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HOUSE WAYS AND MEANS COMMITTEE
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IN REGARDS TO OPERATIONS AND OVERSIGHT OF TAX-EXEMPT ORGANIZATIONS

Chairman Boustany, Ranking Member Lewis, and members of the Subcommittee, I am honored to provide testimony as to the design and efficacy of the chief tool by which oversight of the operations, activities and finances of most tax-exempt organizations is prosecuted: the IRS Form 990, annual return of organizations exempt from income tax under Internal Revenue Code Section 501(c).¹

My remarks today will focus on three areas. First, my experience in preparing Form 990, advising clients about the form, and teaching practitioners and organizational staff about the Form 990 for over 20 years, including most recently over that period which witnessed the revolutionary Form 990 redesign implemented for 2008 and later tax years. Second, those reporting areas for which the Form's 2008 redesign requires additional or new information not previously required. Third, those areas of the Form which I believe require further improvement and redesign in order to provide greater clarity and reduce compliance burden.

There is no doubt that the Redesigned Form 990 is a major improvement over the form's prior version. In my experience, the Form's new structure is both easier to follow and has resulted in filers providing more accurate versions of their activities. Filed Forms 990 now include much broader contextual data (mission, narration of changes in programming, explanation of changes in fiscal resources from the prior year or of new policies, etc.) than that which was available via pre-2008 Forms.² It is widely-admitted, albeit sometimes grudgingly,

¹ My remarks do not address the Form 990-EZ (short form for many smaller exempt organizations), the Form 990-T (the annual return to report and pay the unrelated business income tax), or the Form 990-PF (the annual return for private foundations) none of which have been redesigned.

² The baseline Form, called the "Core Form" consists of twelve pages filled out by all filers along with a Schedule of blank lines, the Schedule O, where filers narrate additional information called for by the Core Form. A sample Core Form and common Schedule O annotated with tips and explanations that I use in my teaching may be accessed at:

[http://taxexempt.ehclients.com/images/uploads/990_ERB_sample_core_form_2011_and_O_final.pdf_\(locked\).pdf](http://taxexempt.ehclients.com/images/uploads/990_ERB_sample_core_form_2011_and_O_final.pdf_(locked).pdf)

that the addition of a full page Part³ on Governance, where filers must address various aspects of their management structure, has been extremely successful in focusing attention upon basic “good governance” precepts and highlighted Board and manager’s responsibilities.

One of the advantages of the Form is that by providing all regulators – the IRS, the States, and the ‘court of public opinion’ – more complete information both on the Core Form and through some key Schedules, filers are cognizant of the Form’s importance not only from a tax-administration perspective but from a public relations perspective. It is clear that one of the three goals of the Redesign, “to take advantage of the Form’s transparency aspects,” has borne fruit and given credence to the notion that “sunshine is the best antiseptic.” I believe that the lay-out of the Redesigned 990 and the additional substantive data requested in the ancillary Schedules allows the IRS to more efficiently and effectively “hone in” on filers’ activities and study specific sub-sectors, analyze trends, and more appropriately allocate their limited resources to educational efforts and compliance programs.

I. Expertise/Experience with the Form 990

For my entire professional career, my legal practice has focused on advising and representing small and mid-size exempt organizations. My clientele does not include hospital systems, higher education systems (aside from 990 reviews), or other types of the largest exempt organizations (again, aside from 990 reviews or specific engagements related to IRS controversies). As a result, my experience has been with the size and type of organization that comprises the vast majority of organizations filing the Form 990.

I first began to practice tax law in 1985 when I joined the tax department of a Big 8 accounting firm after law school. There, I was assigned to Form 990 preparation, an assignment I had requested. For tax years begun in 1985, the Form 990 was five pages, supplemented by an additional Schedule for 501(c)(3) organizations which added three pages. At that time, the Form’s questions focused on virtually every federal income tax mandate to which the exempt sector was subject.

Incremental changes to the Form took place over the next several years. As the Form changed, so did my professional opportunities. I opened my own firm and began to represent tax-exempt organizations exclusively, on both exemption qualification and tax planning, and on IRS examinations of filed 990s. The 1989 Form added a Part requiring filers to ‘self-audit/report’ the basis by which their revenue streams were or were not subject to the unrelated business income tax. That addition was made after the IRS expressed concern that the Form provided no

³ To save space, I have placed the names of Parts and Titles in footnotes. Part VI of the Core Form is titled, *Governance, Management, and Disclosure*.

windows into those activities of filers that were generating non-contribution revenues (such revenues then potentially being subject to reach of the unrelated business income tax). The expansion created new demand for continuing professional education on the Form, and I ended up being asked to design and teach a 990 course for my home state CPA Society, which was later recommended by the Minnesota CPA Society to other State Societies. Over the course of 1991-1996, my self-authored/instructed whole day 990 continuing professional education (CPE) course was provided to more than 1,200 participants, by 12 State CPA Societies.

In the latter half of the 1990s, the increasing complexity of the Form and its accompanying Instructions grew as if on steroids, which increased my teaching opportunities. The number of State Societies that offered my 990 day class grew to 20. The most frequent critique of my all-day course at that time was that it was too short and really should be a two day course. In 2000, in response to demand from non-preparers seeking instruction on the Form, I developed a "half day" version of a 990 class for "real people." 990 educational presentations were increasingly sought by State nonprofit associations and by CPA Societies sponsoring conferences for nonprofits. All of that attention was directly related to the Form's unwieldy growth in complexity.

By 2007, the Form was a total of nine pages, with the additional Schedule required of 501(c)(3) organizations adding seven more pages. It was widely regarded -- by the filing sector, by public users, by paid preparers, and by the IRS -- as a "disastrous monster" that was staggering under its own weight, lacking any coherent design, and suffering from Instructions that could barely earn that title. The Form had been amended piecemeal over time, mostly at the request of Congress, in order to access more nuanced and relevant information from reporting organizations. By the time of the 2007 Form's release, it was clear that it was time to redesign the Form.

During 2007 and 2008, the IRS ramped up its efforts to redesign the Form and requested public comments to advance the Form's redesign. As someone whose experience with the Form had been informed by the many practical questions participants raised in my 990 classes (by that point more than 2,500 professionals had taken the 8-credit CPE 990 class from me) and by the nearly 20 years of practice representing organizations of all sizes before the IRS on audit examination, I eagerly participated in that comment process. I believe that my affinity for assisting small and medium organizations on understanding compliance mandates, including Form 990 preparation challenges, informed my approach. I participated via task forces from both the American Bar Association and the American Institute of Certified Public Accountants, and also provided personal comments to the IRS on their proposals for the Redesign. Ultimately, I played a part in providing close to 600 pages of the approximately 3000 pages of comments the IRS received.

I have continued to provide comments to the IRS on the Redesigned Form and its instructions to the present day. I continue to teach on the Form. I now offer two all day courses (the second day being an “advanced” Schedules class). I do not address the reporting mandates faced by nonprofit hospital facilities, leaving that specialty topic to the health care specialists. My course participants increasingly come directly from the exempt sector as more medium-sized entities choose to self-prepare their 990 filing.

In all venues of my work with the “Redesigned 990” – via comments to the IRS, teaching preparers, educating readers, and reviewing prepared Forms pre-filing for clients – my goal has always been to make the form and instructions more understandable so that the filing’s precepts are understood by those preparing a form for filing or accessing a form that has been filed. Promoting consistent and appropriate inputs on the Form not only enhances the credibility and stature of the exempt sector but allows those who regulate the sector to keep up with changing trends and tailor enforcement efforts accordingly.

II. The “Opportunity” Seized by the Redesigned 990 – Expanded and More Tailored Disclosures in Key Arenas Relevant Not Just to IRS but to Multiple Stakeholders

The Redesigned Form, if filled out properly by an exempt organization, captures far more specific and appropriate information in twelve arenas of operations and administration than did its predecessor. As a result, preparation of the Redesigned Form requires more labor than the prior form. However, that result occurs not just because of the new information sought, but because the Form requires *disclosures on multiple non-financial realms*. Those demands exist in spite of the fact that the Redesigned Form 990’s structure (a Core Form that all filers complete, with narrowly tailored-to-subject Schedules that apply in specific circumstances) implies that each Part or Schedule square with a “one size fits all” approach. Individual filer’s answers and inputs are not going to be “uniform” with those of other filers unless their circumstances are exactly the same.⁴ Trends and similarities will certainly cut across sub-sectors,⁵ but each filer must approach its own circumstances not only in devising the appropriate answer, but in many cases designing a narrative response.

The Redesigned Form 990 asks the filer to report on virtually all aspects of the exempt organization’s enterprise – what the filer’s programs achieved during the year, what managers (and certain other employees) and fiduciaries were in place, what those managers and fiduciaries

⁴ For example, all filers who have an executive committee empowered to act with delegated power of the Board would presumably identify that fact and explain the composition of individuals residing thereupon in responding to Line 1a of the Governance Part of the Form.

⁵ For example, most private schools and colleges will have some directors who are not in the count of “independent directors” because they have children attending the institution who were the recipients of financial aid or merit awards paid out during the tax year.

were paid, what governance and internal policies were in place by the end of the year, the existence of insider transactions, the type and total amount of grants or assistance provided to individuals, information on non-cash contributions received, results from larger fundraising activities or events, number of volunteers engaged (this is optional), narration of lobbying activities or detail of lobbying dollars disbursed for those under the lobbying election (this only for 501(c)(3)s), and dollar amounts of revenues garnered in conducting the organization's three largest (and then all other) programs (this only for 501(c)(3)s and (c)(4)s.) This requires filers to access *their* facts and *cull internal information* from multiple sources – staff on the program side of the organization, administrative/operations officers, and those who keep the organization's financial recordkeeping.

The twelve new arenas of expanded reporting required by the Redesigned 990 are largely related to operational imperatives that the public expects to be met by the exempt sector. Each of these arenas is listed below, separated into new areas and expanded areas of information reporting.

Eight Completely New Arenas

1. **Updating** the organization's ongoing **exemption application record** -- accomplished in the "Program Service Accomplishment" Part of the 990 Core Form, Part III, via three questions:
 - Inquiring whether the organization is undertaking any activity not previously reported to the IRS upon an exemption application and/or prior-filed 990s
 - Inquiring whether the organization has ceased any activities it previously reported to the IRS or has significantly changed how it conducts any previously reported activities
 - Requiring recitation of the organization's Board-approved mission statement
2. Focusing attention on **the authority and management practices** that are in place as a result of the inherent and ultimate authority **exercised by the exempt filer's governing Board** -- accomplished by (Core Form) Part VI⁶ and Part XII⁷ which ask questions that previously were absent from the Form concerning:
 - Board composition
 - Board's delegation of authority
 - Accountability to members if members exist (and denoting rights reserved to those members)

⁶ Part VI is titled, *Governance, Management, and Disclosure*.

⁷ Part XII is titled, *Financial Statements and Reporting*.

- Policies and procedures in place with respect to management practices overall in conflict of interest scenarios
 - Whether standard basic practices are employed in setting executives' compensation – also asked of in Schedule J, Part I⁸
 - Attention paid by the Board to review of the 990 filed with the IRS
 - How the organization makes public inspection of its 990 available as well as whether chartering and key governance documents (including audited financial statements) are available to the public
3. Providing information on each “related organization” (parent/subsidiary/brother-sister corporations, supporting/supported organizations, certain partnerships and trusts) – accomplished via Schedule R regarding related organizations
 4. Providing information on **arenas of operation regulated by the States** – accomplished via the following Schedules:
 - Schedule G⁹, Part I – addressing use of “professional fundraisers” and requiring organizations to certify they have met registration/reporting responsibilities in jurisdictions where professional fundraiser solicitation has occurred
 - Schedule G, Part III – addressing compliance of gaming operations with State (and local) law mandates
 - Schedule N¹⁰ – addresses “substantial contraction” and dissolution, merger, and termination of the organization
 5. Providing details on types of non-cash (colloquially referred to as “**property**”) **contributions**, including method of valuation – accomplished via Schedule M¹¹
 6. Providing information on **political (i.e., support or opposition of candidates for elective office) activities** undertaken – accomplished via Schedule C¹², Part I
 7. Providing information on **financial and other undertakings outside of U.S. borders** – accomplished via Schedule F¹³

⁸ Schedule J is titled, *Compensation Information*; Part II of the Schedule provides input on the same managers reported upon (Core) Form Part VII.

⁹ Schedule G is titled, *Supplemental Information Regarding Fundraising or Gaming Activities*.

¹⁰ Schedule N is titled, *Liquidation, Termination, Dissolution, or Significant Disposition of Assets*.

¹¹ Schedule M is titled, *Noncash Contributions*.

¹² Schedule C is titled, *Political Campaign and Lobbying Activities*

¹³ Schedule F is titled, *Statement of Activities Outside the U.S.*

8. Providing information on **tax-exempt bond issuances** – accomplished via Schedule K¹⁴

Four NOW EXPANDED Arenas of Inquiry (numbering continuing from above)

9. Requiring due diligence (i.e., reasonable efforts) to ascertain if parties who are themselves ‘insiders’ or who are connected to ‘insiders’ received grants or assistance from the organization or had business transactions with the organization *and then* disclosing basic parameters of such intersections – accomplished via Schedule L, Parts III and IV¹⁵
10. Reporting more revenue sourcing detail on potential types of unrelated business income tax-susceptible revenue – accomplished via (Core Form) Part III (solely for 501(c)(3)s and 501(c)(4)s), joint venture focus overall and specifically including Schedule R, Part VI and Schedule R, Part II column identifying 512(b)(13) controlled entities, and Schedule G, Part III
11. Compensation to managers (Board members, Officers, “Key Employees,” and the five highest compensated employees whose taxable income is at six figures or greater) is now reported using a consistent period and methodology (and details compensation paid by the filer and its related organizations) at (Core) Form Part VII Section A and Schedule J Part II
12. Consistent definitions for identifying “in charge” employees and Officers (current and former) that are subject to reporting at (Core) Form Part VII Section A and Schedule J Part II

III. How Well has the Opportunity Been Realized (i.e., How Complete/Accurate are Prepared Returns)?

Informing the answer here is the fact that the Form 990 is not a tax return. It is an annual information return. The difference between the functions of those two types of return is huge! In the Redesigned Form 990, there are only three pages of the (Core) Form that exclusively present financial statement data. The remaining nine pages, while in some places requiring numeric input, speak almost exclusively to topics that are either specific to exempt organization tax mandates or specific to programs and activities. In other words, the information is not likely to be in the knowledge base of an organization’s outside auditor or tax consultant. While these

¹⁴ Schedule K is titled, *Supplemental Information on Tax-Exempt Bonds*.

¹⁵ Schedule L is titled, *Transactions with Interested Persons*; Part III is titled, *Grants or Assistance Benefitting Interested Persons*, and Part IV is titled, *Business Transactions Involving Interested Persons*.

nine pages of the Core Form (and almost all the ancillary Schedules) do require numeric input, the numbers sought are typically to be culled not in line with generally-accepted accounting principles (GAAP). A truism for those of us who work with CPAs is that a non-profit auditor is almost always not an exempt organizations tax person and in many firms it is the case that “never the twain shall meet.”

Proper completion of the Redesigned 990 has required a steep learning curve. Filers have only recently begun to master the Form.

Preparers and users of the Form have found, for the most part, that the Form’s instructions are useful and relatively ‘plain English’. However, there is no denying that multiple areas of the Form have introduced new and/or complex concepts so that in total a steep learning curve exists. Not surprisingly, the pace by which the filing community has moved ahead in advancing on that learning curve has been slow. Indeed, in my judgment, it is only with the fourth filing season of the Redesign now in hand that palpable mastery and accurate completion of the new Form is being widely evidenced.

Self-preparers have had a much easier time in adjusting to the new Form than has the paid preparer community. Their learning curve progress has been advanced by the fact that in most cases the staff that does internal preparation actually reads the instructions. (My first teaching tip on the Redesigned Form is to “read the instructions.”) Furthermore, they can apply what they find in the instructions based on their firsthand knowledge of their own organization. The availability in the last decade of software for such self-preparers from the National Center of Charitable Statistics (via the efile.form990.org website) has also advanced the ability of exempt organizations to do their own returns – that software (“desktop 990”) is not expensive (it is practically free to small and medium organizations), allows the user to “pop up” the instruction for each entry point of the filing, save their work, have fail-safe error recognition, and ultimately e-file the return.

The generally slower advance on the learning curve by the professional “paid preparer” community is not surprising to me, as the quality of work by that community pre-Redesign was often impeded by several challenges, including:

- many CPA firms do exempt organization audit and tax work as a courtesy to their for-profit clients and do not have tax professionals in house who are adequately trained in exempt organizations tax mandates; the incentive to build out such expertise in smaller CPA firms and in firms in most non-metropolitan areas is lacking for multiple reasons (i.e., the nonprofit world has limited desire and ability to pay for what the work would cost; it is expensive to train staff on these mandates or work with associated experts to get the prepared returns properly reviewed; and little incentive

exists to commit to training when the firm is at risk of losing the individuals trained who may have more remunerative fields to ply).

- the longstanding misperception that a corporate tax preparer, or an auditor who knows the organization's financial statements, can easily and accurately complete a Form 990
- the reality that those serving multiple clients on tight deadlines will need to coordinate access to and input of data from the filer, then must interpret the Form's instructions in the context of that data (ignoring results that may have arisen from other fact scenarios), and then await review and further input from the filer before making the return final

And finally, regardless of whether an organization's preparer – internal or external – may be qualified to assist in or perform the actual 990 preparation, three other factors have slowed progress on the Redesigned 990's learning curve over the course of the first two to three years of the new Form's existence:

- a. the opaqueness of the pre-Redesigned Form's instructions led to an understandable initial resistance by most preparers to pick up and read all the Redesigned Form's instructions. The instructions packet is of daunting length, but there really are 'only' 34 substantive instruction pages pertaining to the 12 pages of the Core Form, and most of the ancillary Schedules have instructions running 3-5 pages. The Core Form instructions include a very valuable Glossary in which common terms are set out clearly and succinctly.
- b. a good old fashioned "this can't be" negative reaction to some of the Redesigned Form's demands fueled a lot of resistance My personal experience with that carping is that oftentimes people spend more time whining than they would expend in properly learning the application that fits their (or their client's) situation.
- c. the propensity of folks to not read the instructions fully when they do read them. . . . In teaching CPAs I always get a big laugh when I tell people NOT to stop reading when they get the answer they want.

Ultimately, in my experience, the reporting organizations themselves have become more willing to tackle the Form's requirements. This is in great part due to increasing public awareness of the Form and the information that it provides. Many filers are being challenged by readers of their 990 filings (particularly funding sources) who note that data is missing or inconsistent. This is in line with the intent of the Redesign, which is to have the Form not only foster compliance by providing information to the regulatory community but by taking advantage of the Form's transparency aspects.

IV. *Where Can The Form Be Improved?*

There are five *wishes* that almost all preparers (and those advising preparers) of the new 990 have. My address of these subjects, and recommendations in each arena, should not be interpreted as my belief that the five arenas in which those wishes vest (with one exception) are inappropriate for or otherwise unworthy topics of disclosure. My point is simply that the IRS could do a more efficient and effective and less burdensome job of getting information from the Schedule L, the Schedule F, the Core Form's Governance Part VI, and overall from small organizations. At the end of this section I also make some observations on Schedule R's reporting on transactions with "related organizations" and suggest the IRS seek comments as to how some of the Schedule L and R complexity can be attenuated to the end of reducing burden.

Additional IRS Education on "Semantics" and Reporting Implications

There is a need for education of the reporting community as to the meaning of key semantics the Form employs. There is also a need to foster an understanding that the IRS definitions for the Form are not necessarily the same used by others for other purposes, and that in many instances what appears to be negative reporting on the Form does not mean that the organization is doing anything improper. A classic example of this is the insider transactions reporting on Schedule L, which requires an organization to disclose many transactions which are common-place, even though the transaction may be advantageous to the organization. Reporting organizations and preparers are concerned that their reporting of Board members (Trustees or Directors) who are NOT "*independent*," or that their reporting that some of their Board members, Officers, or Key Employees are related to each other by "*business relationships*" or "*family relationships*," means that the involved individuals lack competence and appropriate capacity to serve the filer. Filers are similarly anxious if they must report having undertaken business transactions with firms or parties who are connected to their Board members, Officers, or Key Employees, upon Schedule L, Part IV, especially when the existence of such transactions is commonplace and commercially reasonable. Indeed, transactions are reportable upon Schedule L, Part IV regardless of whether they offer extreme advantage to the organization or afford the filer of opportunities that would not otherwise be available. Nonetheless, many organizations are fearful that the mere requirement to report the existence of such transactions on the Form 990 means that the transaction is improper, and that the involved individual should step down, a result that would deprive the organization of a valuable employee or Board member.

It would be beneficial to the sector for the IRS to address this problem by providing educational materials explaining that the only obligation (from an exemption qualification perspective) that a filer has in disclosing the existence of non-*independent* directors, managers with "*family*" or "*business*" relationships, or Schedule L, Part IV *reportable business transactions* is to ensure that those insiders (or those connected to them) are not being privately

benefited from their influence over the organization. The disclosures are there to focus attention on governors' responsibility to protect the filer from uneven exchanges to the organization's detriment and to ensure that transactions outside of the filer's best interests are not undertaken. Practitioners attempt to communicate this point, but the voice that should speak on this subject so that the message is delivered uniformly and with authority is that of the IRS. This is an area where additional IRS educational outreach, rather than revision of the form, would do much to solve the problem.

Simplify Schedule L

For the vast majority of organizations, Schedule L is the most difficult of all the Schedules that Form 990 filers must complete. The difficulties start with the significant burden in reviewing the circumstances that, if in place, would trigger the Schedule's application. Filers must self-assess if they have:

- if a 501(c)(3) or (c)(4) organization, engaged in a Code Section 4958 *excess benefit transaction* in the current year or have discovered such a transaction from a prior year that was not previously reported upon the Form 990. Such transactions are those that are undertaken with *disqualified* persons that unfairly benefit such persons.
- a loan on the balance sheet to or from a manager listed on the Core Form Part VII Section A or to or from a Code Section 4958 *disqualified* person
- grants or assistance provided to a pool of interested persons that includes managers listed on the Core Form Part VI Section A *other than five highest compensated employees*, family members of the preceding, grant selection committee members and their family members, contributors appearing on Form 990's Schedule B, and in some instances those contributors' employees
- business transactions with the same pool of managers reached by the preceding bullet, or their family members, or certain entities connected to any of those parties by control (in the case of nonprofit corporations, but this is attenuated when the other entity is 501(c)(3)), ownership (in the case of other than nonprofit corporations) or management involved by those individuals (in the case of business or investment entities) *and those transactions are above certain thresholds*

It would be beneficial to the sector if the Schedule L definitions were simplified. The fact that experts such as myself have spent tens of hours (if not a hundred or more) to be well-versed in the instructions for just two of the Schedule L's Parts (those in the final two bullet points preceding) reflects how difficult it is to have the sector become conversant with the parameters at play. The instructions require filers to make "reasonable efforts" to inquire of their managers if they are aware if they, their family members, or other entities with whom they or their family members are connected are getting grants or assistance from the filer, or have

engaged in business transactions with the filer. As a result, filers must convey the instructions' parameters to numerous insider parties in order to properly conduct a "reasonable effort" inquiry of managers. Either the IRS should attempt to simplify the present definitions for Schedule L's Parts III and IV, or it should provide flow-chart materials or similar tools in the Instructions to help demonstrate the numerous and complex reporting relationships encompassed in these Parts.

Allow Most Small Organizations to File a Form 990-EZ that Captures the Broader Information Sought by the 990's Core Form But Does Not Require Full Completion of All the Redesigned 990's Schedules

The Redesigned 990 overly burdens small charities and small non-501(c)(3) exempt organizations. In my experience, reporting organizations whose budget is on average under \$1,000,000 of revenue per year are not able to self-prepare the Form and are unlikely to have access to paid or volunteer professional preparers who are well-versed in the Form's intricacies. The present threshold at which the Form 990 is required (and the Form 990-EZ may not be used) for most filers: gross receipts for the year less than \$200,000 and gross assets at year end of less than \$500,000 – should be altered. To more closely tailor the reporting burden to the size of these organizations, my recommendation would be to allow exempt organizations with gross receipts for the year less than \$1,000,000 and gross assets at year end of less than \$3,000,000 to file a Form 990-EZ, modified in key ways, in lieu of the 990. Many will argue that this would exclude too many organizations from the full blown reporting of the Form 990, but I believe the response to that would be to utilize the Form 990 Core Form for most of these filers and modify the reach and extent to which the full Form's ancillary Schedules are required. The full blown Form 990 is too comprehensive for most of the sector's small organizations.

Eliminate or Streamline Schedule F, Statement of Activities Outside the United States

One of the most significant changes made by the redesigned form was the additional reporting pertaining to foreign activities and investments. Although many exempt organizations do not engage in foreign activities and thus are not subject to this additional reporting, for the many that do engage in relatively small amounts of foreign activity, the Schedule F reporting is daunting. For organizations with significant foreign activities it is not only difficult but extremely burdensome due to having undergone numerous reporting changes yielding evolving instructions and new learning curves each year.

The rules for determining when an organization is required to complete Schedule F have been altered significantly several times over the four filing years that the Redesigned Form 990 has been in place, requiring preparers each year to reacquaint themselves with new reporting triggers that lead to the Schedule's employ. In addition, the Schedule has for the last two years

asked if filers are responsible to report to the IRS upon any of six additional IRS Forms involving ownership in or transfers with foreign entities. The complexity of those tax Forms is well beyond the purview of most exempt organizations professionals, indeed of most tax professionals overall. Furthermore, as investment vehicles grow in complexity across the commercial sector, it is not uncommon for exempt organizations to have their reserves or endowment funds partially placed in investment partnerships that have some interests in foreign corporations.

In my experience, organizations of all size are struggling with both the “triggers” to the Schedule F (which determine when the schedule must be completed) and how to complete its Parts when they do apply. By way of example, it is not uncommon for U.S. groups working on issues that reach across the border to Canada to spend hours of preparation time detailing the expenses and receipts (for example from materials carried to meetings in Canada for which a charge is made) of work of theirs undertaken in our neighbor’s borders (assuming the total of same is \$10,000). Similarly, secondary schools who conduct student field trips in which a border crossing occurs find that their 990 reporting costs are exponentially higher in years in which such programming occurs versus those in which it does not.

This is one arena of reporting in which the benefits of the reported information do not presently outweigh the burden of compiling and gathering the information. The information collected by the IRS on Schedule F is unlikely to be of assistance to the IRS or other federal agencies with respect to combatting terrorism and/or promoting exempt organizations tax compliance. Its completion is not only a burden but a disincentive for organizations to conduct programming or participate in activities with connection to non-U.S. jurisdictions. For all the aforementioned reasons, this Schedule should be eliminated or its scope substantially reduced.

Eliminate the Statement of Functional Expenses

In the course of the public’s participation on the redesign of the Form 990, one of the most common complaints regarding the Form’s burden was the requirement that 501(c)(3) and 501(c)(4) organizations report expenses by both type or class of expenditure, and also by *function*. However, the Redesigned Form did not alter that requirement and it, like its predecessor, requires these organizations to report each class of expense they incur allocated between “program services,” “management and general,” and “fundraising.” The chorus of valid comments against this requirement that came in during the redesign process highlighted that the information captured by such “functionalization” was ill-documented, unbelievably subjective, and all-too-often geared to the desire to appease donors or meet aspirational criteria employed by charity watch-dog groups. Aside from the charity watch-dog groups (who themselves have come around to the position I now assert), there was virtual unanimity that this requirement should be struck from the Redesigned Form.

In the course of finalizing the Redesigned Form, the IRS bowed to the requests of State regulators and did not remove the columns by which functionalized expenses are reported. The States' concern was that many 501(c)(3) and some 501(c)(4) organizations who solicit in their jurisdictions are subject to State law reporting requirements, which typically include the responsibility to report total fundraising expenses or fundraising and management expenses versus program expenses. Filers who complete the Form 990 (but not the 990-EZ) have this data "readily available" from their completed Form, but those who do not complete the Form 990 typically must be provided an additional sheet by the State to complete. A point perhaps overlooked by the States in seeking the retention of the 990's functionalized expense reporting is that the Redesigned Form provides more detail on professional fundraisers and fundraising events and activities (including expenses incurred) than reflected on the predecessor form.

Given the lack of benefit to the IRS of requiring this information from all 501(c)(3) and 501(c)(4) filers, the burden it places on the filing sector to either have contemporaneous documentation systems in place or to undertake laborious post-year end processes, and the growing understanding that such reporting brings little value to the table, it is appropriate for the IRS to no longer require this information.

Regarding the Schedule R, One Aspect of Schedule L Reporting, and The Complexity of these Two Schedules' Definitions

Large complex institutions have repeatedly (and validly) opined a further wish – that reporting on Schedule R of transactions undertaken with "related organizations" be made mechanically simpler. That concern rarely vests with small and medium size organizations. An overall observation I would make with respect to Schedule R reporting of related organizations transactions that affects all filers is that in the instance where a "related organization" is also an "interested person" for purposes of reporting business transactions on Schedule L, unnecessary duplication results. One way the IRS could encourage compliance and reduce burden in getting disclosure of such transactions is to except from Schedule L Part IV's definition of "interested persons," all "related organizations." Alternatively, the reporting thresholds between the two Schedules could be synchronized.

There is no doubt that a public interest is served (and compliance promoted) by having filers detail transactions undertaken with parties who are connected to their insiders. In my recommendations I note that the IRS should provide education of the sector to emphasize that reporting of such transactions does not imply that the transaction is "bad." I have further recommended that the IRS simplify the Schedule L definitions or provide materials that guide preparers through their parameters. To access preparers' experience as we approach the close of the fourth filing season of the Redesigned 990, I would suggest that the IRS seek public

comments as to what burden-reducing improvements could be made in seeking the valid data now sought by both Schedules L and R.

V. Conclusion

In the few short years of its employ, the Redesigned Form 990 has brought a better “form” to reporting organizations for their completion and the public and regulators’ use. For the most part, the data sought on the reconfigured form promotes greater transparency and much more fully-fleshed out and relevant information on filing organizations. That has led to individual organizations having an increased appreciation of exempt organization compliance points, particularly related to management and governance overall. It has also led to the IRS (and other regulatory agencies) having better access to specific information that Congress has required by statute or policymakers have encouraged as being relevant to activities and trends that the IRS (and/or Congress) wishes to explore.

The “cost” to the filing sector of the Form’s redesign has been a steep learning curve and the need for filing organizations to be more participatory in the completion of the filing. Over the course of the first several filing seasons, it has become apparent that many organizations can prepare the bulk of the filing themselves and successfully file a complete and accurate return. Based on my experience, it is likely to take several more years for the sector to have widely mastered the learning curve, adequately planned for the increased burden of the filing as a cost of exemption, and fully realized that gaps in the paid professional community may require them to move to self-preparation and/or utilization of more experienced professionals on a consultative basis.

The Redesigned Form has achieved much of what it was intended to do. However, further improvements could and should be made to reduce unnecessary burden in a few areas and tailor the reporting to the size of the reporting organization. I believe that the five specific recommendations made above, along with the suggestion that the IRS seek comments on ways to minimize Schedule L and Schedule R burden, would address most of these concerns and improve the Form 990 even more.