



READY REFERENCE PAGE

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FOR YOUR FILE

30 Key Issues on the Form 990:

PR opportunities and traps for unwary

Form 990 is an organization's most important public relations document because it is instantly available to the world on the Internet at any moment

The Form 990 tax information return for most tax-exempt organizations is the organization's most important public relations document. This is especially true for public charities. More important than a group's fancy annual report that is sent to a couple thousand people, perused briefly and usually trashed shortly thereafter, the Form 990 provides a huge amount of information that is instantly available on the Internet at any moment to anyone in the world who has access to a computer.

The Form 990 is read by donors and funders, by staff and volunteers, by competitors, by "watchdog" agencies, by regulators other than the Internal Revenue Service, and particularly by the media that wants to know about the organization. As one of a very few tax documents available to the public, it has developed a whole cadre of people who understand how to read it for what it says — and what it doesn't say — about the operations of the organization. It is a lot more than the numbers.

Underestimating its importance is a mistake. Every line and every question is important. But here is a list of 30 top issues that offer opportunities for public relations benefit or traps for the unwary.

Part I. Summary

Question 1. *Describe the mission or most significant activities.* This is the IRS's initial softball pitch, giving the organization the chance to hit it out of the park on the first substantive question. The IRS Instructions, which provide very helpful explanations of what is required for virtually every line of the Form, give the organization the choice of emphasizing the mission or the most significant activities. The organization should think carefully about what it wants to emphasize, particularly when it can state (or re-state) the formal mission in Part III and outline specific program service accomplishments in that part as well. But this is the opportunity to tout how the organization makes the world a better place. And if it won't fit in the two and a half lines made available on the Form, it can be continued on the open-ended space on Schedule O. Be succinct, but be positive.

Question 6. *Total number of volunteers.* This is a recognition opportunity for direct service volunteers as well as volunteer directors or trustees. But it can have two indirect legal effects that may not be immediately apparent. If the organization is on the cusp of qualifying as publicly supported under Sections 509(a)(1) and 170(b)(1)(A)(vi) within the "facts and circumstances" test for organizations with between 10% and 33 1/3% of public support, the greater the number of people who contribute time (as opposed to dollars) to support the organization, the more likely it is to qualify as publicly supported. Not recognizing the volunteers on the Form makes it harder to claim their support in the justification narrative on Schedule A. ([See Ready Reference Pages: "Calculating Public Support Percentage" and "New Schedule A Reflects Change in Public Support Rules"](#))

Failing to recognize the volunteers may have a similar impact if the organization wants to claim charity status in one of the states that requires an element of subsidy or gift in its services to the public to qualify

as a charity under state law. Some of those states allow the organization to count the value of volunteer time as an unreimbursed cost and subsidy to the program. If volunteers aren't recognized on the Form 990, which the state authorities will undoubtedly review, it is harder to claim their value convincingly.

Part II. Signature Block

Sign Here. The Form must be signed by the current president, vice-president, treasurer or other authorized officer **under penalty of perjury**. Even if prepared by an accountant or auditing firm at considerable expense, the organization, and its signing officer, are the ones responsible. Don't sign without reading and thinking carefully.

Part III. Statement of Program Service Accomplishments

Question 1. *Briefly describe the organization's mission.* The IRS requests the mission "as articulated in its mission statement or as otherwise adopted by the organization's governing body." If there hasn't been formal action, the answer is supposed to be "none." Although most return preparers probably ignore the requirement for "none," this is another effort by the IRS to get nonprofits to follow best practices in formalizing their purpose. If the organization simply repeats the same mission statement in the Summary on page 1 and this question on page 2 of the Form, it has lost a public relations opportunity.

Question 2. *Did the organization undertake any significant new program services during the year?* The IRS doesn't say what it means by "significant," but our rule of thumb is anything that hasn't been done before and is important enough to get a separate story in the organization's newsletter. Why should the organization care?

First, because organizations' missions morph over time and they may begin to do things not mentioned in their Form 1023 application for recognition of exemption. If the activity generates revenue and the IRS audits the organization, the revenue could be considered unrelated business income because, even though generally considered charitable, it is unrelated to anything the IRS recognizes as a reason for the organization's exemption. If it is unrelated to the reason for exemption, it could generate unrelated business income tax ("UBIT"). Since most organizations don't separately report new activities, this question may be the closest thing available and at least creates an argument that it was reported and accepted by the IRS as an exempt activity.

Second, the IRS has prosecuted people who failed to report new activities. In one case involving suspected jihadists, the IRS convicted an executive for failing to report a new activity on the Form 990. *A la Al Capone*, the government didn't have to prove that the defendant was actually supporting terrorist activities. It only had to prove the executive failed to report the new activity on the Form. ([See Non-profit Issues®, 7/16/08.](#))

Question 4. *Describe the organization's program service accomplishments.* This is obviously the most important public relations opportunity. The IRS asks for information on the three largest programs and allows a continuation for more on Schedule O. It is important to spell out the accomplishments in ways that make sense to readers, and in type large enough to read comfortably. We saw one 990 that described program service accomplishments in a single word: "small." We have seen other Forms where the type is so small that it is almost impossible to read without a magnifying glass, and without a magnifying glass didn't bother.

Don't just say you spent \$1 million on job training. Tell how many people were trained, how many got and retained jobs, and perhaps how much they paid in taxes or how much was saved in safety net payments as a result of the training. Don't just say that you provided music education for kids. Tell how many kids, whether they were from schools that no longer taught music, whether you have studies that show these students do better in school. If you provide humanitarian relief, tell us how many countries, how many people you helped, what you did for them and perhaps for how long.

You have 11 lines for each activity, plus the space on Schedule O. Make them as impressive as possible consistent with the truth.

Part IV. Checklist of Required Schedules

This Part has 38 questions about whether the organization needs to file supplementary schedules. For the most part, they are self-explanatory and merely give more financial information when required. A couple are of particular importance.

Question 3. *Did the organization engage in political activity?* For a 501(c)(3) public charity, a "yes" answer to this question is the kiss of death. Charities are not permitted to intervene in elections or they can lose their exempt status. Electioneering is okay for (c)(4) social welfare organizations or (c)(6) trade associations, but is not permitted for (c)(3) charities. ([See Ready Reference Page: "IRS Issues New Guidance on Electioneering"](#))

Question 4. (For 501(c)(3) organizations only.) *Did the organization engage in lobbying activity?* Some charities still have the sense that they may not lobby on legislative issues and reflexively want to answer this question "no." Our view is that if a charity is not lobbying, it is probably not doing its job. So much of what charities deal with is the result of public policy decisions that we take the view that charities ought to be lobbying to affect those decisions for the betterment of their clients and their communities. We look at this question to see if we should look at the schedule to see how much they are spending on lobbying activity. ([See Ready Reference Page: "Lobbying Rules Create Opportunity for Charities"](#))

Question 25. *Did the organization engage in an excess benefit transaction during the year or a prior year that was unreported?* The IRS requires self-reporting of excess benefit transactions in which a disqualified person receives more from the organization than the person gives in return. ([See Ready Reference Page: "Charities Must Avoid Excess Benefit Transactions"](#)) You can't avoid the issue just because the IRS hasn't found out about it yet. Remember that the Form is signed under penalty of perjury.

Question 28. *Did the organization engage in certain conflict of interest transactions?* This is another question that charities fear, but conflict of interest transactions are not absolutely prohibited by law and most charities don't adopt an absolute prohibition. These transactions can be tremendously helpful to the organization and can be explained that way on Schedule L. Failure to report, when discovered by a competitor or an antagonistic newspaper reporter, can create huge problems for the organization.

Part V. Statements Regarding Other Filings

Question 3. *Did the organization have gross unrelated business income of more than \$1000?* If so, the organization must report on the Form 990-T and must pay unrelated business income tax if the net unrelated business taxable income is more than \$1000. The Form 990-T is also a public document and must be shown to anyone who asks. In a 2013 report, the IRS found significant additional unrelated business

income in colleges and universities it studied and it is always on the lookout for more revenue. ([See Ready Reference Page: “IRS Finds Unrelated Business Income, Unreported Compensation in College Study”](#))

Question 7. *Did the organization comply with quid pro quo rules and other charitable giving requirements?* This is an omnibus question with 8 subparts that brings into play the whole gamut of special rules for substantiation, quid pro quo gifts, reporting disposition of gifts of tangible personal property, and other areas in which the IRS has found substantial abuses. The managers of the organization have to understand the rules in order to be able to answer these questions accurately.

Part VI. Governance, Management, and Disclosure

Most of this Part was added when the IRS expanded the Form 990 in 2008 in order to promote transparency and accountability in the nonprofit sector. Most of the questions are merely informational and do not reflect legal requirements. They are designed to give the reading public a greater understanding of the way the organization operates.

Section A. Governing Body.

Question 2. *Did any officer, director, trustee or key employee have a family relationship or a business relationship with any other officer, director, trustee, or key employee?* This is not the standard conflict of interest question. It deals with family and business relationships among the key people of the organization, flushing out nepotism issues as well as cozy business relationships. The questionnaire to get accurate answers to this question is a complex one. These relationships are not prohibited, but “too many” of them can create a picture of cronyism that could adversely affect the public perception of the organization.

Question 5. *Did the organization become aware during the year of a significant diversion of the organization’s assets?* Significant is defined as a gross value of diversions (not considering restitution, insurance collections or similar recoveries) exceeding the lesser of 5% of gross receipts during the year, 5% of total assets at the end of the year, or \$250,000. Note that the question is whether the organization became aware, not whether the diversion occurred, during the year. Knowing the reporting requirement, and the requirement to explain what happened and how the organization followed up on Schedule O, an organization may be much less likely to let the thief go quietly and much more likely to file a police report and prosecute in appropriate situations. It is a disclosure of particular interest to donors.

Question 8. *Did the organization contemporaneously document the meetings of its governing body and committees?* This seems like an elementary activity, but it is amazing how much litigation is undertaken that could probably have been avoided if the organization kept minutes of its meetings and there was prima facie evidence of what actually happened. In one recent case, individuals litigated over who the members of the board were when there were no minutes stating who was elected and the Form 990 listing of directors was not consistent from year to year. ([See Nonprofit Issues®, “Court Refuses to Decide Control of Nonprofit Board Without Trial,” 9/16/09.](#))

Section B. Policies. (that the IRS specifically says are not required by the Internal Revenue Code)

Question 11. Has the organization provided a complete copy of the Form 990 to each member of the governing body before it was filed? It is important for members of the Board to be able to see what is being said about them and the organization before it is filed for all the world to see. The Directors may

be able to spot errors before the Form is finalized but they will probably also learn a lot about the organization if they actually read it. Many organizations have the Form approved first by an audit or finance committee, but the question asks whether it is sent to all members of the Board. An explanation is required if it is not sent to all in advance.

Questions 12, 13, and 14. *Does the organization have policies on conflict of interest, whistleblower protection and document retention and destruction?* Sarbanes-Oxley generally applied only to for-profit companies, but two provisions applied to all organizations. It is a crime to retaliate against a whistleblower who reports to federal (not state or local) officials or to destroy documents once a person is aware of a federal investigation. Good whistleblower policies, however, will protect staff and board against good faith reporting of any perceived irregularity, and document retention and destruction policies will cover the whole range of retention, not just litigation holds. The conflict policy is important not only as good governance, but also as a way to get the information to answer the conflict questions on the Form 990 itself. Failure to answer yes to having each of these policies is a public relations negative.

Section C. Disclosure

Question 17. *List the states with which a copy of the Form 990 is required to be filed.* The question asks where the Form is required to be filed, not where it is filed. It may be required to be filed in each of the 39 states and the District of Columbia that have charitable solicitation registration laws in which the organization solicits charitable contributions. This question is regularly used by state charity regulators to see if the organizations are filing where required. Failure to file and report on Form 990 may also be a negative for sophisticated donors who know the rules.

Part VII. Compensation

This is probably the most read part of the Form, the list of directors and the compensation of the paid staff. For directors, a good faith estimate of the average number of hours per week spent on organizational business is required. It is not sufficient to say something like “as required” and it is not helpful to say that they spend 0- hours a week on the organization. That would be by definition a breach of fiduciary duty, even though the Instructions specifically contemplate it as a possible answer. The Instructions also allow an estimate, in tenths of an hour, if the estimate is less than an hour a week.

Some lazy preparers simply attach a copy of the board list to the Form instead of filling out the blocks on the Form itself. But those board lists frequently include personal addresses, phone numbers, email addresses, names of spouses and even Social Security numbers. None of that needs to be made public and ought not to be.

The compensation figures are to be reported on a calendar year basis, to line up with W-2 and 1099 reporting, even if the other financial information is reported on a fiscal year basis. Therefore, it may appear that total officer salaries listed in Part VII are inconsistent with the figures for officer compensation on the Statement of Functional Expenses in Part IX, but the two sections could be reporting two different sets of numbers. Explain on Schedule O.

List compensation for the top management official, such as the CEO or Executive Director, and the top financial officer, such as the CFO or treasurer, even if their compensation might not otherwise be large enough to make the list.

In calculating compensation from the organization itself and related entities, various types of non-reportable benefits must be included. Check the Instructions for a complete list of items that must be calculated and the types of benefits that may be disregarded. As the most read section of the Form 990, these numbers are particularly important.

To some extent, organizations are caught in a bind on reporting compensation. Failure to report all the required compensation can lead to major public relations problems when it all comes out. Reporting what the public might perceive to be “too much” compensation can also cause problems. That may be a consideration when compensation is being set originally. But the compensation is what it is by the time it gets to Form 990 reporting and it is not a good idea to try to shade it one way or the other.

If compensation is particularly skewed in any one year, because of a special bonus or a large pension contribution that has to be taken into income during the year, for example, it may be appropriate to explain the aberration on Schedule O in order to anticipate the questions that are almost inevitable because of the size the compensation in the year of the report.

Part VIII. Statement of Revenue

Line 1. *Contributions, Gifts and Grants.* Membership dues, particularly for a public charity, may include a portion of the payment that is for goods or services received by members and a portion that is a contribution. Only the contribution portion is supposed to be reported on line 1b, with the payment portion reported as program service revenue on line 2. The IRS says this is one of the most frequent errors in 990 reporting.

The organization must distinguish between government grants reported on line 1e and government contracts reported on line 2, even though the government may call both of the documents “contracts.” A government payment is reported as a grant if its primary purpose is to enable the organization to provide its charitable services to the general public rather than to provide a direct benefit to the paying agency. It is program service revenue if it provides a direct benefit to the agency or is a payment on behalf of a specific individual, such as Medicare or Medicaid.

The value of noncash contributions that are recordable, such as gifts of stuff but not services, must be totaled separately on line 1g. Many Forms simply neglect this line.

Line 6. *Rents.* This line is for rent from unrelated activities, not rents from program service activities, which are reported on line 2. Program service rents include rents received from low income housing tenants, from social service agencies located in a community center, or from students in college dorms. Putting rent on the wrong line can have a significant effect on the public support calculation of Schedule A.

Line 8. *Fundraising Events.* This calculation is frequently ignored or reported improperly. It requires dividing quid pro quo payments for the fundraising event between the payment for the goods or services received at the event and the extra amount that is a contribution to the organization. Many organizations will have to reconsider how they account for these events to get it correct, since some of the accounting software does not accommodate the requirements. ([See Ready Reference Page: “Form 990 Reporting for Special Events Can Be Tricky – And Is Often Wrong”](#))

Part IX. Statement of Functional Expenses

Public charities are required to divide all expenses among program services, management and general, and fundraising. The ratio is watched by the “watchdog” agencies to rate organizations on how much they are applying to program. Although there is significant resistance to the “overhead myth,” it is still alive and well. Be sure to allocate as much as is appropriate to program service expenses.

Many organizations fail to segregate fundraising costs, even though they report significant contribution revenue. It is the kind of omission that frequently leads to adverse stories in the local business press or the Chronicle of Philanthropy. It is possible that there is a good reason for the omission, such as fundraising cost being absorbed by a related foundation, but that should be spelled out in Schedule O.

Line 11e. *Professional fundraising services.* This line, which is carried forward to line 16b of the Summary on Page 1 of the Form, is a tip off for state charitable solicitation registration offices to see if the professional fundraising counsel or solicitors are properly registered with their states. In some cases, states have refused to register the charity until all of its paid consultants have themselves registered their contracts.

Part X. Balance Sheet

Line 1. *Cash – non-interest bearing.* The accountants usually get the balance sheet right, but some of them list millions of dollars as being in non-interest bearing accounts even though they are actually earning a little bit of money in a money-market type account. When a charity is continually seeking contributions, like a private school asking tuition-paying parents to contribute even more at the end of the year, it doesn’t look very good to have a lot of cash in non-interest bearing accounts on the balance sheet. It looks as though the organization isn’t paying attention to its money management, which is not good while the organization is asking for more gifts.

Lines 27-29. *Classification of net assets.* The accounting profession does not seem to have reached a consensus on the accounting treatment for endowment funds under the Uniform Prudent Management of Institutional Funds Act. The classification between unrestricted, temporarily restricted and permanently restricted can have a significant impact on donors’ and creditors’ view of an organization. ([See Ready Reference Page: “Permanently Restricted Assets Should Be Classified As Permanently Restricted Under UPMIFA”](#))

Part XII. Financial Statements and Reporting.

Question 2. *Is there an audited financial statement?* The IRS does not require an audited financial statement for Form 990 filings. Organizations that are required to register to solicit charitable contributions are required to have audits under various state laws depending on the level of contribution income received during the year. An organization of any size that wants to give donors the greatest assurance that its financial records are accurate will probably want to have audited statements even if not required by law.

A well done Form 990 helps convince the public that an organization has its act together and knows what it is doing. A badly done 990 suggests exactly the opposite. When an organization is dependent on voluntary contributions and the trust of the public to generate those donations, it is certainly better to look like the organization knows what it is doing.