

NON-PROFIT

POSSIBILITIES



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3 *New Tax Laws and Non-Profits: What You Should Know*

FORM 990

*Significant Areas for Boards to Assess***OVERVIEW**

Organizations, both those with calendar and fiscal year-ends, have been through at least one year of the revised Form 990 reporting. Governance best practices, transparency and accountability were key messages addressed in the revised Form 990. These key messages serve as reminders to the boards of exempt organizations of their fiduciary duties of care. Now that the most overwhelming year of reporting has been completed, it is important for boards to take a step back and assess the most significant areas of the Form, as well as those that caused the most concern.

Governance and Management

The IRS believes good governance comes from an engaged and independent board and leads to better tax compliance. As you recall, the Form 990 asks numerous questions related to the exempt organization's governing body. Two of the most significant questions are:

- How many voting members are independent?
- Do family and/or business relationships exist between the board members or other key executives?

While there is no federal law requiring a minimum number of independent board members, the IRS clearly favors this. Boards should be well-educated on what impairs independence—the definition is complicated and may not appear logical. Many organizations found the task of gathering information on independence cumbersome.

Organizations must also disclose family or business relationships amongst board members and key executives. Again, many organizations found this information-collecting process difficult and time consuming. Factors contributing to the frustration were improper education on what constitutes a family or business relationship and lack of advance notice that this information would be disclosed in

the return. Boards should be aware it is sufficient to list “family relationship” or “business relationship” without greater detail.

One recommendation to improve these processes for 2009 and beyond is to gather information early. Organizations may distribute an annual letter or checklist to board members asking them to respond “Yes” or “No” to specific independence, family relationship and business relationship questions. Include examples and definitions in the letter/checklist to help reduce the number of questions from board members and key employees, as well as speed up the process. Organizations should also clearly communicate that this information may be included in the return, which is open for public inspection. By sending a letter, the organization can track responses and meet the reasonable effort requirement of the IRS. Another suggestion is to distribute this letter/checklist at a board meeting and require completion by the next board meeting.

Organizations relying on their conflict of interest (COI) policies for gathering this information should do so with caution. In most cases, a COI policy will not contain all of the information needed on the Form 990. For example, most COI policies do not cover business relationships between interested persons who do not involve the reporting organization. This comes into play when there is a current or former officer, director, trustee or key employee with an indirect business relationship through ownership of more than 35 percent in another entity (individually or collectively with another person or persons who are current or former officers, directors, trustees or key employees).

Transactions with Interested Persons

Another significant area boards need to be aware of is Schedule L – Transactions with Interested Persons. Organizations are required to disclose

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transactions, which are broken down into four parts:

- Excess benefit transactions
- Loans to and/or from interested persons
- Grants or assistance benefitting interested persons
- Business transactions involving interested persons

Again, the organization is required to gather this information and determine if disclosure is necessary. It is important to note each part has a different definition of “interested persons,” and different thresholds for reporting transactions. Many organizations struggle with how much effort is required to capture and report these transactions when management of the organization may not know all of the respective relationships and arrangements.

Parts related to grants or assistance and business transactions may rely on reasonable effort. Therefore, organizations may rely on the diligence and accuracy of board members’ responses to an annual letter or checklist. Organizations may choose to distribute one letter or checklist that covers independence, family and business relationships, and other transactions in order to reduce the number of requests made of board members.

Again, organizations relying on their COI policies for this information should be cautious. The COI may have a different definition of interested person.

Boards should analyze whether or not their current methods for requesting this information is adequate. In addition, they should be educated on the various types of transactions that may require disclosure.

Policies and Procedures

The Form 990 asks detailed questions on a variety of policies that are not required by the IRS, but nonetheless must be answered. Some of the more significant and scrutinized questions are:

- Is a copy of the Form 990 provided to the full governing body before filing?
- Is there a conflict of interest policy?

- Did the compensation process (for certain individuals) include a review by independent persons, comparability data and contemporaneous substantiation of the deliberation and decision?

In order to respond “Yes” to whether or not the Form 990 was reviewed prior to filing, an organization must be able to say each voting member of the governing body received a final copy prior to filing. Many organizations have the form completed just before the filing date, which hampers the governing body’s ability to review it prior to filing. The IRS states an organization may answer “Yes” if it e-mails the entire governing body a copy of the Form 990 and notes in the e-mail the Form is provided for review. Therefore, regardless of whether or not the governing body actually reviews the Form 990, the organization is able to respond “Yes.”

The IRS’ intent in asking this question is to ensure boards take an active role in the tax compliance process and understand what is being reported. Though it is not necessary for a member of the governing body to review the Form 990 to satisfy the fiduciary duty of care, it is considered a best practice. Depending on the size of the governing body, it may make sense to distribute a copy to everyone, but designate a committee to review the Form 990 in-depth and report back to the full board.

Most organizations have a COI policy. However, if an organization states they have a COI, but then indicates they don’t require officers, directors or trustees, and key employees to make annual disclosures—what kind of policy is it? Some organizations have individuals complete a COI statement when they first become a board member or are first employed, but never require it to be updated on an annual basis. Also, many organizations structure their COI policy to only cover the governing body. The IRS asks whether the governing body and key employees are required to disclose conflicts. Board members need to carefully review their COI policy before answering these questions.

Many organizations have responded by adopting a practice to request board members to state



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New Tax Laws and Non-Profits:

What You Should Know

At the end of 2010, we saw a flurry of legislation, including the Small Business Jobs Act and the Tax Relief, Unemployment Insurance Authorization and Job Creation Act of 2010 (Tax Relief 2010), which created some significant tax changes for businesses. Although the majority of the provisions of this new legislation impact for-profit businesses and individuals, certain aspects will also have an impact on non-profits. This article will summarize some of the key aspects of the new legislation that may impact non-profits.

- In the hope of stimulating the economy, Tax Relief 2010 creates an employee payroll tax holiday. For 2011, employees will pay 2 percentage points less (4.2 percent rather than 6.2) on Social Security wages. For those non-profits that work with contractors, this same tax holiday extends to them with a tax reduction to 10.4 percent from 12.4.
- If a non-profit's 401(k), 457 or 403(b) plan has a qualified Roth contribution program and provides for in-plan rollovers, a distribution to an employee or surviving spouse from an account under the plan that is not a designated Roth account is permitted to be rolled over into a designated Roth account under the plan for the individual. Such a rollover is taxable.
- Non-profits that provide an educational assistance benefit to employees can exclude up to \$5,250 in employer-provided education

assistance annually from income and employment taxes. Originally scheduled to expire after 2010, Tax Relief 2010 extends these provisions through December 31, 2012.

- Tax Relief 2010 provides for tax-free distribution from individual retirement plans for charitable purposes. Such distributions are limited to \$100,000 and will expire on December 31, 2011.

In addition to extending tax-free distributions from retirement plans for charitable purposes, Tax Relief 2010 also extends the following provisions through 2011:

- Certain charitable deductions for contribution of food inventory
- Charitable deductions of computer equipment for educational purposes from corporations
- Basis adjustment to stock of S corporations making charitable contributions of property

If you have additional questions, please contact your Eide Bailly representative. ■



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RETURN SERVICE REQUESTED

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potential conflicts at each separate meeting, versus relying on an annual signed COI statement. If an organization does not already have a COI in place, it is highly recommended that one be developed. For an example policy, see the appendix to the instructions for Form 1023 – Application for Exemption.

An organization’s compensation review policy is of great interest to the IRS and will be for the foreseeable future. The excess benefit transaction regulations provide procedures by which a public charity can establish a “rebuttable presumption” that compensation is reasonable. The Form 990 asks whether or not an organization followed these procedures when establishing compensation for the top management official, as well as other officers and key employees:

- Review and approval by independent persons
- Comparability data
- Contemporaneous substantiation of deliberation and decision

If an organization cannot answer “Yes” to this question, it is highly recommended the organization make changes to its current policy or adopt and implement a policy that includes

all of these elements. If an organization is currently responding “Yes” for the top management official and “No” for other officers and directors, boards should consider whether changes be made in order to respond “Yes” to both questions.

While the initial year for the revised Form 990 has come and gone, the Form continues to undergo change. Boards are encouraged to revisit previous responses and narratives on an annual basis and not rely on prior years’ answers. In addition, boards need to be more engaged than ever due to the amount of information contained in these returns. ■



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