the superior organization, but may be constituted of members with no direct relationship with the superior organization at all), are not necessarily identical with the larger, superior organization. Many superior affiliated organizations specifically reserve *ex officio* governing body positions or vice presidencies for members of subordinate affiliates, for example a youth vice president of a national sports organization who is also president of the sports organization's youth affiliate. In this case, the governing body member or officer is elected specifically in a representative capacity, which is a knowing choice by the superior organization made in its governing documents. Dual loyalty situations also arise on largely independent, self-perpetuating governing bodies that reserve seats (either explicitly or as a tacit assumption) for representatives of major donor institutions, recipients of services in social service organizations, or other significant stakeholders.

This is not to say that such dual loyalty situations are bad for either organization. There can be important programmatic reasons for dual loyalty situations that support the interlocking and overlapping missions of both organizations. For example, superior affiliate organizations with direct representation of their member constituency affiliates on the governing body value the contributions that can be made by individuals who, among other things, are highly engaged in the work of the group at a grassroots level, have knowledge of current grassroots concerns, can provide leadership at the grassroots level in implementing national policies, and can achieve buy-in to the superior organization's governing body's decisions because the subordinate unit had one of its leaders at the table when the decision was made.

Therefore, if conflict of interest is defined to include dual loyalty situations, the instructions should make it clear that such situations are not inherently troublesome and may often be beneficial for both affiliated entities. The important considerations are transparency (disclosure) and abstention of the relevant fiduciary (director, trustee, officer) from decisionmaking directly affecting the relationship between two entities to which he or she owes fiduciary obligations. Mandatory abstention should not, however, apply in cases of representation by subordinate affiliates on a superior affiliate's governing body when a decision by a superior affiliated organization affects several subordinate affiliates at the same time or affects affiliates generally. Conflict of interest policies considering the possibility of dual loyalty should also require regular annual updating by fiduciaries of their commitment to the policy, including disclosure of all other entities to which the individual owes fiduciary obligations.

*Glossary, Independent Member of Governing Body*

Under the definition in the current draft, ordinary members of a membership organization might arguably be considered "inside" directors, because they often receive some benefits for their memberships, which could arguably be considered material financial benefits, yet they are typically not members of a charitable class served by the organization, a term that arguably only applies to the indigent.

For example, the parents of a child basketball player may be members of the league in which their child plays. The opportunity to play in the league, particularly if it is a highly competitive league likely to receive attention by college scouts, is arguably a substantial material benefit. It is certainly a benefit that many individuals would readily pay a sum in excess of the league dues to obtain for their children. Nevertheless, the parents of a child in the league are not likely to be indigent. As another example, in some religious congregations, pews are property owned by individual members, and received by virtue of joining the congregation. Similarly, a professional association may grant accreditation that has substantial value professionally.

Nevertheless, the benefits for the members, although arguably material, are shared with and disbursed among a large group of other similarly situated individuals, none of whom should be considered "insiders." If members generally, or a class or group of members, obtains material benefits from membership or opportunities open to the entire membership or a significant group of members, the principle as drafted would have the perverse effect of requiring such organizations to be governed by governing bodies composed primarily of non-members, individuals with little interest in the goals, purposes, and mission of the organization. In volunteer-run nonprofits organized on a membership-basis, it is often difficult to find individuals who are not members who are interested in volunteering, or who should have to resign their membership in order to become "independent" directors.

Receipt of the ordinary benefits of membership in an organization should not make an individual an "insider." For this reason, the third clause of the definition should add a reference to membership organizations along these lines: "who do not receive, directly or indirectly, material financial benefits from the organization except as a member of the organization, a member of a class, group, or constituent unit of the organization, or as a member of a charitable class served by the organization."

*Glossary, Related Organization*

The glossary definition of "related organization," does not appear to include organizations related as affiliated superior and subordinate organizations eligible for a group determination letter. The instructions in regard to Part IV, line 1d, however, apparently intend that such affiliated organizations will be considered "related organizations" because they refer to "a parent organization or affiliates at the state, local, or regional level." State, local, and regional affiliates, however, often do not meet the definition of parent-subsidiary or brother-sister organizations in regard to control, let alone supporting and supported.

Legally, each affiliated superior and subordinate entity is generally a separate legal entity. Typically, a local unit is a voluntary unincorporated association consisting of its local members. The national or international superior organization is usually a nonprofit membership corporation consisting of all the members of the organization nationally or internationally, and governed by a national or international governing body. The local members in a subordinate unit control the bulk of the activities of the local unit, with minimal supervision from the superior organization, which may do no more than grant a charter to the local unit prescribing minimal requirements for continued affiliation. These local subordinate units may be under the "general supervision" of the national or international superior organization for purposes of a group determination letter, but they are not under the control of the superior organization.

Therefore, if affiliated organizations are intended to be included in the definition of "related organization," for reasons of clarity and transparency, the definition should add two additional bullet points along these lines:

- Central—an organization which has general supervision or control over affiliated subordinate organizations
- Subordinate—an organization subject to the general supervision or control of an affiliated central organization

*Form 990 "Core," Part III, Governance*

*Line 1. Governing Body Composition*

In nonprofit organizations with members, the governing body should strive to reflect the diversity among the members. In particular, if the organization consists of a number of separately organized constituencies, such as a central national organization with geographically based and interest-group based constituent units, the governing body should include individuals who reflect the various geographic regions and interest groups that participate in the central national organization. If the governing body is not representative of the membership and locally organized members do not feel that they have a real stake in organizational governance at higher levels, the organization is not likely to maintain the long-term support and enthusiasm of the members.

Perhaps more important, nonprofits do not face market discipline in the markets for capital or their products and they are not subject to shareholder discipline for poor performance. State and federal regulators often have limited mandates and limited funding.

Often review of governing body conduct by the members is the only form of assuring meaningful accountability in the nonprofit corporation. Because unpaid volunteer governing body members often have close, highly dependent relationships with paid staff (unlike directors of business corporations, who are compensated for their time and may have significant independent corporate resources devoted to their performance of their duties), they are susceptible to being co-opted by staff, or at least lulled into relaxed vigilance. In those cases, an active and involved membership is the only way to provide realistic accountability and oversight. An active and empowered membership is frequently the answer to the query "Quis custodiet ipsos custodes?"

A recent empirical study, one of the first to address the importance of member participation in governance, found significant benefit to election of directors by members. Francie Ostrower, *Nonprofit Governance in the United States: Findings on Performance and Accountability from the First National Representative Study* 16–17 (Urban Institute, Center on Nonprofits and Philanthropy 2007). Ostrower found that organizations having at least one governing body member directly elected by membership improves governing body performance. Such member involvement in governance had a high correlation with governing body "activity in multiple internal and externally oriented roles (e.g. fundraising, financial oversight, planning, monitoring programs, setting policy)." *Id.*

Academic writers have similarly theorized that an empowered membership may serve important oversight and monitoring functions as well as anchoring fidelity to mission. *See* Evelyn Brody, *Charity Governance: What's Trust Law Got to Do with It?* 80 Chi.-Kent L. Rev. 641, 669 (2005) ("If provided for, members of the organization may exercise influence through their election of the governing board, and through their participation in decisions to take certain extraordinary transactions."); Dana Brakman Reiser, *Enron.Org: Why Sarbanes-Oxley Will Not Ensure Comprehensive Nonprofit Accountability*, 38 U.C. Davis L. Rev. 205, 277 n.270 (2004) ("[W]hen members do exist, they have advantages in perceiving mission creep, and for some types of nonprofits, training and empowering members may allow for mission accountability gains."); James J. Fishman, *Improving Charitable Accountability*, 62 Md. L. Rev. 218, 256 (2003); Dana Brakman Reiser, *Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits*,82 Or. L. Rev. 829, 849, 853, 880, 899–900 (2003);[1] Evelyn Brody, *Agents Without Principles: The Economic Convergence of the Nonprofit and For-Profit Organizational Forms*, 40 N.Y.L. Sch. L. Rev. 457 (1996) ("In those few nonprofits that have a membership who elect directors, the members perform the oversight function of

[1] "Members play two distinct, but related roles—as ultimate decision-makers and as monitors/enforcers of nonprofit directors and managers." "Perhaps a voting membership is an unrecognized mechanism of filling [the nonprofit governance] accountability gap." "The trend away from members . . . threatens the legitimacy of the nonprofit sector and the advantages it receives [from government]." "Optionality [allowing nonprofits to choose a membership structure or a self-perpetuating board structure] results in a systematic bias against internal democracy in nonprofit governance. Without some form of encouragement for the adoption of democratic, membership-based governance structures, members will become more and more rare. . . . However, dismembering the nonprofit sector would exact a serious social cost by reducing its ability to constitute a sphere of civil society with democracy-enhancing effects. This failure alone should concern a society that believes in the importance of civil society and democracy."

shareholders."); James J, Fishman, *The Development of Nonprofit Corporation Law and an Agenda for Reform,* 34 Emory L.J. 617, 661 (1985) (In certain corporations, "[m]embers have the potential power to control the organization and to ensure that its nonprofit purposes are achieved."). *See also* Dana Brakman Reiser, *Nonprofit Takeovers: Regulating the Market for Mission Control,* 2006 B.Y.U. L. Rev. 1181 (in two case studies of member activism regarding programmatic initiatives, active grass-roots members challenged board-driven changes from longstanding interpretations of organizational missions, contrary to assumptions mentioned in the article; in the case of the Sierra Club, members challenged a board-driven change of policy favoring immigration; in the case of the Royal Society for the Prevention of Cruelty to Animals, members challenged a board-driven change of policy opposing hunting).

Therefore, it might be helpful to add a third sub-line under line 1, along these lines:

1c If a membership organization, enter the number of members of the governing body elected by the members of the organization

*Line 2. Governance Changes*

As discussed in regard to line 1, membership oversight over governing body conduct is often a critical component of good governance. Unfortunately, as detailed by Professor Dana Brakman Reiser of Brooklyn Law School, institutional concerns valuing efficiency over accountability often result in disempowerment or elimination of members or new organizations being formed without members. Dana Brakman Reiser, *Dismembering Civil Society: The Social Cost of Internally Undemocratic Nonprofits,*82 Or. L. Rev. 829 (2003). In the experience of the author of this letter, active and engaged memberships have turned out governing bodies that became too entrenched and then found sloppy, if not downright improper, accounting practices by the ousted governing body. These practices usually occurred not through improper motives, but because entrenched governing bodies become unaccountable and increasingly informal. An active and empowered membership can serve as an important counterbalance in ferreting out undue coziness in entrenched governing body leadership or professional management.

Therefore, it might be useful to add a line to the examples of significant governance changes listed in the instructions along these lines:

- to the role and responsibilities of the members in organizational governance

*Line 6. Contemporaneous Minutes*

Consistent with the comments above on the significance of active member involvement in governance, the question should be reformulated to refer to meetings of members as a body and houses of delegates or other similar bodies representative of the members.

In addition, many committees are organized simply to study and make recommendations. Only committees empowered to act for the organization need to keep minutes in the detail required of governing bodies, members acting as a body, or houses of delegates.

Therefore, it might be better to ask a question along the following lines:

> Does the organization contemporaneously document the meetings of the members or representatives of the members, the governing body, and committees with power to act for the organization through the preparation of minutes or other similar documentation?

*Line 9. Audit Function*

The author welcomes the suggestions that nonprofit organizations should have an active audit committee and not rely solely on outside audits, which many small-to mid-sized nonprofits cannot afford. An important aspect of nonprofit governance, however, is not just that there be an audit, but that the audit be reviewed and approved by a body likely to review, understand, and ask questions about the audit. Especially with volunteer auditors, review and approval is a significant additional check on financial expenditures. Longstanding best practice in voluntary membership organizations has been for the membership, not the governing body, to review and approve the audit committee report and never to approve a treasure's report without an audit. Henry M. Robert, *Robert's Rules of Order Newly Revised* (10th ed. 2000) pp. 461–62. Moreover, another significant concern is the selection and composition of the audit committee. The treasurer and the professional staff working in the financial area should not be involved in selection of or serve on the audit committee. Alice Sturgis, *Standard Code of Parliamentary Procedure* (4th ed. 2001) ("TSC") p. 214.

Therefore, the question on Line 9 should contain more detail, along the following lines, and instructions should be added reflective of the concerns addressed in this comment:

a. Does the organization have an audit committee?

b. If the answer to 1a is "yes," how is the audit committee composed and selected?

c. If the answer to 1a is "yes," which body approves the audit committee's report?

*Line 10. Governing Body's Governance Involvement*

The author applauds the intent behind the suggestion in this line that governing bodies take an active role in governance and financial oversight of nonprofit organizations through review of the Form 990. The author has some concerns that the form suggests that the governing body review the form 990 before it is filed, as review of the final version (as opposed to a draft) may be impractical in many circumstances given potential conflicts between infrequent board meetings and IRS filing deadlines. It may be more practical to suggest the adoption of a policy that final the Form 990 be circulated to all members of the governing body after filing and that any changes between any draft Form 990 previously circulated to the governing body and the final Form 990 be highlighted for the members of the governing body.

A significant element of good governance for governing bodies that is not addressed in this part of the draft form is regular governing body training in its fiduciary responsibilities (including fidelity to mission), financial literacy, and the tools necessary for active participation in meetings and committee service. Even nonprofit governing bodies with relatively infrequent

turnover need regular training in their proper roles (including oversight responsibility and handling conflicts of interest) and the tools of parliamentary procedure necessary to exert their influence and make their opinions heard.

Without training, the most powerful, independent, and well meaning governing body will not function effectively. Good governing body evaluation and training are essential to a governing body's members' ability to exercise their fiduciary duty of care. New governing body members should have an orientation before or shortly after commencing service, and longstanding board members should have a perhaps shorter, but more intensive training at least every several years. For governing bodies with frequent turnover, annual training is a good idea, which in such cases can typically be combined with new governing body member orientation.

A recent study supports this conclusion. Patricia Dautel Nobbie & Jeffrey L. Brudney, *Testing the Implementation, Board Performance and Organizational Effectiveness of the Policy Governance Model in Nonprofit Boards of Directors*, 32 Nonprofit & Vol. Sector Q. 571, 591–92 (2003) (no significant difference in effectiveness in achieving mission goals between governing bodies receiving Carver policy governance training and broader, nonprescriptive training by National Center for Nonprofit Boards). Nobbie & Burdney discovered that all governing bodies that underwent self-examination and governing body development performed better on a number of indices than governing bodies that did not have training and development. The actual substantive teachings of the training and development process (Carver policy governance v. NCNB) were not as important as the required re-examination of mission, practices, and procedures through the governing body development process, which should include regular governing body training.

Quality governing body training contains several essential elements: fiduciary responsibilities (including fidelity to mission), financial literacy, and the tools necessary for active participation in meetings and committee service. In order to utilize their substantive knowledge to the benefit of the organization, a particularly important and often overlooked vital need is for the members of the governing body to know how to participate actively in governing body meetings, get their points across in a fair and courteous manner, and adhere to procedures that allow for fair and respectful participation by all governing body members.

Without any adopted procedures (even relatively short, informal ones), meetings of more than about one half-dozen participants can rapidly descend into chaos once a contentious issue erupts. Moreover, unless procedures are adopted in advance, any procedure (no matter how well intended) that is adopted on an ad hoc basis to deal with a particular situation, the perception of unfairness is likely to persist in the party that did not prevail. The larger the group, the greater the need for formality in decision making for all members to feel that they can participate equally fairly.

Without strong governing body training in meeting procedures and a set of participation-friendly adopted rules, the presiding officer can control the meeting and achieve his or her own personal goals through the organization, while stymieing the efforts of those who disagree to make others understand their side of the argument. Adopting objectively fair procedures adopted in advance and regularly training governing body members in their use

allows governing body members to educate themselves before a meeting about how decisions will be made and how to present their positions vigorously but fairly in case of disagreement.

The draft might therefore benefit from the addition of another sub-line along the following lines:

> 10b Does the organization's governing body have readily accessible rules for the conduct of meetings and policies concerning new governing body member orientation and regular governing body training?

*Line 11. Availability to the public.*

Another critical component of good financial governance is budgeting in advance of spending and the fiscal discipline necessary to stay close to budgeted expenses and income. TSC p. 215. Financial statements alone do not demonstrate fidelity to budget discipline, as a comparison of variance between budgeted and actual income and expenditures does. Another sub-line might be added under Line 11 for budget and budget variance report.

Many noncharitable nonprofits, particularly social clubs under 501 (c) (7) and fraternal societies under 502 (c) (8) & (10), may have good programmatic reasons not to disclose their internal financial affairs, detailed governance arrangements, or membership criteria to the public, except to the extent required by law. Even if the entity chooses not to provide to the public the governance-related documents listed in Line 11, those documents should be available to the membership, for the reasons of transparency and accountability to members discussed above in regard to Line 1. Availability of such documents to a large, active, engaged, and well-informed membership will provide (1) an incentive to fair conduct for those preparing the documents, and (2) a means for diligent, concerned, and well-intentioned members to ensure accountability of organizational fiduciaries.

Therefore, the question should be re-phrased:

> How do you make the following available to the public or members only? Place a *P* in the applicable box to indicate "public," an *M* to indicate "members only," or leave blank to indicate unavailable in a particular format.

In that case, the instructions should indicate that availability of a document to members on a website may be by password access limited to members.

Thank you for your consideration of these comments. Please feel free to contact me with any questions.

Yours truly,

Michael E. Malamut

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*Michael E. Malamut*

***Attorney-at-Law**** | ***Professional Registered Parliamentarian***
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May 7, 2007

Division of Exempt Organizations
Internal Revenue Service
PO Box 192
Covington, KY 41012-0192

Re: Comments on Draft Good Governance Practices for 501 (c) (3) Organizations

Dear Sir or Madam:

The following comments on the Draft Good Governance Practices for 501 (c) (3) Organizations are based on the professional experiences of the author of this letter as an attorney and professional parliamentarian working with many nonprofit membership organizations. In my practice, I work with a number of charitable membership organizations, including local, state, and national governing bodies for sports; international governing bodies for twelve-step organizations; and religious institutions.

*Introduction, Paragraph 2. Composition of the Board*

In charities with members, the board should strive to reflect the diversity among the members. In particular, if the charity consists of a number of separately organized constituencies, such as a national organization with geographically based and interest-group based constituent units, the board should include individuals who reflect the various geographic regions and interest groups that participate in the organization. If the board is not representative of the membership and locally organized members do not feel that they have a real stake in organizational governance at higher levels, the organization is not likely to maintain the long-term support and enthusiasm of the members. The paragraph might be enhanced if it added a statement along the following lines: "The governing board of an organization operating on a membership basis should include members representing the diversity in the backgrounds of the members, and, if it consists of constituent units, the board should include members representing the diversity of the constituent units."

*Principle 3. Due Diligence.*

In order to utilize their substantive knowledge to the benefit of the organization, the members of the board must know how to participate actively in board meetings, get their points across in a fair and courteous manner, and adhere to procedures that allow for fair and respectful participation by all board members. Without any adopted procedures (even relatively short, informal ones), meetings of more than about one half-dozen participants can

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* Admitted to practice in Massachusetts, New York, and the District of Columbia.

rapidly descend into chaos once a contentious issue erupts. The larger the group, the greater the need for formality in decision making for all members to feel that they can participate equally fairly. Having objectively fair procedures adopted in advance allows board members to educate themselves before a meeting about how decisions will be made when there is a disagreement among the members.

Board member training should include, as a significant component, training in the procedures used by the board to take action, which typically occurs through the making of, debate over, and adoption of motions. Without strong board training in meeting procedures and a set of member-supportive adopted rules, the presiding officer can control the meeting and achieve his or her own personal goals through the organization, while stymieing the efforts of those who disagree to make others understand their side of the argument.

The draft might therefore benefit from the addition of a final bullet point along the following lines: "is knowledgeable about the procedures for how to participate actively in the deliberative decision-making process of the board."

Thank you for your consideration of these comments. Please feel free to contact me with any questions.

Yours truly,

Michael E. Malamut

**From:** Amy Mignogna
**To:** *TE/GE-EO-F990-Revision;
**CC:**
**Subject:** draft Form 990 comment letter
**Date:** Friday, September 14, 2007 1:14:24 PM
**Attachments:** draft990letter.pdf

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To whom it may concern:

The Ohio Society of CPAs has prepared a comment letter on the draft Form 990, which is attached to this email.

If you have any difficulty opening the PDF or have any questions regarding the content of the comment letter, please contact me at the phone number below.

Regards,

Amy Mignogna

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Senior Manager, Governmental Affairs
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THE OHIO SOCIETY
OF CERTIFIED
PUBLIC
ACCOUNTANTS

September 14, 2007

Form 990 Redesign
ATTN: SE:T:EO
1111 Constitution Ave., N.W.
Washington, D.C. 20224

*RE: Form 990 Redesign*

To Whom It May Concern:

A task force of The Ohio Society of CPAs, a professional association representing 24,000 members, has reviewed the IRS's proposed redesigned Form 990 and submits the following comments for consideration.

The changes contained in the redesigned form are expansive and have broad implications for exempt organizations and the tax practitioners responsible for preparing the form. Due to the breadth of the changes, we feel that a ninety-day comment period is an inadequate amount of time to thoroughly review and substantively comment on each of the changes prescribed in the draft 990. We feel strongly that an extension of the comment period would allow for a more thoughtful deliberation of the impact of the changes and provide a better understanding of the goals and objectives of the IRS in making these modifications. Despite the compressed comment period, The Ohio Society of CPAs draft 990 task force, a seven-person group with a combined 160 years of experience in the area of exempt organization tax, has identified four overarching areas of concern. Examples of related definitional and administrative concerns are also outlined in this comment letter:

1) **The questions related to governance issues apply a standard that is not appropriate for all organizations, will promote public confusion and will inspire misreporting.** The order of the draft 990 de-emphasizes the purpose and programs of the exempt organization, allowing for an uninformed public to pull out a few arbitrary facts or statistics that may or may not be relevant for many organizations as opposed to gaining a clear understanding of the exempt organizations goals and objectives. In addition, the prominence within the return and the nature of the questions on governance practices makes a strong public statement that the Internal Revenue Service is prescribing a standard of governance practices for all exempt organizations in excess of what is required by law, and which may not be appropriate for all types of exempt organizations.

   Many questions assume that all organizations should internally operate in the same manner, which may not be the most beneficial practice for all organizations. For example, Part II, Section B, question 3, assumes that an organization's governing body approves the compensation of their Chief

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Financial Officer, which is not nor should it be standard practice for most tax exempt organizations. Additionally, in Part III, all but question 2 are related to governance policies that are not required. To the uninformed reader, honest and justifiable answers could paint an unwarranted negative picture of an organization, causing unnecessary negative media exposure. This increases incentives for misreporting, and may cause organizations to make operational changes that are not always in the best interest of their exempt purpose.

The ratios calculated in Part I are arbitrary, as they are not comparable for different types and sizes of exempt organizations. Additionally, the fundraising percentage on line 26 referencing Schedule G would be significantly different for similar organizations when one uses an outside consultant while the other has an in-house development employee, as the employee does not need to be listed on Schedule G, while the consultant does. There are also some return errors, for example, Line 8(a) in Part I cannot be calculated by a 501(c)(6) organization, as it does not complete Line 17. Presuming what ratios are important to the reader places undue focus on specific elements of the return, and will inspire aggressive accounting as exempt organizations attempt to manage to those ratios from a public relations perspective.

Disclosures related to salary information for other than top executives cause trepidation to many organizations served by our membership. Specifically, there are concerns that the information is not comparable, as the disclosures are not able to incorporate life cycle issues of an exempt organization; for example, the organization that is just beginning to make the transition into an in-house development director. The IRS's own executive compensation study found that abuses in the area of executive compensation were not nearly as prevalent as had been anticipated. It appears that a very wide net is being cast as a result of a very small number of abuses.

**RECOMMENDATION: Consistent with the agency's goal of providing a realistic picture of the organization and a basis for comparison to other organizations, arbitrary ratios calculated on the face of the return should be eliminated. The order of presentation of the required elements of the return should also permit organizations to present items such as the mission, exempt purpose, and primary programs to provide context for the disclosures that follow (for example, move Part IX to Part I.) Consider which compensation information is truly useful in furthering public service objectives, and what will serve more to mislead the public when taken out of context.**

2) **Questions related to statutory requirements of exempt organizations should be separated from questions which are not mandated by statute but are common exempt organization best practices.** By co-mingling questions on the return related to procedures mandated by the tax code and those that are considered by the agency to be exempt organization best practices, there is an implication to the uneducated reader of the return that an exempt organization is legally required to adhere to the best practice. Examples include maintaining documents such as a conflict of interest policy and providing audited financial statements as public documents, neither of which are required by the tax code.

   Additionally, asking for the number of independent members of an organization's governing body implies to the user of the return that independence is a requirement. In application, perfectly legal practices such as family members serving on boards together may be unavoidable, particularly in smaller communities, or within exempt organizations of a specific purpose. In addition, depending upon the knowledge and skill of each board member, this may be necessary to successfully fulfill the mission of the exempt organization. Many of the questions in the proposed revision of the form are primarily targeted to a publicly supported charity. The general public is unaware of such distinctions, and as a result of the prominence of the questions on the return related to best practices for the most common situations, this may cast an unfavorable view upon organizations that operate fully within the provisions of the law but whose organizational structure or purpose is unique.

   **RECOMMENDATION: Consistent with the agency's goal of enhancing the transparency of the return to the public, the revised Form 990 should clearly distinguish between questions that are requirements of the tax code and those that are best practices for common types of exempt organizations.**

3) **The compliance burden associated with the redesigned 990 will be disproportionately burdensome on many exempt organizations, particularly smaller ones.** Despite the commentary included with the draft that most organizations will not experience a material change in burden, tax practitioners on our task force indicated that most of their smaller exempt organization clients will be required to complete and provide five or six schedules in addition to the core form. Estimates from tax preparers

participating on our task force review were that preparation time would increase by as much as two to three times what is required for the current 990 and supporting schedules. Tax preparers will be required to interview parties not previously involved in tax preparation, including board members, marketing departments, and individuals involved in operational and structural decisions going well beyond the scope of current tax preparation and even audit engagements of these entities. Many exempt organizations also do not currently have a recordkeeping infrastructure to comply with some of the added requirements and we question whether the increased information justifies the time and expense.

The amount of added time required for a tax preparer to gather the information and prepare the form will be cost-prohibitive to many exempt organizations. The additional expense will decrease the resources that can be offered to program services in support of the organization's mission. We question whether that cost may exceed the benefit of the service to the public of the added information. With little reserves available to pay for such added expenses, the choice will be made by many organizations to forgo using a professional and to prepare returns in-house. Additionally, external preparers, who often donate services to small exempt organizations, will increasingly find that they are not able to sufficiently respond to the requirements, as the infrastructure of the organization does not permit providing adequate comfort that information is complete. These consequences will result in greater unintended errors, will decrease the quality of information provided and will increase the volume of amended returns, adding a cost burden to the IRS and the economy.

To minimize the length of the core 990 form, questions that refer to separate schedules should be contained on those separate schedules. For example, questions 14 and 15 on Part VII should be on separate schedules only required for 501(c)(7) and 501(c)(12) organizations.

**RECOMMENDATION: Consistent with the agency's goal of promoting compliance, consider extending the time for implementation of the new form to provide for exempt organization education. Consider relief for the smallest of exempt organizations (for example, is it time for the revenue threshold for those required to file the Form 990 to be raised?) The IRS should consider sponsoring significant education for exempt organizations to increase their capacity for compliance.**

4) **There are a number of definitional errors throughout the draft 990 form.** We appreciate the IRS' acknowledgment that definitional edits are needed. Ambiguous language and uneccesary redundancy would increase the compliance and cost burden on exempt organizations and the IRS.

Examples noted by the Ohio Society of CPAs task force include:

- Part III, Question 10 asks if the organization's governing body reviewed the 990 before it was submitted. Because this question will always be asked before the form is signed, the answer will always be "no" and the question is therefore unnecessary.
- The first half of Question 8 on Part III is confusing to the uneducated reader. It is perfectly appropriate (in fact, preferred in most cases) for an officer or employee to prepare the organization's financial statements. We recommend eliminating the first half of the question.
- On Schedule F, Foreign Activities, "Activities" needs to be better defined. Many organizations are concerned that listing activity for every country separately will present a significant compliance burden.
- Compensation information is duplicated in Part II and Schedules J and L.

**Additional Comments:**

- Members of The Ohio Society of CPAs draft 990 task force are concerned about the inability to attach schedules when filing electronically. Experience has shown that a need for additional explanatory material is most significant for exempt organizations, particularly since the return is a public document. For purposes of transparency and clarity, the capability to attach files with additional explanatory information is absolutely critical.
- On Part II, Section A of the core form, task force members preferred the separation of officers and highly compensated employee disclosures for clarity.
- On Part II, Section B, Question 5 adds a significant recordkeeping burden for exempt organizations to comply. Obtaining assurance from all parties listed on each of these items for a 5-year period will require significant resources that would better be directed to the organization's exempt purpose. Additionally, it is not clear what level of responsibility the signer would have for determining whether the representations they have received from all parties on these questions are complete. This provides significant potential exposure to the organization of an unintended misrepresentation. Task force members were not able to identify any requirement in the tax code for this information.

- Task force members continue to express a desire that the IRS provide the option for financial statements prepared under generally accepted accounting principles and accept consolidated 990s. The differences between GAAP and tax-basis financial statements are confusing to the public user.
- On Schedule D, Part VII, the requirement to include uncertain tax positions disclosed on the audited financial statements is a first step in making the audited financial statements a public document, something that is not required under the law. Task force members also expressed concerns that there is not sufficient space provided to respond to this question without the ability to attach a document.
- On Schedule M, an exception or guidance is needed for how to value incidental non-cash contributions. Non-profit organizations do not currently have the recordkeeping systems to track incidental non-cash contributions, and this requirement would add a significant new compliance burden. Tax practitioners are also concerned about their ability to gain adequate comfort with this information.

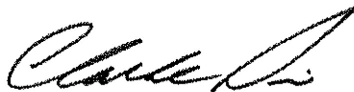
The Ohio Society of CPAs draft 990 task force embraces the objectives of the Form 990 redesign to improve transparency, clarity and public usefulness, and to minimize the burden on complying organizations; however, we believe that this proposal will have negative consequences in each of these areas:

- The added compliance requirements of this proposal will be overpowering to many complying entities, as well as unduly confusing to the public attempting to understand them.
- The increased economic costs of the proposal, as well as the impact on the proportion of public funds being directed to compliance, instead of to accomplishing the purposes of tax exempt organizations, will be significant and negative.
- The quality of information provided through the Form 990 will be reduced. Many added questions not required by law focus on specific elements of governance that are not the most relevant measures for all exempt organizations, and are overreaching in terms of the objective of promoting compliance.
- The addition of and the positioning of arbitrary measures in the return will cause the public to focus on and misinterpret figures taken out of context, and will incent organizations to manage their reporting to those measures, reducing openness, transparency and clarity.

We strongly recommend that additional time be devoted to considering all dimensions of impact of the redesign proposal, and if the comment period is not extended, that additional time be added to the period preceding implementation. Organizations will need multiple business cycles to adopt new recordkeeping, related party reporting and budgeting for the added costs of compliance.

We appreciate the opportunity to comment on the draft Form 990. Feel free to contact me or Amy Mignogna, senior manager, governmental affairs, at 800.686.2727 if you have any questions.

Regards,



Clarke Price, CAE
President & CEO
The Ohio Society of CPAs

David M. Reape, CPA
Chair, Draft 990 Task Force
The Ohio Society of CPAs

**From:** davidcohn

**To:** *TE/GE-EO-F990-Revision;

**CC:**

**Subject:** Proposed IRS Form 990: Comments and Questions

**Date:** Friday, September 14, 2007 1:26:29 PM

**Attachments:** IRS Form 990 Letter 091407.pdf

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To whom it may concern:

Attached are comments and suggestions prepared by Sullivan, Cotter and Associates, Inc. regarding the proposed IRS Form 990.

Please contact me at the phone number or email address below if you have any questions.

Best regards,

David Cohn, ASA, EA, MAAA
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September 14, 2007

Internal Revenue Service
Form 990 Redesign
ATTN: SE:T:EO
1111 Constitution Ave., N.W.
Washington, DC 20224

RE: Comments regarding the proposed IRS Form 990

Sullivan, Cotter and Associates, Inc., a compensation consulting firm that serves many U.S. tax-exempt organizations, respectfully submits our comments regarding the proposed Form 990 for fiscal year 2008. As requested to be submitted by the September 14, 2007 due date, the following provides our suggestions as it relates specifically to the proposed **Schedule J "Supplemental Compensation Information".**

**Housing**

We suggest adding more detailed instruction with regard to the reporting of housing benefits to address the circumstances for which the benefit is provided and/or reported to officers, directors, trustees or key employees. We suggest the addition of specific yes or no questions with regard to housing benefits:

- Did the organization provide a cash housing allowance to any Officer, Director, Trustee, Key Employee…?
- Did the organization provide housing to any Officer, Director, Trustee, Key Employee…?
    - If yes, was the housing provided for the convenience of the employee or a requirement of employment?

Since housing can represent a major component of compensation, particularly in larger metropolitan areas, the Service may want to consider requesting information on the Form 990 that specifically captures any housing benefits that are provided.

**Qualified Retirement Benefits**

As we understand it, the proposed Form 990 does not require disclosure of qualified retirement benefits if they are not found on an individual's W-2 Box 5 or Form 1099-MISC Box 7.

We suggest including the disclosure of qualified retirement benefits as, in certain circumstances, they can make up a significant portion of an individual's benefits program, and contribute to the understanding of the "total compensation and benefits" provided to officers, directors, trustees and key employees. In addition, disclosure of qualified retirement benefits is required under the

current Form 990 which would make comparisons difficult between older Form 990s and the revised Form 990.

Our suggestion is to add the following:

- On the proposed Schedule J, add a separate column for these benefits or include these benefits in Column C (i.e., with nonqualified deferred compensation).
- For account-based qualified plans (e.g., 401(a), 401(k), 403(b), or money purchase plans), the amount of deferred compensation should be equal to employer-provided contributions for the year.
- For defined benefit plans (e.g., traditional final average pay or cash balance plans), the amount of deferred compensation should equal the increase in the benefit's actuarial present value due to the accrual of an additional year of service during the year. Effectively, this calculation would be limited to the service cost for the year, which is determined during these plans' SFAS No. 87 annual valuations.

**Nonqualified Deferred Compensation**

As described in the proposed Form 990 instructions, organizations are required to disclose any nonqualified deferred compensation that is not reported on an individual's W-2 Box 5 or Form 1099-MISC Box 7.

In addition to the much improved instructions regarding these benefits, we suggest reporting for different types of nonqualified arrangements as follows:

- Account-based plans. We suggest that deferred compensation should equal the amount of employer-provided contributions made during the year. We do not believe including the interest (or earnings) on the beginning of year balance is appropriate for disclosure of compensation as a relatively high (or low) rate of investment return during the year could distort the amount of compensation disclosed on the Form 990.
- Defined benefit plans. We suggest that deferred compensation should equal the increase in the benefit's actuarial present value due to the accrual of an additional year of service during the year. Effectively, this calculation would be limited to the service cost for the year, which is determined during these plans' SFAS No. 87 annual valuations (and is consistent with our suggested approach above regarding qualified defined benefit plans).

There does not appear to be any reporting for a Supplemental Executive Retirement Plan (SERP) if the benefits are funded through a qualified retirement plan (e.g., "QSERP"). It appears an organization in this circumstance would report a "Y" under Column G and therefore disclose that a SERP exists, but there would not be any nonqualified deferred compensation reported under Column C. Is this the Service's intent? We suggest the Schedule J include a column (or instructions) for reporting qualified retirement plan benefits or specify that SERP benefits must be reported in Column C, regardless of the plan's funding vehicle.

**Split-Dollar Life Insurance (SDLI)**

As we understand it, the "cost of current insurance protection under compensatory split-dollar life insurance arrangements" is to be reported on Schedule J, Column B(iv) which is tied to W-2 Box 5 or Form 1099-MISC Box 7.

We suggest that the Service provide additional guidance for the reporting of SDLI benefits under the two common taxation approaches: economic benefit regime and loan arrangements:

- Under economic benefit reporting, the annual cost of insurance (e.g., term insurance cost) is reported.
- For loan arrangements, as we understand it, the cumulative loan is to be reported in Schedule L.

It appears that this difference in reporting is significant and may distort the true value of compensation provided through SDLI arrangements.

* * *

SullivanCotter wishes to thank the Service for the opportunity to provide comments on the redesign of the Form 990 for fiscal year 2008.

Sullivan, Cotter and Associates, Inc.

David Cohn
Retirement Practice Leader, Chief Actuary
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**From:** Jim O"Guinn

**To:** *TE/GE-EO-F990-Revision;

**CC:**

**Subject:** Comments on proposed changes

**Date:** Thursday, September 13, 2007 6:49:20 PM

**Attachments:** TSCPA Letter to IRS Form 990.doc

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Dear Ms Lerner, Mr. Schultz, and Ms Livingston:

Please find attached comments regarding the proposed changes for IRS Form 990 and its procedures from the perspective of the Texas Society of Certified Public Accountants.

Kindest regards,

*Jim O'Guinn, CCP*
Director, Information Systems
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***Texas Society of CPAs: Connecting. Protecting. Advancing.***

Texas Society of
Certified Public Accountants

September 13, 2007

Lois G. Lerner
Director of the Exempt Organizations Division of the IRS

Ronald J. Schultz
Senior Technical Advisor to the Commissioner of TE/GE

Catherine E. Livingston
Deputy Associate Chief Counsel (Exempt Organizations)

Internal Revenue Service
Form 990 Redesign
ATTN: SE:T:EO
1111 Constitution Avenue, NW
Washington, DC 20224

Dear Ms. Lerner, Mr. Schultz, and Ms. Livingston:

One of the expressed goals of the Texas Society of Certified Public Accountants (TSCPA) is to speak on behalf of its members when such action is in the best interest of its members and serves the cause of Certified Public Accountants in Texas, as well as the public interest. The views expressed herein are written on behalf of Certified Public Accountants that belong to the TSCPA and who serve not for profit entities. We appreciate the opportunity to provide input into your deliberations on the re-design of the Form 990.

The proposed draft Form 990 poses significant questions and concerns for nonprofit organizations that are required to file. Due to the diversity of organizations in the tax-exempt community – diversity in size, type of organization, activities, and sources of revenue – the proposed changes to the form will impact tax-exempt organizations differently. In addition, because of the size of the non profit community, many affected organizations still remain unaware of the significant changes proposed and their potential impact on their organizations.

TSCPA members would like to see an extension of the comment period to allow for prudent consideration of the new draft form and its implications for the different types of filing organizations. We acknowledge the IRS's position that this may not be possible, because of technological and budgetary reasons, so we request a delay in implementation of the core form until the 2009 tax year (returns filed in 2010).

We think the draft Form 990 is directed too much toward charitable organizations and does not take into account the vastly different purposes and practices of non-charitable organizations. The current form does not lend itself to reporting by trade associations, business leagues, and many other non-charitable entities. A properly-designed Form 990 could help educate the general public and the media about the purpose and mission of non-charitable organizations that serve the general public so well.

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Specific Comments:

Page 1 "Summary" section is to provide an overall "snapshot" of the organization which is a useful and logical approach to Form 990 re-design; however, the questions asked will be confusing to the general public and therefore misleading particularly for non-charitable organizations. We need to take the time to develop appropriate summary information before requiring it on the form.

Specific questions related to governing body members, fund-raising and compensation must be re-worded to insure that false impressions are not created in the minds of readers about independence and appropriateness of governance and compensation. It will be important to insure that organizations are not all compared as if they are the same type / purpose organizations.

The expansion of the definition of "key employee" and requiring information about independent contractors is not pertinent for non-charitable organizations. If this information is to be required, it should be on a page specific to non-charitable organizations and not on the summary page.

The new Form 990's required disclosure of the city and state of residence for every person listed in Part II, Section A is very troublesome. Because the Form 990 is available to anyone over the Internet (c3s) and to anyone who requests a copy, the disclosure of this information could lead to privacy invasion, or even outright identity theft. We strongly dispute the importance of this information and suggest that providing the member's state of residence, rather than city and state, would accomplish the same purpose. We strongly believe the organization's address can continue to be an alternative for this reporting purpose. If the IRS does still require the disclosure of city and state, this information should not be available to the general public.

On Schedule J, we do not see any reason to provide nontaxable expense reimbursements (Column E). These amounts merely represent repayments for legitimate business expenditures submitted and documented under an "accountable plan," and no meaningful information can be gleaned by the amount of expenses so reimbursed. Moreover, any large amounts listed may be wrongly misconstrued by non-sophisticated readers of the form. Organizations vary in their reimbursement policies, and what may seem like an excessive amount of reimbursement may merely reflect a difference in accounting practices and procedures. For example, employees and board members of one organization may book and pay for their own travel arrangements, whereas at another organization all travel arrangements are booked and paid for by the organization itself. Including nontaxable reimbursements in Column (F) significantly distorts total compensation figures.

Statement of Program Service Accomplishments (Part IX) – we believe this is a vital part of the information reported on the Form 990. This information should be included on the summary page or moved to the front of the return.

Texas Society of
Certified Public Accountants

We appreciate the opportunity to provide these brief comments on the re-designed form; however, we strongly believe that more time is needed to allow more practitioners, filers and even readers of the Form 990 time to fully digest the significant changes being proposed.

We encourage you to delay any implementation of this new form and to obtain more input before making it required.

Cordially,

James A. Smith
Chairman
Texas Society of Certified Public Accountants

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