



Tax Update: National Association of Black Accountants  
June 2009

# Objectives

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- Your Story
  - IRS
  - Stakeholders
  - The numbers – do they support your story?
- Compensation
- Affiliated and Related Organizations
- Unrelated Business Income Tax
- Foreign Activities
- 990 Process

# Redesigned Form 990

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<b>Form</b>	<b>Form Description</b>
Form 990 Core	Return of Organization Exempt from Income Tax
Schedule A	Public Charity Status & Public Support
Schedule B	Schedule of Contributors
Schedule C	Political Campaign & Lobbying Activities
Schedule D	Supplemental Financial Statements
Schedule E	Schools
Schedule F	Statement of Activities Outside of 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 U.S.
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 to Form 990
Schedule R	Related Organizations and Unrelated Partnerships

## Goals of the Redesigned Form 990

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- *Increasing transparency* by giving the IRS and the public a more comprehensive picture of a tax exempt organization, including its mission, programs and goals, its revenues and expenses, and its internal policies and practices;
- *Promoting accountability* by publicly sharing the way that organizations their assets and conduct their operations; and
- *Encouraging compliance* by accurately reporting on the organization's operations so that the IRS may effectively assess the risk of noncompliance.

## Transitional Relief for Small Organizations

<b>May File 990-EZ for:</b>	<b>If gross receipts are:</b>	<b>If assets are:</b>
2008 tax year (filed in 2009)	> \$25,000 and < \$1,000,000	< \$2.5 million
2009 tax year (filed in 2010)	> \$25,000 and < \$500,000	< \$1.25 million
2010 and later tax years	> \$50,000 and < \$200,000	< \$500,000

# 990 Options

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- Form 990
- Form 990 EZ
- Form 990N
  - Calendar year ending 12/31/07; Fiscal year ending 6/30/08
  - Annual gross receipts of \$25,000 or less
  - Postcard is due by the 15<sup>th</sup> day of the fifth month after the close of the tax year (May 15 or November 15 for most organizations)
  - Automatic revocation for any organization that fails to meet its annual filing requirement for three consecutive years
  - IRS Announcement – 500,000 could lose exemption by May 2010

# Your Story

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- Whistle-blower organizations
  - “Your Nonprofit Story Counts” ... [www.greatnonprofits.org](http://www.greatnonprofits.org)
  - “Find a Charity you can Trust” ... [www.charitynavigator.org](http://www.charitynavigator.org)
  - “The Start of a Great Giving Decision” ... [www.guidestar.org](http://www.guidestar.org)
- Charity Navigator – Six questions to ask before donating
  - Can your charity clearly communicate who they are and what they do?
  - Can your charity define short & long-term goals?
  - Can your charity tell you the progress it has made toward its goals?
  - Do your charity’s programs make sense to you?
  - Can you trust your charity?
  - Are you willing to make a long-term commitment to your charity?
- Guidestar
  - Great giving decisions start with great data. Our data goes beyond the basic IRS listing to give you the most comprehensive information available, such as a nonprofit's mission, programs, leadership, and finances, so that you can make the best, most informed decision possible.

# Important Narratives

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- Activities/Programs
  - New or changed programs
  - Expansion of Schedule D (balance sheet) items
  - Foreign activities/grants
  - Fundraising arrangements
  - Monitoring of domestic grants
  - Transactions with “Interested Persons”
- Governance
  - Form 990 review process
  - Conflict of interest process
  - Compensation policies & practices; specifics for benefits
  - State registrations
  - Public disclosure
  - Fin48 – Accounting for Uncertain Tax Positions
  - Hospitals – charity care, community building, bad debts, collection practices
  - Related organizations

# Mission and Program Service Accomplishments

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- Form 990, Part III
- Compliance with 2 Tests:
  - Organizational Test
    - The organization's governing documents display commitment to exempt purpose
    - Assets must be permanently dedicated to an exempt purpose
  - Operational Test
    - An organization will be regarded as *operated exclusively* for one or more exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in Internal Revenue Code.

## Why are you exempt... 501(c)(3)s and 501(c)(4)s

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- Reporting of 3 largest program services by expenses along with revenue directly derived from activity
- Program Service: An activity of an organization that accomplishes its exempt purpose
- Description should include:
  - Specific measurements – clients served, days of care provided, number of sessions or events held, or publications issued;
  - Objectives – current and long-term goals;
  - Reasonable estimates for any statistical information.
- New program services and changes in program services **MUST** be disclosed in Schedule O.
  - Alignment with exempt purpose!!!

## Why are you exempt...Educational Institutions

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- IRC Sec. 170(b)(1)(A)(ii)
- Satisfaction of 3 Requirements
  - Primary function: Presentation of formal instruction;
  - Regular Faculty and Curriculum;
  - Regularly enrolled body of pupils or students in attendance.
- Public Policy Requirement – Rev. Proc. 75-50



# Why are you exempt...Healthcare Organizations

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- Community Care/Charity Benefit
  - [www.cha.org](http://www.cha.org) – Community Benefit Categories and Standard Definitions for Hospitals and LTC
- Hospitals
  - IRC Sec. 170(b)(1)(A)(iii)
  - Medical or hospital care or medical education or medical research
  - Licensed by state – Schedule H
- Promotion of health in community



## Why are you exempt...Public Charities

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- “Organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals...”
- No private inurement!
- Reason for exemption: Activities must benefit the general public or a segment of the general public large enough to be treated as a charitable class.

## Why are you exempt...Social Welfare Organization

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- IRC Sec. 501(c)(4)
- “Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.”
- “Social Welfare:” Furthering of the common good and general welfare of the people of the community as a whole
- Two general classifications: social welfare associations and local association of employees

## Why are you exempt...Membership Organizations

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- IRC Sec. 501(c)(6)
- “Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.”
- Promotion of common business interest
- Reason for exemption: Devotion to the improvement of business conditions of one or more lines of business as distinguished from performing particular services for individual persons

## Power of Schedule O

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- Reasonable Efforts Standard
  - Reporting organization may rely on *reasonable efforts* to obtain information on interested persons or third parties.
- Specific reporting requirements
  - Part VI, *Governance, Management and Disclosure*, Line 1b – Number of voting members that are independent
  - Part VI, *Governance, Management and Disclosure*, Line 2 – Family or business relationship among officers, directors, trustees and key employees
  - Part VII, Section A, *Officers, Directors, Trustees, Key Employees and Highest Compensation Employees*, Line 1a – Reporting of compensation paid by related organizations
  - Schedule L, *Transactions with Interested Persons*
    - Part III, *Grants or Assistance Benefiting Interested Persons*
    - Part IV, *Business Transactions Involving Interested Persons*
- Examples provided in revised instructions

## Power of Schedule O

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- Use of Management Companies
  - An organization that performs the management duties customarily performed by or under the direct supervision of another's officers, directors, trustees or key employees
  - Duties include: hiring, firing and supervising personnel, planning or executing budgets or financial operations
- Process of Review for Form 990 by Governing Body
  - Instructions: "Yes" if copy of Form 990 provided to each voting member of the governing body prior to filing
  - Additional disclosure of specifics: Who, When and What
  - "No review was or will be conducted" should NOT be a response.
- Monitoring and Enforcement of Conflicts of Interest
  - Explanation of persons covered;
  - Level at which determinations of whether a conflict exists;
  - Level of review for actual conflicts;
  - Restrictions imposed on persons with a conflict.

## Power of Schedule O

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- Rebuttable Presumption of Reasonableness
  - Identification of officers or positions and year last undertaken
  
- 15 Did the process for determining compensation of the following persons include a review and approval by independent persons, comparability data, and contemporaneous substantiation of the deliberation and decision:
  - a The organization's CEO, Executive Director, or top management official? . . . . .
  - b Other officers or key employees of the organization? . . . . .
  
- Public Disclosure Requirements
  - Forms 990, 990T, 1023/1024 Required
  - Audited Financial Statements, Conflict of Interest Policies, Governing Documents – IRS Authority???

## What story do your numbers tell?

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- Fundraising
  - Expense to total contributions
- Revenue Diversification
- Program Services
- Rate of Return
- Functional Expenses
- Compensation Analysis



# Compensation

- 2 Areas of Disclosure for Compensation
  - Part VII – Identification of “Interested Person” regardless of compensation
  - Schedule J - \$150,000 Test below
- Reporting of Compensation paid to Officers, Directors, Trustees or Key Employees
  - Key Employee
    - Three prong definition – Only those persons other than officer, director or trustee, who...
      1. Had reportable compensation exceeding \$150,000 for the year;
      2. Had or shared organization-wide control or influence similar to an officer, director or trustee, or managed or had authority over at least 10% of the organization’s activities; and
      3. Were within that group of organization’s top 20 highest paid persons for the year who satisfied both the \$150,000 test and the responsibility test.
- Reporting of 5 Highest Paid Employees and Independent Contractors
  - ALL Organizations
  - More than \$100,000



# Compensation

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- All components of compensation
  - Breakdown of W-2/1099
    - Base compensation
    - Bonus & incentive
    - Other compensation
  - Deferred Compensation
    - IRC Sections 83; 403(b); 409A; 457(f); 3121(v)
  - Nontaxable Benefits
- Fiscal yearend? Must report using calendar year W-2/1099

# Compensation

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- Nontaxable Benefits
  - Items not reported as taxable compensation, W-2, Box 5
  - Value of housing provided by employer
  - Educational assistance
  - Health insurance
  - Medical reimbursement programs
  - Life insurance
  - Disability benefits
  - Long-term care insurance
  - Dependent case assistance
  - Adoption assistance
  - D&O insurance and other payments – IRC Sec. 42
  - Do not report de minimis fringe benefits

# Compensation

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- Schedule J, Part I, III
  - Expense Reimbursement Substantiation Policy for Officers, Directors, etc
  - Process and Data to establish compensation of CEO/Executive Director
  - Former Officers, Directors, Trustees, Key Employees
  - Process of establishing compensation

- Schedule J, Part II

- 4** For any individual listed in Section A, is the sum of reportable compensation and other compensation from the organization and related organizations greater than \$150,000? If "Yes," complete Schedule J for such individual. . . . .
- 5** Did any person listed in Section A receive or accrue compensation from any unrelated organization for services rendered to the organization? If "Yes," complete Schedule J for such person . . . . .

- More complete picture of compensation packages
  - Breakout of Form 990, Part VII, Schedule A
- "Other Compensation"
  - i.e. Retirement Plan Benefits and Nontaxable Fringe Benefits
- Curb of Abuse
  - Payment of Compensation by Unrelated Organization

# Affiliated & Related Organizations

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- Schedule R

- 33 Did the organization own 100% of an entity disregarded as separate from the organization under Regulations sections 301.7701-2 and 301.7701-3? *If "Yes," complete Schedule R, Part I* . . . . .
  - 34 Was the organization related to any tax-exempt or taxable entity? *If "Yes," complete Schedule R, Parts II, III, IV, and V, line 1* . . . . .
  - 35 Is any related organization a controlled entity within the meaning of section 512(b)(13)? *If "Yes," complete Schedule R, Part V, line 2* . . . . .
  - 36 **Section 501(c)(3) organizations.** Did the organization make any transfers to an exempt non-charitable related organization? *If "Yes," complete Schedule R, Part V, line 2* . . . . .
  - 37 Did the organization conduct more than 5% of its activities through an entity that is not a related organization and that is treated as a partnership for federal income tax purposes? *If "Yes," complete Schedule R, Part VI* . . . . .
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- Goal: Improve transparency of increasingly complex organizational structures of tax-exempt organizations
- Cost-Sharing Arrangements/IRC Sec. 482

# Affiliated & Related Organizations

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- Relationships -
  - Parent/Subsidiary – An organization that controls/controlled by the filing organization
    - Definition of Control:
      - The power to remove and replace (or to appoint or elect) a majority of the directors or trustees, or
      - A management or board overlap where the majority of the subsidiary's officers, directors or trustees are the same as the parent organization
  - Brother/Sister – an organization controlled by the same person/persons as the filing organization
    - Definition of Control: Same persons constitute a majority of the members of the governing body of both organizations
  - Supporting/Supported – IRC Sec. 509(a)(3)

## Affiliated & Related Organizations

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- Tax-Exempt/Taxable Relationship – Definition of Control
  - Corporation: Ownership of more than 50% of the stock (by voting power or value)
  - Partnership: Ownership of more than 50% of the profits or capital interest
  - Trust: Ownership of more than 50% of the beneficial interests
  - Managing member or managing member in a partnership or LLC with three or fewer managing partners or members
  - General partner in a limited partnership which has three or fewer partners
  - Disregarded Entity: Sole member
- Please note that control can be indirect!!!
  - Constructive ownership under IRC Sec. 318

## Schedule R, Part V, Transactions with Related Organizations

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- **Thresholds for Disclosure:**
  - **Controlled Entity under IRC Sec. 512(b)(13): NO THRESHHOLD**
    - The receipt of interest, annuities, royalties or rent from a controlled entity;
    - A loan made to a controlled entity; or
    - Any other transfer of funds between the organization and the controlled entity.
  - **501(c)(3) Organizations: Transactions with related exempt organizations not described in 501(c)(3)**
  - **Other: \$50,000**

# Schedule R, Part V

## Part V Transactions With Related Organizations

Note. Complete line 1 if any entity is listed in Parts II, III, or IV.

	Yes	No
<b>1</b> During the tax year, did the organization engage in any of the following transactions with one or more related organizations listed in Parts II-IV?		
<b>a</b> Receipt of (i) interest (ii) annuities (iii) royalties (iv) rent from a controlled entity . . . . .	<b>1a</b>	
<b>b</b> Gift, grant, or capital contribution to other organization(s) . . . . .	<b>1b</b>	
<b>c</b> Gift, grant, or capital contribution from other organization(s) . . . . .	<b>1c</b>	
<b>d</b> Loans or loan guarantees to or for other organization(s) . . . . .	<b>1d</b>	
<b>e</b> Loans or loan guarantees by other organization(s) . . . . .	<b>1e</b>	
<b>f</b> Sale of assets to other organization(s) . . . . .	<b>1f</b>	
<b>g</b> Purchase of assets from other organization(s) . . . . .	<b>1g</b>	
<b>h</b> Exchange of assets . . . . .	<b>1h</b>	
<b>i</b> Lease of facilities, equipment, or other assets to other organization(s) . . . . .	<b>1i</b>	
<b>j</b> Lease of facilities, equipment, or other assets from other organization(s) . . . . .	<b>1j</b>	
<b>k</b> Performance of services or membership or fundraising solicitations for other organization(s) . . . . .	<b>1k</b>	
<b>l</b> Performance of services or membership or fundraising solicitations by other organization(s) . . . . .	<b>1l</b>	
<b>m</b> Sharing of facilities, equipment, mailing lists, or other assets . . . . .	<b>1m</b>	
<b>n</b> Sharing of paid employees . . . . .	<b>1n</b>	
<b>o</b> Reimbursement paid to other organization for expenses . . . . .	<b>1o</b>	
<b>p</b> Reimbursement paid by other organization for expenses . . . . .	<b>1p</b>	
<b>q</b> Other transfer of cash or property to other organization(s) . . . . .	<b>1q</b>	
<b>r</b> Other transfer of cash or property from other organization(s) . . . . .	<b>1r</b>	

## Schedule R, Part VI, Unrelated Organizations Taxable as Partnerships

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- Meeting of ALL of the Following Conditions:
  - Treated as a partnership for federal income tax purposes,
  - Filing organization was a partner or member at any time during the filing organization's tax year,
  - Filing organization conducted more than 5% of its activities as measured by its total assets or gross revenue.
- Disregard
  - 95% or more of the partnership's gross revenue – interest, dividends, royalties, rents and capital gains (IRC Sec. 512(b)(1)-(3) and (5); and
  - Primary purpose: Production of income or appreciation of property and NOT the conduct of a 501(c)(3) charitable activity.

# Unrelated Business Income

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- Basics:
  - *Trade or Business*
  - *Regularly Carried on*
  - *Unrelated to Exempt Purpose*
- FIN48 Deferral
  - Note: Deferral must be disclosed in audited financial statements!!!
- Partnership Interests: Schedule R, Part III requests disclosure of unrelated business income from Schedule K-1.

# Unrelated Business Income Examples

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- Alternative Investments
- Advertising
- Nonmember services
- Travel Tours
- Summer Camps
- Debt-Financed Rent
- Rent with Services
- Investment Income for 501(c)(7)s and 501(c)(9)s

# Foreign Activities

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- Schedule F

- 14a Did the organization maintain an office, employees, or agents outside of the U.S.? . . . . .
- b Did the organization have aggregate revenues or expenses of more than \$10,000 from grantmaking, fundraising, business, and program service activities outside the U.S.? *If "Yes," complete Schedule F, Part I* . . . . .
- 15 Did the organization report on Part IX, column (A), line 3, more than \$5,000 of grants or assistance to any organization or entity located outside the United States? *If "Yes," complete Schedule F, Part II.* . . . . .

- Regional Basis of Reporting

- Grant-making Procedures for Selection and Monitoring Use of Funds outside the U.S.

## Foreign Activity

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- Grantmaking
  - Includes awards, prizes, cash allocations, stipends, scholarships, fellowships, research grants, and similar payments and distributions made to foreign organizations, foreign individuals or foreign governments.
  - Does not include salaries or other compensation to employees.
- Fundraising
  - Activities undertaken to induce potential donors to contribute money, securities, services, materials, facilities, other assets, or time. Does not include gaming.
- Unrelated trade or business
- Program services –
  - Activities that form the basis of the organization's exemption from federal income tax conducted by the organization outside the United States.
    - Examples: operating an orphanage, school, hospital; disaster relief efforts; providing indigent relief.

## Foreign Activity

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- Maintaining offices, employees, or agents in regions outside the United States for the purpose of conducting such activities
  - Note: “Agent” does not include volunteers.
- Passive investments other than financial accounts –  
Alternative Investments!!

## 990 Process

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- Identify “interested persons” and distribute a questionnaire
- Complete the non-numbers analysis – reviewing narratives early will save on review time later
- Complete financial data
- Board review

## Summary

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- Have you communicated clearly who you are and what you do and do the numbers support your descriptions?
- Do your programs make sense? Would your stakeholders agree?
- Does the presentation of your governance structure and leadership instill stakeholder confidence?
- Are you spending dollars wisely and managing financial matters prudently?
- Is this the most positive presentation of your information? Multiple reviews from multiple perspectives may be necessary.
- Timing of submission

## Contact Information:

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