From: Lucy Bush

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

CC: Paul Keller; Tracy Paglia;

Subject: Form 990 Redesign Comments Attached Due Today, Sept. 14

Date: Friday, September 14, 2007 6:35:45 PM

Attachments: Form 990 Redesign.pdf

Please see comments attached.

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September 13, 2007

Internal Revenue Services
Form 990 Redesign, SE:T:EO
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Washington, DC 20224

To whom it may concern:

We respectfully submit the following comments in response to IR-2007-117 issued on June 14, 2007 requesting comments and discussion on the draft Form 990. Understanding the three guiding principles in the Form 990 redesign (transparency, compliance and minimizing organizational burden), we generally believe that the form has failed in its effort to minimize the burden of the filing organization.

In addition, many of the questions appear to emphasize what could be viewed as "governance best practices" that are not required by law. The public might view these questions as requirements to maintain tax-exempt status. A "no" answer could be misconstrued as a problem when it really is an attempt to increase transparency and governance in operations. We believe the instructions should clarify the fact that many of these are recommendations and not stringent requirements for tax-exempt status.

Please find below our specific comments related to the Form 990 and associated instructions.

GENERAL INSTRUCTIONS

1. The burden of filing this draft form warrants raising the thresholds for filing Form 990-EZ. As currently stated on page 3 of the instructions to the core form, organizations with gross receipts between \$25,000 and \$100,000 <u>and</u> total assets at the end of the year of less than \$250,000 may file Form 990-EZ. We recommend that these thresholds be increased to gross receipts less than \$250,000 <u>or</u> total assets at the end of the year of less than \$500,000 may file Form 990-EZ to reduce the filing burden on small nonprofit organizations.

2. Page 3 of the core form instructions leave a confusing gap in filing. The current phrasing for requiring the Form 990 to be filed is "gross receipts great than or equal to \$100,000 <u>and</u> total assets greater than or equal to \$250,000 at the end of the year are required to file Form 990. Therefore, if an organization had total assets at the end of the year of \$1 million, but normally has gross receipts of \$80,000, they are not

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required to file for 990, but according to the instructions, they are not allowed to file Form 990-EZ as they do not have both normal gross receipts less than $100,000 and total assets at the end of the year of less than $250,000. Please clarify if an organization in this situation is required to file Form 990 or if they would be allowed to file Form 990-EZ.

3. Page 3 of the instructions does not clearly state that controlling organization described in IRC §512(b)(13) and supporting organizations described in IRC §509(a)(3) must file Form 990 regardless of size. This important exception from the general filing rules is buried in a "tip" about filing Form 990-EZ or Form 990-N. This information should be more clearly stated.

4. Page 6, item 15 of the instructions is unclear. This item should be deleted and the point regarding supporting organizations should be emphasized separately on page 3 of the instructions.

5. Page 8, accounting period change: There has been confusion in the past regarding changing an entity's accounting period using the simplified procedures and filing extensions. This would be a good opportunity to provide guidance to an organization who wishes to use the simplified procedures but cannot file by the original due date of the return.

6. Glossary term for independent contractor: Does the Service intend for the definition of "person" to be only payments made to individuals, or are business entities such as corporations included? The clarification is needed specifically for part II, Section B line 10a, which currently suggests only individuals should be listed on part 10a.

FORM 990 CORE FORM

7. Part I, Summary, Line 2, Three Most Significant Activities: There is insufficient space to describe three separate activities. This is very important information and the charities will abbreviate descriptions or reference to a statement explaining their activities. This will defeat the purpose of easy access of the information for the reader and should be removed from page 1.

8. Part I, Summary, Lines 11-24a, Efficiency Indicators of Financial Statements: The use of percentage efficiency indicators relative to the income statement and balance sheet information is inappropriate. The fundamental use of an income statement (a period of time) and a balance sheet (a snap shot picture in time) can be distorted analyzing only the end of year results. By including these percentages, it leads the reader to believe the IRS presumes there is a "good" or "bad" percentage. If the reader wants to compare and analyze the financial information, detailed data is located in the Form at the Statement of Revenue, Statement of Functional Expenses, and Balance Sheet areas. The percentage columns should be eliminated.

9. Part I, Summary, Line 8b, Compensation Metric: The percentage calculated compares total "program function" compensation of officers, directors and key employees to total "program expense". This focus will suggest to the reader that a high percentage is bad or inappropriate. There is no allowance for the charity to explain a high percentage. Further, the percentage is only comparing compensation that has been allocated to program expenditures. A charity will determine whether it is appropriate to functionalize compensation into management & general or fundraising. Further, key employees are included in this category. Not all charities will similarly record who the key employees are. This focused percentage can be manipulated. It would make more sense to review total compensation to total expenditures due to the expense functions inherent to a Form 990.

10. Part I, Summary, Line 19b, Fundraising Metric: The percentage calculated compares total fundraising expense to total contributions and grants. There is an underlying assumption to the reader that a lower percentage is better. This percentage completely ignores IRC Section 509(a)(2) organizations. Such organizations may receive little contributions but incur fundraising costs which are disproportionate compared to IRC §509(a)(1) organizations. A more reasonable percentage could be computed if program revenue was included in the denominator. The Service should allow organizations to report this percentage over a three to five year period, permit the charity to explain high percentages, or eliminate the question in its entirety.

11. Part I, Summary, Line 24b, Total Expenses as a Percentage of Net Assets: This percentage calculation has no value. It gives the reader the presumption that there is a "good" or "bad" percent. Organizations will vary as to whether they are setting aside funds to expand programs or purchase assets, or are currently spending those reserves. Without looking at the Form 990 as a whole, this percentage is misleading.

12. Part II, Section A, Line 1a, Column (B): We appreciate the clarification that individuals reported under the former column are limited to a prior five year Form 990 look back.

13. Part II, Section A, Line 1a, Column (C): We disagree with the change to indicate whether the individual was full time versus the number of hours devoted to the position. When indicating the number of hours, the users of the Form 990 can estimate an hourly rate and assess whether the compensation paid appears to be reasonable or not. With only an indication of full time or not, that assessment is more difficult without requesting information from the organization. For example, one organization's CEO may work 40 hours and be paid reasonable compensation for time and skills provided, while another organization's CEO may work 60 hours and be paid reasonable compensation for their time and skills provided. Both organizations would check the "full time" box, but compensation could be significantly different.

14. Part II, Section A, Line 1a, Column (D): If it is the intention of the IRS that the information for this section be reported is on a calendar year basis, the instructions

should affirmatively note that this may be a deviation from the organization's adopted fiscal year and therefore not agree to part V, line 5.

15. Part II, Section B, Line 3: Rather than listing out positions by title, a reference to key employees might be more appropriate to capture people who are key employees but use a different title than those noted in the question.

16. Part II, Section B, Line 5c - 5e: The qualification that the transaction exceeds $5,000 should be noted in the questions and not buried in the instructions. The instructions could continue to emphasize that transactions less than $5,000 do not require disclosure.

17. Part II, Section B, Line 8: The definition of reportable or other compensation includes nontaxable fringe benefits which might be difficult to calculate. De minimis fringe benefits are nontaxable because accounting for them may be considered an administrative burden. Requiring a computation for disclosure in Section B should not be material to the reportable compensation and would be difficult to compute.

18. Part III, Line 3b: Most organizations don't tabulate the number of transactions that might have been reviewed because they potentially cause a conflict. In addition, many organizations err on the conservative side and discuss transactions that don't necessarily present a conflict of interest but could potentially be viewed as such. The effort to tabulate and report this data exceeds the usefulness of the information and may give a misleading picture of the organization. A suggested rewording to this question would be "if "yes", are members of the governing body required to review the policy for conflicts at least annually?" This should accomplish the Service's desire to know that the policy is considered in decision making without requiring additional work on the organization's part to gather additional specific information.

19. Part III, Line 10: There is no guidance in the instructions to whom or how many of the governing body must review the Form 990 before it is filed. Does this imply that the finance committee should review or the entire board of directors? Would a key person of organization management qualify? It is generally not practical for the full board to review the Form 990 before it is filed, but it is customary to have at least one key employee who is responsible for the form review a draft prior to filing.

20. Part IV, Line 10d: This line is misleading by saying, "net gain or loss from investments," when sale of other assets, including disposed fixed assets, have to be shown on this line.

21. Part VII, line 8: No definition is provided for "substantial", which leaves the question open to interpretation by the return preparer. Guidance should be provided for consistency among organizations.

22. Part VII, line 11 and 12: The phrasing of these questions does not consider non-written policy and practice of the organization. Organizations are not required to

have these policies in writing; it seems these questions are in the draft form to force organizations to adopt written policies that are not required, or may not apply to the organization (i.e., one who does not have investments or participate in disregarded entities).

23. Part VIII, question 8b: Form 990-T is required if gross receipts are over $1,000, so question 8b is redundant. Instead, question 8 should add the sentence "If yes, complete Form 990-T." and 8b should be removed.

24. Part IX, question 2: Many organizations do not have one most significant program, but several. We are not clear why line 2 is needed when line 3 is available. It seems the activity described in part IX line 2 would also be described on line 3 as the total for line 3, column B must equal total program expenses on part V.

25. Part IX, line 3: What is the "activity code"? Guidance is not provided in the instructions. This likely would not be helpful to a user of the form as sufficient detail is entered on the line to explain what the activity is. Also, given the vast array of programs exempt organizations participate in, it is unlikely the Service could develop a reasonable comprehensive list.

SCHEDULE A: SUPPLEMENTAL INFORMATION FOR ORGANIZATIONS EXEMPT UNDER SECTION 501(C)(3)

26. Part I, line 11f: Until recently, the IRS has not specified the supporting organization type on the determination letters. Therefore, most organizations will be forced to check "no" to this question, which is misleading for readers of the forms. We suggest that this question be removed. If the question is left on the form, is the Service prepared to timely respond to the requests for this information?

27. Part II heading: The heading should specify (as it does on part III) that this schedule should be completed on a cash method of accounting.

28. Instructions for part II and III should again clarify that these sections are to be completed on the cash method of accounting.

29. Unusual Grants: Nowhere on the Schedule A does it refer to the new schedule required pursuant to the instructions for unusual grants. We recommend adding back in the line currently on Schedule A at the bottom of Part IV-A to the draft at the bottom of part II and III so return preparers are alerted to the new statement requirement. Another option is for line 1 of part II and III could refer to the instructions regarding unusual grants.

Schedule B: Schedule of Contributors

30. The instructions are unclear on how to treat donors who give both cash and noncash contributions who, when added together, have donated over the dollar threshold required to be reported on Schedule B. Clarification on reporting in these situations would be appreciated. Also, clarification of whether this schedule should be prepared on the cash or accrual method of accounting would assist return preparers. If the schedule is to be prepared on the accrual method, it would be helpful for the instructions to include examples of how to reconcile the GAAP reporting rules to the actual contribution received.

Schedule D: Supplemental Financial Statements

31. Part I – Many large exempt organizations have developed investment plans using a combination of different types of alternative investments. While this is not "secret", the specific approaches the advisors use are considered proprietary information. It would be beneficial to allow the exempt organizations to aggregate investments by type for this purpose.

32. The Service has specifically requested feedback on Schedule D regarding whether the aggregation of balance sheet disclosures in this manner works. We believe this schedule will eliminate much of the "white paper" statements that were previously filed and likely will increase compliance with the requirements to provide this information which have been overlooked in the past.

33. Part VII – This section requests the text of the footnote to the organization's financial statements that reports the organization's liability for uncertain tax positions under FIN 48. Many organizations do not issue GAAP financial statements, and therefore this question would not apply. For those that do issue GAAP statements, the footnote would likely be too large to fit on this line, causing another required attachment which defeats the purpose of this schedule. Additionally, the financial statements are not open to public inspection. This question effectively makes this part of the financial statements public. Most users of the return will not understand the footnote and mechanics of FIN 48, so the question fights against the Service's desire for transparency by including confusing information. The Overview of the Schedule D says the Service has determined that the Form 990 should indicate if an organization disclosed any uncertain tax positions in their financial statements. The question should be changed to simply ask if there is a FIN 48 footnote in the organization's financials, but should not ask for that footnote to be included in the Form 990 filing.

34. Part VIII, line 5: Most organizations who hold conservation easements do not currently track staff hours devoted to monitoring and enforcing conservation easements or expenses incurred in that monitoring and enforcing process. Requesting a number of staff hours and dollar figure of expenses increases the compliance burden on organizations holding easements. Question 7 should be a sufficient answer to the

Service regarding the monitoring of easements and compliance with rules involving those easements.

35. Part X, line 3: In many cases, the footnote would likely be too large to fit on this line, causing another white paper attachment which defeats the purpose of this schedule. In the volumes of information requested on the draft Form 990, this request is insignificant and should be removed. The financial statement is not open to public inspection, and this request effectively makes this part of the statement open. An organization should have the option to make their statement public information, not be forced to due to the Form 990 questions which do not accomplish a meaningful purpose. The Overview of the Schedule says this information is requested because the Service is concerned that the full financial status of the organization is not reflected due to SFAS 116. The question could be rephrased to request detailed information about any collections that are excluded from the balance sheet due to the difficulty of valuing the collection.

36. Part XII: The Service is requesting comments on alternatives to improve transparency of the organization's accumulation of endowment fund assets. The instructions to the Schedule do not request information regarding endowment fund assets held through related organizations; this information should be reported on the related organization's Form 990 and therefore should not be required here. A suggestion to improve transparency and completeness of information would be to add a few lines where the organization can explain the intended purpose of the endowment funds.

37. Part XIV and XV: The instructions for this reconciliation to the audited financial statements of the organization should provide guidance for organizations that file consolidated financial statements but separate tax returns. Without guidance on the starting point to use, similar organizations could have very different starting points and adjustments to arrive at the revenue and expenses reported on the return. Without guidance, some organizations will start with separate entity revenue and expenses in supplemental schedules, while others will be required to start with the consolidated revenue and expenses when supplemental schedules by company are not provided in the financial statements.

SCHEDULE F: STATEMENT OF ACTIVITIES OUTSIDE THE U.S.

38. Part I: The space provided will not be sufficient to answer the questions asked, which will result in additional white paper schedules not previously required.

39. Part I: For organizations with substantial overseas activity, accumulating the number of employees or agents by country will be onerous without providing substantial additional transparency. We recommend removing this column from the required information as the total expenditures, number of accounts or offices and a description of activities is sufficient information without causing a large amount of additional work in collecting the information.

40. Part II and III: We cannot see how the manner of cash disbursement adds transparency to the report. Organizations generally use the same method of transmitting grant funds for the majority of grant recipients, so requiring them to find the exceptions to these general methods would entail unnecessary additional work without providing substantial additional transparency in reporting. We recommend these columns be removed from part II and III.

SCHEDULE G: SUPPLEMENTAL INFORMATION REGARDING FUNDRAISING ACTIVITIES

41. Part I, question b: The wording of this question is unclear. We suggest the question be rephrased to say "Did the organization have a written or oral agreement with any individual or organization to conduct fundraising activities on behalf of the organization?"

SCHEDULE I: SUPPLEMENTAL INFORMATION ON GRANTS IN THE U.S.

42. Part II: The organizations are currently not required to request the EIN of grant recipients. Requiring organizations to collect and report this information is an additional unnecessary burden on the filing organization which should be eliminated from this schedule.

43. Part III: The number of recipients of a type of grant or assistance is requested in column (b). For organizations who may have small dollar amount of grants with many recipients, requiring them to track the number of recipients is a burdensome task.

SCHEDULE J: COMPENSATION INFORMATION

44. The Service has requested comments on the thresholds for Schedule J and if they are appropriate. Based on the thresholds of the core form, part II, Section B, questions 6 through 9, we agree that it would be unlikely that a small organization would be required to complete Schedule J. The only exception would be small organizations who have payments to former directors or trustees in their capacity as former directors or trustees who receive more than $10,000 in reportable compensation. The Service might consider raising that $10,000 threshold in the part II, Section B, line 6 phrasing of the question.

45. Form 990 is a public document and contains sensitive personal information regarding key employee compensation on Schedule J, line 1. As long as the organization is meeting the provisions outlined in the core form, part II, Section B, line 3, this additional breakdown provides unnecessary disclosure of details of the organization's compensation plan.

46. Supplying the information required for line 1 is an overwhelming task for typical nonprofits. For example, column d requires a dollar amount be assigned to nontaxable benefits. De minimis fringe benefits are nontaxable because accounting for them may be considered an administrative burden. Requiring a computation for disclosure in Section B should not be material to the reportable compensation and would be difficult to compute. The time needed by the organization to capture and compute this value far exceeds the value to the public of disclosing the information.

47. Question 3 is unduly prejudicial. The question suggests that the organization cannot pay or reimburse for first-class travel, club dues, or use of a personal residence, or by checking "yes" will result in additional scrutiny from the IRS or the public. It does not ask the further question if the personal use portion of the reimbursements were included in the employee's compensation, or if these expenses are a requirement of the organization (i.e., a president of a University who is required to live on campus) rather than a preference of the employee. These further questions would clarify the actual situation, rather than simply make the organization look on the surface that they are misusing organization funds. We would be interested to know the rationale behind asking this questions, and if the question remains, what the IRS intends to do with the "yes" answers.

48. The instructions for line 4(a) need to clarify if the "revenue" referred to is net of expenses or gross revenue.

SCHEDULE M: NON-CASH CONTRIBUTIONS

49. <u>Part I, Lines 4, 5, and 6:</u> Many exempt organizations receive household goods and clothing in large quantities as part of their program activities. To require them to track the quantity of the items received does not give the Service or the public any useful information. Some provision should be made that would not require these organizations to incur this substantial burden.

We thank the Service for their willingness to listen to the comments from the exempt organization community. While we understand the concern raised by the legislative branch, most people would acknowledge the exempt community is a valuable and worthwhile segment of our society. We do not feel the community should be judged based on the lowest common denominator. Many of the proposed changes to Form 990 will increase the administrative cost to make modifications to the organization so it "appears" better in how the questions are completed. It will most certainly increase the cost to prepare the revised 990, both of costs to the professional and time it takes to work with the professional. This could have a significant negative impact on many of the smaller organizations and could result in diverting needed funds away from program services. This is directly opposite what the public is asking for with the push toward transparency. We ask the Service to be cognizant of the additional burden these proposed changes could cause and evaluate whether the changes truly allow the Service to better enforce the Internal Revenue Code, or if it would just be nice to have.

Sincerely,

Paul D Keller

Moss Adams LLP by
Paul D. Keller, CPA
Partner

From:	Chip Nielsen
To:	*TE/GE-EO-F990-Revision;
CC:	
Subject:	Redesigned Form 990
Date:	Friday, September 14, 2007 7:38:25 PM
Attachments:	Memo re Draft Form 990 Question 75(c) v2.doc

Thank you for considering our comments on this matter.

Chip Nielsen

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September 14, 2007

VIA EMAIL ONLY

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

FROM: Chip Nielsen

RE: Draft Form 990 Question 75 (c)

Introduction

This comment specifically addresses the instructions the IRS will be providing to those entities required to file Form 990 that form as non-profit organizations solely to conduct a ballot measure campaign in a state that permits voter initiatives and referendum.

A ballot measure committee is a unique campaign organization in United States tax law. Unlike candidate campaign committees, a ballot measure organization cannot enjoy tax-exempt status under IRC 527.

When a corporation, labor union or trade association decides it will support or oppose an initiative or referendum ballot measure, it often learns (1) that it must first open a separate bank account for reporting campaign requirements imposed by state law, (2) the bank will not open such an account without an IRS EIN number, and (3) that the EIN application does not have a category for ballot measures. As the IRS has recognized in its "Election Year Issues" publication, ballot measure organizations therefore typically file for a letter of determination under IRS 501(c)(4). Once granted, among other obligations, the organization is required to file Form 990 and answer Question 75(c).

This submission suggests that for such a registered and sponsored "ballot measure committee," that satisfies certain IRS prescribed criteria, as suggested below, the answer to Question 75(c) should be "No."

History

For almost 30 years, this law firm routinely organizes such ballot measure committees and seeks and receives tax-exemption as a social welfare non-profit organization. Such organizations simultaneously comply with the California campaign finance disclosure laws, and after an election, we prepare and file IRS Form 990, disclosing much less information then already disclosed on these campaign reports.

With the IRS' new concern about "related organizations," the new instructions to Question 75(c) seemed to ask at least some such entities to disclose the corporate, union or trade association salary of whatever executive who is assigned to the non-profit board to oversee the campaign. In states like California, the campaign disclosure laws already require the identification of "sponsors" of ballot measure committees on their Statements of Organization, sometimes even in the name of the committee itself, and often on disclaimers for its campaign advertising.

For such sponsored committees, the individual representing the sponsors may be the senior executive of the corporation, union or trade association or they may be one or more vice presidents of governmental affairs office, or both. We have never represented a ballot measure committee that paid a sponsored organization's executive compensation for serving on the non-profit board.

Question 75(c) is Currently Ambiguous

The current understanding of what is sought when both related organizations and social welfare non-profits become sources of income to certain individuals is not relevant where a ballot measure non-profit board member is not compensated. Consequently, it is difficult for us to understand any public purpose to compel disclosure of an executive's salary for his or her “day job” just because that person serves on the non-profit ballot measure board as the sponsor's representative for the campaign. It seems even less relevant to force disclosure of this private salary information if the person is a vice president of governmental affairs for a corporation, union or trade association.

Notably, IRC 527 recognizes the futility of over disclosure for political campaigns by exempting “qualifying” organizations with sufficient state campaign filing obligations.

Recommendation

We recommend that Form 990 instructions recognize that the appropriate answer to Question 75(c) is "No" when (1) the filer is a registered ballot measure committee that, (2) receives no funds, expends no funds and conducts no activities other than campaigning for or against an initiative or a referendum, (3) where the "related organization" sponsorship is identified publicly under the campaign finance laws, or voluntarily disclosed on campaign documents, (4) where the applicable board director is not compensated by the campaign committee, and (5) the board director is handling that responsibility as a representative of the "related organization."

We appreciate your consideration of these comments, and we thank you for the opportunity of providing them.

VGN/cll

From: Alua Arthur
To: *TE/GE-EO-F990-Revision;
CC:
Subject: Draft Form 990 Comments
Date: Friday, September 14, 2007 8:10:06 PM
Attachments: Draft Redesigned Form 990 comments.doc

To Whom It May Concern:

Attached, please find the comments of the Legal Aid Foundation of Los Angeles regarding the Draft Redesigned Form 990. If you have any questions or concerns, please feel free to contact me at the contact numbers listed below.

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Writer's Direct Dial Number

Our File Number

September 14, 2007

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

Internal Revenue Service
Form 990 Redesign
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Dear Ms. Lerner, Mr. Schultz, and Ms. Livingston:

In our capacity as the largest legal aid organization in California, the Legal Aid Foundation of Los Angeles (LAFLA) respectfully submits the following comments in response to your request of June 14, 2007, regarding the draft Form 990 and accompanying schedules, currently scheduled to be released in final form in 2009, for the 2008 return filing year.

LAFLA is the frontline law firm for low-income people in Los Angeles. LAFLA is committed to promoting access to justice, strengthening communities, combating discrimination and effecting systemic change through representation, advocacy, and community education. The Community Economic Development (CED) unit aims to empower Los Angeles communities and community-based organizations in their efforts attack poverty at its roots. Our emphasis is working with emerging and community based nonprofits.

Your agency's guiding principles behind the redesign – to enhance transparency, promote tax compliance, and minimize the burden on filing organizations – are sure to be appreciated by the public. However, we do not believe that the draft form released in June adequately addresses these principles. Some of the most problematic areas include: (1) new methods for reporting financial information, which could affect audits and maintenance of nonprofit financial records and create an administrative burden; (2) schedules that include information that many nonprofit currently prepare separately and attach to the Form 990; (3) the inclusion of several ratios, including fundraising efficiency ratios and executive compensation ratios, on a summary page; (4) the requirement to report on "best practices" that aren't legal requirements and (5) new methods for reporting compensation of staff and board members. It is unclear whether these additional requirements will actually increase transparency, while it is very probable that the expanded form will not only increase organizations' recordkeeping and information-gathering burdens, but may actually promote greater noncompliance, as organizations struggle to keep up with an ever-growing regulatory burden that diverts valuable time and resources away from the valuable core purposes and programs.

It is my understanding that the IRS seeks to introduce the new form in tax year 2008 (returns filed in 2009). This implementation schedule may cause problems for some nonprofits, since the new form will likely require many organizations to change their accounting systems and governance practices in a short amount of time.

METHODS FOR REPORTING FINANCIAL INFORMATION AND PROGRAM SERVICES INCREASE THE ADMINISTRATIVE BURDEN ON NONPROFITS

The redesigned Form 990 would require nonprofits to report their revenues and functional expenses differently than current practice. Many of the reporting categories on the new form are different from standard nonprofit accounting classifications and will require changes to the chart of accounts currently in use in the nonprofit sector. Specifically, the new form requires nonprofits to break down their contributions, gifts, and grants into categories of (a) federated campaigns, (b) outside fundraising or commercial co-ventures, (c) fundraising events, (d) related organizations, (e) government grants, (f) other gifts, grants, and contributions, and (g) noncash contributions.

Additionally, nonprofits would be required to identify a business code for each classification of program service revenue identified on the new Form 990, itemize functional expenses categorized as "other expenses", list new classifications of functional expenses, and follow Statement of Position 98-2 for allocation of fundraising expenses. Since most nonprofits follow general accounting classifications, these requirements are burdensome and time consuming, requiring nonprofit accountants to depart from traditional methods.

Under the new Form 990, nonprofits would be required to report direct revenue related to each of their three most significant program services. Currently, nonprofits report only program service expenses for each program service. Direct revenue would include only income from fees for services and sales of goods directly related to a program; it would not include other indirect revenue or in-kind contributions. This direct revenue figure could be misleading, particularly since it would appear next to the total program service expenses on the Form 990.

Furthermore, nonprofits would only be provided five lines to describe their three most significant program service accomplishments. Currently, nonprofits can submit attachments with more detailed information about their program services. Providing less information about program services may make the Form 990 less useful to the public, including donors, as they attempt to learn about the activities of nonprofits.

Lastly, the redesigned form would ask nonprofits to describe (in three lines) their most significant program service accomplishment for the year. This requirement may be difficult for nonprofits with a broad range of program services. Furthermore, we believe information about the organization's most significant program service accomplishments is essential to any public disclosure and the reader's understanding of whether an organization is meeting its exempt purpose. As this important information is minimized by its location on the last page of the core form, we recommend this information be moved up toward the beginning of the form.

Organizations large and small, charitable and non-charitable, will be forced to spend many additional hours gathering information for both the core form and the schedules. Consequently, the changes may require many nonprofits to revise their accounting systems and software. This will be especially burdensome for small organizations, especially those staffed chiefly by volunteers, whose resources are thin to begin with. It should be an objective of the IRS to promote work in this field rather than to dissuade it by imposing strict reporting requirements.

THE LENGTHIER FORM INCLUDES ADDITIONAL REPORTING INCREASING THE REGULATORY BURDEN

The draft Form 990 is significantly lengthier than the original. The draft redesign change includes a longer core form 10 pages as opposed to the current 9 due to a new first summary page. Furthermore, it adds 15 possible schedules as opposed to the current two and 36 possible attachments due to moving some of the information from the current 990 onto a schedule that requires more detailed information and additional information not previously required.

For example, for small nonprofits currently filing only a 990-EZ and Schedule A, the change will require filing a 990, if the 990-EZ is eliminated, a more detailed Schedule A-Supplementary Information for 501(c)(3) Exempt Organizations, and a new Schedule D-Supplemental Financial Statements. For those currently also filing a Schedule B-Schedule of Contributors because one or more donors annually gives $5,000 or more, the change will still require filing an unchanged Schedule B. For those receiving more than $5,000 annually in non-cash contributions, like those operating food and clothing banks, the change will also require filing the new Schedule M-Non-Cash Contributions.

One of your agency's goals in redrafting the 990 form is reduced regulatory burdens. However, additional reporting requirements through burdensome and complicated schedules increase the regulatory burden on your agency.

THE INCLUSION OF RATIOS AND COMPENSATION INFORMATION ON THE SUMMARY PAGE IS MISLEADING

We understand that the purpose of the Page 1 "Summary" section is to provide an overall "snapshot" of the organization. This is a useful and logical approach to Form 990 redesign, and LAFLA believes that the information presented in this section should be pertinent, important, consistent, and contextually accurate. The current draft summary page, however, appears to be more of a collection of disparate facts, rather than an overall cohesive picture of the reporting organization. Furthermore, the summary page calculates compensation and fundraising expense ratios that are grossly misleading, especially to the casual Form 990 reader.

While your agency has emphasized that there are no "correct" ratios for nonprofits, the inclusion of these ratios in the summary page may lead to misleading inferences (both positive and negative) about the practices of many nonprofits. For example, for small nonprofits, the compensation of key employees may be very high relative to program services expenses. Also, a nonprofit undertaking an endowment program or major fundraising initiative during a year may have particularly high percentages for several of these ratios involving fundraising expenses for that year.

Specifically, Question 7 asks for the highest compensation amount reported in Part II. It provides salary information completely out of context with the rest of the organization, its size, mission, revenues, and programs. Providing a single compensation figure out of context is utterly misleading. Since compensation for the executive director, typically the highest compensated employee, is required in Part II of the core form, LAFLA recommends this question be eliminated from the summary page.

Similarly, Questions 8b, 19b, and 24b calculate "metrics" or percentage ratios that purport to measure certain organizational efficiencies. These ratios are arbitrary; furthermore, they are neither accepted nor used in any segment of the nonprofit world. Furthermore, because of the vast diversity of organizations required to file the 990, any attempts to use these metrics to compare one organization with another -- even similar organizations -- would yield highly unreliable results. Examples:

- An organization's fundraising efforts are not necessarily constant from year to year. In the initial years of a fundraising campaign, the "investment" (fundraising expenditure) is usually fairly large, compared with contributions actually received. A young exempt organization might end up being unjustly penalized by a meaningless, but unfavorable, ratio, because the unsophisticated donor will avoid contributing to it. And, as a single year's ratio is relatively meaningless and could be confusing, it might also be useful to have an organization disclose, on that schedule, fundraising expense information for a period of several years.

- The executive compensation ratio provides no useful information whatsoever, as it fails take into account organization size and complexity. In a small-staff organization, the CEO might be only one of a handful of employees, or may even be the sole employee. His or her compensation could, accordingly, constitute a significant portion of overall expense. Without the proper context, the casual Form 990 reader is likely to merely latch onto the reported ratio and look no further, even to other possibly clarifying information on the summary page.

LAFLA firmly suggests that all "efficiency metrics" or ratios be removed from the Form 990, as they will merely take the place of thoughtful evaluation on the part of Form 990 readers -- especially the media, potential donors, and grantmakers.

THE DRAFT FORM 990 REQUIRES REPORTING ON GOVERNANCE PRACTICES WHICH ARE NOT LEGAL REQUIREMENTS(Part III)

The revision of Form 990 would change the way nonprofits report on their policies, operations, and governance practices in several important ways. While LAFLA believes, as IRS does, that a well-governed organization is one that is compliant, LAFLA nevertheless feels that these questions are not appropriate for Form 990 reporting, nor do they accurately reflect a complete governance picture. This focus on governance issues - typically issues which are not covered by any section of the tax code - continues throughout the draft form. For example, nonprofits would need to identify whether they have an audit committee, whether they keep contemporaneous records of board and committee meetings, and whether (and how) they make audit reports, financial statements, and conflict of interest policies available to the public.

Additionally, nonprofits would be asked to report the number of transactions reviewed under their conflict of interest policies each year. This information can be misleading, and it does not necessarily reflect best practices, whereas it might be more useful for nonprofits to report whether they require officers, directors, and key employees to disclose their financial and organizational interests each year.

The governance practices implied by these questions are not necessarily appropriate for all of the vastly different types organizations required to file a 990. Some of the practices suggested by the questions are, frankly, impractical. Additionally, not all documents listed in Question 11 are required to be disclosed, and LAFLA is concerned that a "no" answer may have negative implications, creating a *de facto* standard where none should exist.

<u>THE COMPENSATION REPORTING REQUIRED BY THE DRAFT FORM 990 IS MMISLEADING AND MAY BE AN INVASION OF PRIVACY</u> (Part II and Schedule J)

LAFLA firmly supports the concept of transparency, including disclosure of compensation for officers, directors, and key employees. Nevertheless, we are greatly concerned over the extensive compensation reporting required by the new Form 990.

Additionally, compensation figures are to be taken from W-2s or 1099s. While this will make compensation reporting simpler and more consistent, these figures may be misleading, since they represent calendar year compensation (whereas many nonprofits have fiscal years that are different than the calendar year). Also, this could make the key executive compensation ratio from the summary page meaningless, since it may be a ratio of calendar year compensation and fiscal year program services expenses.

Moreover, LAFLA is troubled by the new Form 990's disclosure of the city and state of residence for every person listed in Part II, Section A. Because the Form 990 is available to anyone over the Internet via Guidestar (and possibly other online venues, as well), the disclosure of this information could lead to privacy invasion, or even outright identity theft. In public comments, you have indicated that knowing the physical location of these individuals is meaningful for 990 reporting purposes. However, LAFLA suggests that providing the member's state of residence, rather than city and state, would accomplish the same purpose, and would constitute a far lesser invasion of privacy. Ideally, we request that the organization's address continue to be an alternative for this reporting purpose.

LAFLA believes that transparency, compliance, and reduced regulatory burdens benefit both nonprofit organizations and the communities they serve. LAFLA does not believe that the current draft effectively addresses these principles. We strongly suggest that your agency properly formulate a revised Form 990 that will indeed accomplish these stated goals of the IRS *without* unintended consequences and increased burden on the filing community.

To that end, we strongly suggest that your agency solicit and accept further comment on the Form 990 once changes are made. Understandably, this will delay the introduction of the new form until the 2009 tax year (returns filed in 2010). However, this time extension will be necessary for the small nonprofit organizations that will need to revamp their accounting methods to adapt to the new reporting requirements.

Sincerely,
/s/
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