UNDERSTANDING THE NEW FORM 990

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After years of discussion at the Internal Revenue Service (the "IRS") and among exempt organizations, the IRS unveiled the final draft of its new Form 990 – the information tax return most exempt organizations must file with the IRS each year – late last year. On August 19, 2008, the IRS issued a nearly finalized set of instructions that will accompany the form. The purpose of this presentation is to provide an overview of the new Form 990 and highlight the new provisions that likely will impact the day-to-day operations of fraternity and sorority foundations.

I. <u>New Form 990: General Background</u>

A. <u>What</u>. As noted above, Form 990 is the information tax return that most tax exempt organizations, including fraternity and sorority foundations, must file with the IRS each year.

B. <u>When</u>. Form 990 is due each year by the fifteenth day of the fifth month following the close of the exempt organization's tax year. The new Form 990 will begin being filed in 2009, for the 2008 tax year. To ease smaller organizations' compliance burden, the IRS has provided for a three-year phase-in of the new Form 990.

- **Tax Year 2008 (filed 2009)**: Organizations with gross receipts of less than $1 million <u>and</u> assets of less than $2.5 million may file Form 990-EZ rather than the new Form 990.

- **Tax Year 2009 (filed (2010)**: Organizations with gross receipts of less than $500,000 <u>and</u> assets of less than $1.25 million may file Form 990-EZ rather than the new Form 990.

- **Tax Year 2010 (filed 2011)**: Organizations with gross receipts of less than $200,000 and assets of less than $500,000 may file Form 990-EZ rather than the new Form 990.

- **Note Regarding Form 990-N (e-postcard)**: Organizations with gross receipts of less than $25,000 may file Form 990-N, which is an electronic postcard filing that requires much less information than Form 990 or Form 990-EZ. The IRS has announced that it will raise this $25,000 threshold to $50,000 beginning in tax year 2009 (filed 2010).

- **Fiscal Year Organizations**: Organizations with fiscal years ending in 2008 may file the 2007 Form 990 rather than the new 2008 Form 990 for the short year ending in 2008.

- **Form 990-EZ Changes**: No major changes have been made to Form 990-EZ. The form had to be updated in some respects, because it utilizes the same Schedules A and B as the old Form 990, and those Schedules A and B have been revised with the new Form 990.

C. Why. The last time the IRS completed major revisions to Form 990 was in 1979. The IRS has recognized that the current form has failed to keep pace with changes in the law and tax exempt sector, has failed to meet IRS tax compliance interests, and has failed to meet transparency and accountability needs of states and the public at large. Accordingly, the IRS embraced three guiding principles in its preparation of the new Form 990: enhancing transparency, promoting tax compliance, and minimizing the burden on filing organizations.

II. Structure of New Form 990. The new Form 990 consists of an eleven page "core form," plus sixteen schedules designed to require reporting of information only from those organizations that conduct particular activities (*i.e.*, organizations need only file those schedules applicable to their activities).

A. Core Form. The "core form" portion of the new Form 990 is structured as follows:

Part I: Summary
Part II: Signature Block
Part III: Statement of Program Service Accomplishments
Part IV: Checklist of Required Schedules
Part V: Statements Regarding Other IRS Filings and Tax Compliance
Part VI: Governance, Management, and Disclosure
Part VII: Compensation of Officers Directors, Trustees, Key Employees, Highest Compensated Employees, and Independent Contractors
Part VIII: Statement of Revenue
Part IX: Statement of Functional Expenses
Part X: Balance Sheet
Part XI: Financial Statements and Reporting

B. The Sixteen Schedules. The sixteen schedules of the new Form 990 represent a major change from the old form. The old Form 990 has only two schedules: Schedule A ("Organizations Exempt Under Section 501(c)(3)") and Schedule B ("Schedule of Contributors"). The IRS has explained that the new form's sixteen schedules are designed, in part, to reduce the burden of filing organizations: Much of the information required by the new schedules was required by the old Form 990, but the old form was less user-friendly in that it requested that such information be provided in unstructured attachments to be created by the filing organization. The new schedules should assist organizations in providing all required information, and they should assist the public and others who review filed Forms 990 by ensuring that such information is reported in a consistent order and format. The sixteen schedules are:

Schedule A:	Public Charity Status and Public Support
Schedule B:	Schedule of Contributors
Schedule C:	Political Campaign and Lobbying Activities
Schedule D:	Supplemental Financial Statements
Schedule E:	Schools
Schedule F:	Statement of Activities Outside the United States
Schedule G:	Supplemental Information Regarding Fundraising or Gaming Activities
Schedule H:	Hospitals
Schedule I:	Supplemental Information on Grants and Other Assistance to Organizations, Governments, and Individuals in the United States
Schedule J:	Compensation Information
Schedule K:	Supplemental Information on Tax Exempt Bonds
Schedule L:	Transactions with Interested Persons
Schedule M:	Non-Cash Contributions
Schedule N:	Liquidation, Termination, Dissolution, or Significant Disposition of Assets
Schedule O:	Supplemental Information
Schedule R:	Related Organizations and Unrelated Partnerships

III. Part-by-Part Overview of New Form 990 – Core Form

A. Part I, Summary

- Opening portion of new Form 990 collects basic information not collected on old Form 990:
  - Gross Receipts
  - Type of Organization (corporation, trust, association, other)
  - Year of Formation
  - State of Legal Domicile

- "Part I, Summary" provides a snapshot of key governance, operating, and financial information. This one-page overview will enable members of the public and others to obtain some of the most important information about the organization in one quick glance.

  Information requested in the Summary section includes:

  - Number of voting members of the governing body
  - Number of independent voting members of the governing body
    - Meaning of "independent"? See discussion of Part VI below.
  - Total number of employees
  - Total number of volunteers
    - Volunteers include part time and full time individuals who volunteered during the year.
    - Filing organization may use any reasonable basis to estimate the number of volunteers.
  - Basic financial information

B. Part II, Signature Block. The signature block previously appeared on the last page of old Form 990. In keeping with the "snapshot" of essential information that page 1 of the new Form 990 now provides, the signature block has been moved to the bottom of page 1 of new Form 990.

C. Part III, Statement of Program Service Accomplishments

- IRS intentionally placed this section at the beginning of form so the filing organization can "tell its story" before reporting other information
- More space to describe organization's mission
- Provides opportunity to identify changes in programming from prior year

D. Part IV, Checklist of Required Schedules

- Part IV contains 37 "trigger" questions, the answers to which should tell an organization which schedules it must complete.
- Much of the information that is required by these trigger questions and the new schedules was required by old Form 990, however, old Form 990 did not provide the prescribed schedules on which to report such information.

E. Part V, Statements Regarding Other IRS Filings and Tax Compliance

- Part V contains a new set of questions that did not appear on old Form 990. These questions, which relate to other types of tax and reporting, are designed to (i) alert the filing organization to other federal tax compliance and filing obligations and (ii) collect important federal tax compliance information in one place.

- Issues covered by Part V include:

    - Employee Withholding and Employment Taxes

    - Unrelated Business Taxable Income and Related Form 990-T

    - Activities in Foreign Countries and Related Filing Requirements

    - Prohibited Tax Shelter Activities and Related Filing Requirements

    - Solicitation of Charitable Contributions and Related Record-Keeping, Filing, and other Requirements

    - Questions Gauging Compliance with Requirements Applicable to:

        - Organizations maintaining donor advised funds

        - Code section 501(c)(7) organizations (such as fraternities and sororities)

F. Part VI, Governance, Management, and Disclosure. Part VI of new Form 990 requires the disclosure of a significant amount of information that previously was not requested on old Form 990. Information requested by Part VI includes:

- Overall Number of Directors

- Number of Directors who are "Independent"

    - Meaning of "independent"? The August 19, 2008, draft instructions define an "independent" director as a person to whom all three of the following circumstances apply:

        - The person was not compensated as an officer or other employee of the organization or of a related organization.

        - The person did not receive total compensation or other payments exceeding $10,000 for the year from the organization or from related organizations as an independent contractor, other than reimbursement of expenses or reasonable compensation for services provided in the capacity as a member of the governing body.

        - Neither the person nor the person's family members were involved in either (i) a transaction with the organization that is reportable on Schedule L (transactions with interested persons) or (ii) a transaction with a related organization that would be reportable on Schedule L if filed by the related organization.

- Existence of any family or business relationships among officers, directors, trustees, or key employees

    - "Family Relationship" includes a person's spouse, ancestors, brothers and sisters (whether whole or half blood), children (whether natural or adopted), grandchildren, great grandchildren, and spouses of brothers, sisters, children, grandchildren, and great grandchildren.

    - "Business Relationship": a business relationship between two people includes the following: (i) one person is employed by the other in a sole proprietorship or by an organization with which the other is associated as a trustee, director, officer, key employee, or greater-than-35% owner, (ii) one person is transacting business with the other, directly or indirectly, in one or more contracts of sale, lease, license, loan, performance of services, or other transaction involving transfers of cash or property valued in excess of $5,000 in the aggregate during the tax year (indirect transactions are transactions with an organization with which the one person is associated as a trustee, director, officer, key employee, or greater-than-35% owner), and (iii) the two persons are each a director, trustee, officer, or greater than 10% owner in the same business or investment entity.

      The August 19, 2008, instructions add two exceptions to the term "business relationship": an "ordinary course of business exception," which requires the transaction to be on the same terms as are generally offered to the public, and the "privileged relationship exception," which includes one of three privileged relationships (attorney / client, medical professional / patient, and priest / clergy or penitent / communicant).

- Whether the organization delegated control over management duties customarily performed by or under the direct supervision of officers, directors, or trustees, or key employees to a management company or other person

    - "Management duties" for purposes of this question, according to the draft instructions, include hiring, firing, and supervising personnel; planning or executing budgets or financial operations; or supervising exempt operations or unrelated trades or businesses of the organization.

- Whether minutes of various meetings were taken

- Whether the organization has local chapters, branches, or affiliates, and if so, whether it has policies and procedures governing their activities to ensure their operations are consistent with the organization's operations

    - According to the draft instructions, a local chapter, branch, or affiliate would include an organization (regardless of whether such an organization is a separate legal entity) over which the filing organization has legal authority to exercise supervision and control.

- Whether a copy of the completed Form 990 was provided to the organization's governing body before it was filed

    - All organizations must describe, in Schedule O, the process through which the organization's officers, directors, trustees, board committee members, or management reviewed the form (or state "no review was conducted" if no such review took place).

- Whether the organization has a written conflict of interest policy, and if so, whether the organization (a) requires annual disclosure of potential conflicts by directors, officers, key employees and (b) regularly monitors and enforces compliance

- Whether the organization has a written whistleblower policy

- Whether the organization has a written document retention and destruction policy

- Whether the organization followed specific processes and procedures when it set compensation for the CEO, Executive Director, or other person who is the top management official; such procedures include:

    - Review and approval by independent members of the governing body or compensation committee

    - Use of data as to the comparable compensation for similarly qualified persons in functionally comparable positions at similarly situated organizations

    - Contemporaneous documentation and recordkeeping with respect to the deliberations and decisions regarding the compensation arrangement

- Whether the organization participated in any joint ventures or other similar arrangements

G. <u>Part VII, Compensation of Officers, Directors, Trustees, Key Employees, Highest Compensated Employees, and Independent Contractors</u>

- As was true for public charities completing old Form 990, compensation information must be disclosed for the organization's officers, directors, trustees, and key employees, and also five highest compensated employees that are paid more than $100,000 per year and that are not also an officer, director, trustee, or key employee.

    - Note: The IRS increased the dollar threshold for who will constitute a "highest compensated employee." Before it was $50,000; now it is $100,000.

- Note: According to the draft instructions, a key employee is an employee of the organization who: (1) had reportable compensation exceeding $150,000 for the year (the $150,000 test), (2) had or shared organization-wide control or influence similar to that of an officer, director, or trustee, or managed or had authority or control over at least ten percent of the organization's activities (the "Responsibility Test"), and (3) was within that group of the organization's top twenty highest paid employees for the year who satisfied both the $150,000 test and the Responsibility Test (the "Top 20 Test").

- Amount to be reported by the organization is the amount reported on Forms W-2 or 1099

  - This is a change (formerly, there was no reference to the W-2 or 1099 amounts) that is aimed at reducing the subjectivity in reporting executive compensation, which should assist the IRS and the general public in examining executive compensation.

  - The IRS did include a column for "other" income to be reported, however, so that other types of compensation, such as contributions to retirement plans, health and welfare benefits, etc., are reported for a more complete picture of compensation packages for those who use Form 990 to assess compensation comparability across different types of organizations. Because valuing certain fringe benefits can be extremely difficult, the IRS has included a provision in the instructions that allows organizations to estimate "other compensation" for purposes of this column.

  - Note: W-2 and 1099 amounts are reported on a calendar year (rather than fiscal year) basis. Because new Form 990 requires that compensation be reported in W-2 and 1099 amounts, fiscal year organizations no longer may report their compensation on a fiscal year basis. Fiscal year organizations will continue to be required to use fiscal year reporting, however, to report aggregate compensation on the statement of expenses.

- This Part VII includes three "trigger" questions, the answers to which could require the organization to provide additional information in Schedule J:

  - whether any FORMER officer, director, trustee, key employee, or highest compensated employee now receives over $100,000 in compensation from the organization (or over $10,000 from the organization or any related organization due to their capacity as a former officer, director, trustee, key employee, or highest compensated employee)

  - whether any current or former officer, director, trustee, key employee, or highest compensated employee listed in Part VII receives compensation of more than $150,000 from the organization and any related organizations

- whether any current or former officer, director, trustee, key employee, or highest compensated employee listed in Part VII receives compensation from any <u>un</u>related organization for services rendered to the organization (IRS was attempting to address abusive situations where organizations are trying to "hide" portions of an individual's compensation by having unrelated organizations pay the compensation)

H. <u>Part VIII, Statement of Revenues</u>. The new Form 990 generally requests the same revenue figures as the old form requested, but the new form streamlines some of the categories of revenue from the old form. The old form contained a section for revenues and a separate "analysis of income-producing activities"; the new form combines these sections in the single Statement of Revenue of Part VIII.

I. <u>Part IX, Statement of Functional Expenses</u>. The IRS made no major changes to this portion of Form 990.

J. <u>Part X, Balance Sheet</u>. The only change to the "Balance Sheet" portion of Form 990 is that the new form requires that organizations include the value of (i) program related investments, if any, and (ii) program related land, buildings, and equipment.

K. <u>Part XI, Financial Statements and Reporting</u>. Part XI is a new section of the Form 990 that will require reporting of certain information regarding financial statement compilations, reviews, or audits. This portion of the new form contains questions regarding audits and the existence of an audit committee.

IV. <u>Schedules</u>

(Schedules with no likely impact on fraternity and sorority foundations are not included below.)

A. <u>Schedule A Public Charity Status and Public Support</u>

- Schedule A of the old Form 990 is a schedule that had to be completed by all public charities and required information regarding a number of unrelated topics, such as the following: compensation of independent contractors and highly compensated employees, the basis for an organization's public charity status (and the related support schedule for publicly supported organizations), a private school's non-discrimination policies and practices, lobbying, specific actions posing compliance concerns, and transactions or relationships with non-charitable organizations. The <u>new</u> Form 990 transforms Schedule A into a schedule that focuses exclusively on the organization's public charity status, with other parts of the old Schedule A moved elsewhere in the form.

- The support schedule for publicly supported organizations has been modified as follows (note that most fraternity and sorority foundations are publicly supported organizations):

- The public support testing period has been increased from four to five years, including the current tax year.

- The new form separates the public support tests for Code section 170(b)(1)(A)(vi) publicly supported organizations (most fraternity and sorority foundations) from the support test for 509(a)(2) publicly supported organizations.

- The old Form 990 required organizations to use the cash method of accounting in their public support schedule, even if they used accrual method elsewhere on the form; the new Form 990 eliminates this requirement so that an organization now must use the same method of accounting on the core Form 990 and on the support schedule.

B. Schedule B, Schedule of Contributors. Schedule B of the old form was required for Code section 501(c)(3) organizations and required reporting limited information regarding contributors and contributions, including the name of the contributor, aggregate contributions, type of contribution, and description of the property (for non-cash contributions). The new form does not change Schedule B in any respect.

C. Schedule C, Political Campaign and Lobbying Activities. The IRS basically reorganized questions that already appeared on old Form 990 and placed them together in the new Schedule C. Accordingly, the content required by Schedule C represents little change from the old form.

D. Schedule D, Supplemental Financial Statements. Old Form 990 required several attachments for financial information (attachments not displayed in the form or on a schedule); Schedule D now compiles these attachments in a single schedule and provides the format within which to report the information. Schedule D also incorporates new and existing reporting requirements for donor advised funds, conservation easements, escrow accounts, endowment funds, certain art and museum collections, and financial statement reconciliations.

E. Schedule G, Fundraising and Gaming Activities. Schedule G must be filed by:
(i) organizations spending more than $15,000 on professional fundraisers,
(ii) organizations receiving more than $15,000 on fundraising events, and
(iii) organizations receiving more than $15,000 on gaming activities. The schedule requires more detailed information regarding such fundraising, events, and gaming activities and the proceeds derived therefrom.

F. Schedule I, Supplemental Information on Grants and Other Assistance to Organizations, Governments, and Individuals in the United States. The old Form 990 required an attachment to Part II, lines 22a, 22b, and 23 to report grants made and assistance provided to individuals and organizations. New Schedule I consolidates these unstructured attachments so that all information relating to grants and other assistance to persons inside the US is reported in this one schedule. The filing threshold for such grants to be reported on Schedule I is $5,000 per grant.

G. Schedule J, Compensation Information. Schedule J must be filed if the organization (i) has any FORMER officer, director, trustee, key employee, or highest compensated employee that now receives over $100,000 in compensation from the organization (or over $10,000 from the organization or any related organization due to their capacity as a former officer, director, trustee, key employee, or highest compensated employee), (ii) has a current or former officer, director, trustee, key employee, or highest compensated employee listed in Part VII who receives compensation of more than $150,000 from the organization and any related organizations, or (iii) has a current or former officer, director, trustee, key employee, or highest compensated employee listed in Part VII who receives compensation from any unrelated organization for services rendered to the organization.

H. Schedule L, Transactions with Interested Persons. Schedule L requires information with respect to four potentially problematic types of transaction: (i) excess benefit transactions, (ii) loans to and from interested persons, (iii) grants or assistance benefiting interested persons, and (iv) business transactions involving interested persons.

I. Schedule M, Non-Cash Contributions. This is a new schedule that requires information from organizations receiving non-cash contributions. The information required by Schedule M previously was not collected on the old Form 990. The IRS is collecting this information because non-cash contributions have posed significant tax compliance problems. Schedule M must be completed by organizations receiving (i) more than $25,000 in non-cash contributions or (ii) contributions of art, historical treasures, or similar assets, or qualified conservation contributions.

J. Schedule O, Supplemental Information. The purpose of Schedule O is to provide space for organizations to (i) provide explanations and narratives with respect to specific information requested by Form 990 and the schedules and (ii) supplement information provided on the Form 990, even if there is not a specific instruction requiring the organization to do so.

K. Schedule R, Related Organizations and Unrelated Partnerships. Schedule R must be completed by organizations that have certain defined relationships with other organizations. Such relationships include the following:

- Parent – Subsidiary: the filing organization is controlled by another organization or vice-versa

- Brother/Sister: the filing organization is controlled by the same person or persons that control the filing organization

- Supporting/Supported: the filing organization is (or claims to be) (i) a Code section 509(a)(3) supporting organization of another organization or (ii) the supported organization of a Code section 509(a)(3) supporting organization.

- “Control,” for these purposes, means (i) the power to remove and replace a majority of a nonprofit organization’s directors or trustees, or (ii) a management overlap where a majority of the controlled entity’s directors or trustees are trustees, directors, officers, employees, or agents of the controlling organization.