

## **New IRS Form 990: Promoting Good Governance**

The Internal Revenue Service (the “Service”) has significantly redesigned the Form 990, the annual return for nonprofit entities. The impetus for redesigning the Form 990 was to increase tax compliance as well as make exempt organizations more transparent and accountable to the public. This memorandum will focus on the “Governance, Management, and Disclosure” section (Part VI) of the redesigned Form 990. The questions in Part VI relate to specific policies and procedures that the Service believes promote good governance. Since the 990 is a public document, the way in which organizations answer these questions will have a strong impact on how they are perceived by their donors, other organizations including funders, and, perhaps, state regulatory agencies.

Beginning with the 2008 tax year, the Service’s redesigned Form 990 is being phased in over a three year period with the largest organizations leading the way. The phase in for the new Form 990 is as follows:

	<u>Gross receipts</u>	<u>Assets</u>
2008 tax year (filed in 2009)	Between \$25,000 and \$1 Million	Less than \$2.5 million
2009 tax year (filed in 2010)	Between \$25,000 and \$500,000	Less than \$1.25 million
2010 and later tax years	Between \$50,000 and \$200,000	Less than \$500,000

Organizations that fall below these thresholds may file the Form 990-EZ which does not contain the same governance inquiries. After the phase-in period is over, however, only organizations with less than \$200,000 in gross receipts and less than \$500,000 in total assets will be able to avoid responding to these questions.

### **The Governance Questions**

Part VI of the Form 990, attached to this memo, now requires nonprofit entities to respond to a laundry list of questions related to the governance of the organization, including the following:

1. How many members of the governing board are independent?
2. Does the governing board review the organization’s tax filings?
3. Does the organization have a written conflict of interest policy?
4. Does the organization require regular disclosure of potential conflicts?
5. Does the organization have a written whistleblower policy?
6. Has the organization identified persons to whom whistleblowers may voice concerns?
7. Does the organization have a written document retention and destruction policy?
8. What process does the governing board use to determine compensation for its chief personnel?
9. How does the organization make its tax filings (forms 1023 and 990) available to the public?
10. How does the organization make its governing documents (articles and bylaws), conflict policy, and financial statements available to the public?

11. Does the organization keep records related to meeting of its governing body and committees with authority to act on behalf of the governing body?

For each of these questions, there is an implicit “correct” answer, and, in our opinion, all organizations should consider whether their practices and policies are consistent with what the Service views as best practices and whether they should enact or update those policies or practices now. First, you should focus on the specific policies about which Form 990 inquires: a conflict of interest policy, a whistleblower policy, and a document retention and destruction policy. Although particularly small organizations may find some of this pointless, it can be done without significant effort.

### **Conflict of Interest Policy**

A conflict of interest arises when a person in a position of authority within an organization, such as an officer, director, or manager, may benefit financially from a decision that he or she is empowered to make. Included are indirect benefits to family members or to other entities with which the person is affiliated. Organizations should have a policy that defines conflict of interest, identifies the classes of individuals within the organization covered by the policy, facilitates disclosure of information that may help identify conflicts of interest, and specifies procedures to be followed in managing conflicts of interest.

An organization’s conflict of interest policy should be written, define what a conflict is, describe who may have a conflict, require annual disclosure of potential conflicts and prompt disclosure of real conflicts, and prohibit conflicted directors, officers, or key employees from making final decisions on matters related to the conflict. We can help you with adoption of a conflict policy, if your organization does not have one. Alternatively, the Service has released a model policy which you can find on the IRS website, [www.irs.gov](http://www.irs.gov).

### **Whistleblower Policy**

The governance questions suggest that an organization should have a written whistleblower policy. Such a policy encourages employees and volunteers to come forward with credible information on illegal practices or violations of adopted policies of the organization, specifies that the organization will protect persons who do so from retaliation, and identifies those staff or board members or outside parties to whom such information can be reported. Particularly for organizations with small or non-existent staffs, it may seem silly to have such a policy. On the other hand, the policy can be very simple and, so long as it is in writing, it will allow the organization to answer the question “yes.”

### **Document Retention and Destruction Policy**

A document retention and destruction policy identifies the responsibilities of employees, volunteers, board members, and outsiders for maintaining and documenting the storage and destruction of the organization’s documents and records. Again, the Form 990 only asks

whether the organization has a written document retention and destruction policy. Thus, for small organizations particularly, a very simple written policy could be crafted, and we would be happy to assist your organization in implementing such a policy.

### **Questions related to Transparency Practices**

The Form 990 also inquires as to how and whether an organization makes its Forms 990 and 1023, governing documents, and conflict of interest policy available for public inspection, whether its board contains independent members, whether it keeps minutes of meetings, how it sets compensation, and whether it reviews the organization's tax filings. Implicit in these questions are expectations about how organizations should conduct themselves. Each organization should conduct a review of its operations to make sure they are consistent with best governance practices.

### **Conclusion**

As the calendar year comes to a close, we recommend that you evaluate the governance practices and policies of your organization, using the Form 990's inquiries as a guidepost.

*For more information on these issues, please contact one of our attorneys at 212-566-3200 or by email.*

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