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Via Email to Form990Revision@irs.gov
and via U.S. Postal Service

Form 990 Redesign
ATTN: SE:T:EO
1111 Constitution Ave., N.W.
Washington, DC 20224

Dear Sir or Madam:

We write for the purpose of providing comments on the proposed revision of IRS Form 990.

The proposed revision is a thoughtful and comprehensive effort to rethink this important form and reflects an enormous amount of time and consideration by the Exempt Organizations branch. We are confident that state and federal regulators, exempt organizations and their various stakeholders will benefit from the added clarity and transparency of the new form. We welcome this opportunity to offer suggestions and recommendations for refinements and improvements to the draft.

We have organized our comments sequentially, by Part, Line and Schedule. Although our comments address a number of issues, they are necessarily selective and not exhaustive. Many of the points we might otherwise make have already been well made by others.

Part I.

Lines 8b and 19b. We propose that Part I, Lines 8b and 19b be deleted.

Line 8b seeks a quantification of an organization's compensation to officers, directors, trustees and other key employees as a percentage of program service expenses. Line 19b seeks a quantification of an organization's fundraising expenses as a percentage of total contributions. The reason for requesting these calculations is unclear, and therein lies the problem. Because the underlying information is provided and readers of Form 990 can easily run any calculations they wish, why does the IRS want to focus attention and significance on these two calculations?

Exempt-organization clients of all sizes and from different sectors have expressed to us a significant concern that the creation of these metrics on Form 990 will encourage donors, private foundations and other funders of tax-exempt organizations to (a) confuse this data with accomplishment and success and (b) set arbitrary funding thresholds using data that may or may not be indicative of an organization's efficiency or efficacy.

There are countless situations in which the requested statistics would not present fair or useful data, yet because of the nature of Form 990, an organization has no opportunity to explain why that is so.

For example, in a small organization where the Executive Director is also the only program officer, it may be that the program services compensation to the Executive Director (Part V, line 5, column (b)) accounts for all or most of the organization's program service expenses. Similarly, an organization that conducts worthwhile but unpopular charitable activities or an organization that is establishing itself within a community may have an unusually high ratio of fundraising expenses. By requiring such organizations to report certain expense ratios on the front page of the new Form 990, the form would place a great deal of emphasis on the ratios without providing the organization with any opportunity to contextualize them. Although requiring this information on Form 990 may not rise to Constitutional proportions, it is certainly a step onto a slippery slope. One implication of requiring the disclosure is that these expense ratios are, for some reason, meaningful indicators of an organization's worthiness as a donee, even though that may or may not be the case. In turn, worthy organizations may find themselves disqualified from receiving gifts or grants from some funders based solely on irrelevant or misleading statistics that appear on the front page of the new Form 990.

Part III.

Line 3b. We propose that Part III, Line 3b be deleted.

Line 3b asks those organizations with a conflict of interest policy to disclose the number of transactions reviewed under the policy and related procedures during the year. It is unclear what purpose is served by this question. Does the review of a large number of conflict transactions mean that the organization is well governed or poorly governed? Does having no conflict transactions mean anything? It is undoubtedly important that an organization have a conflict of interest policy. However, we do not believe Form 990 should ask organizations to present statistical conflicts information that may appear, needlessly, to carry a negative connotation. One risk of such a question is that organizations may choose to adopt narrow definitions of conflicts of interest in order to reduce the number of conflict transactions that must be reviewed and, in turn, to reduce the number of conflict transactions that must be reported on Line 3b. We do not think Form 990 should create *disincentives* for organizations to bring transactions within their conflict of interest policies.

Line 9. We propose that Part III, Line 9 be deleted.

Line 9 asks whether the organization has an audit committee. The decision whether to have an audit committee may be driven by state law requirements or the nature and size of the organization itself. (The draft instructions recognize the influence of state law by recommending that organizations check whether state law requires an audit committee.) Furthermore, the board of a small organization may serve as an audit committee, or a board may delegate the audit function to another committee (e.g., the finance committee or the executive committee). The concept of "best practices" must be adapted to the needs and structure of each organization; good governance is not a "one-size-fits-all" proposition. Yet Line 9 suggests strongly that the absence of an audit committee is somehow a "bad" governance practice, when in fact a decision not to have an audit committee may be grounded on sound, independent advice of counsel and much thought and deliberation.

Line 10. We propose that Part III, Line 10 be modified – e.g., to ask whether the organization's governing body or a committee of the governing body has been provided with the opportunity to comment on a draft of Form 990 prior to filing.

Line 10 asks whether the organization's governing body "reviewed" the Form 990 before it was filed. The implication of this question is that an organization's entire board (no matter how large) is now expected to review the Form 990 before it is filed. We question how an organization could ascertain that its governing body had indeed "reviewed" Form 990. Would it be sufficient simply to circulate the draft document, or would it be necessary to seek written confirmation of the review? If the draft Form 990 is altered on account of the review, would it be necessary to circulate revised drafts for further full-board review until there are no more comments? Furthermore, we question whether all board members are qualified to "review" the Form 990, a task more commonly entrusted to qualified accountants and attorneys, board members on the audit, finance or executive committee, and/or staff with relevant expertise. We also question whether there will be adequate time to permit a review by the full board of an organization.

We believe that a modified question concerning the preparation of Form 990 – focusing on the opportunity of the governing body or a committee to comment on a draft of Form 990 prior to its filing – would adequately serve the purpose of promoting board-level involvement in the preparation of Form 990.

Part VII.

Lines 11 and 12. We propose that Part VII, Lines 11 and 12 be deleted.

Line 11 asks whether the organization has a written policy or procedure to review the organization's investments or participation in disregarded entities, joint ventures, or other affiliated organizations (exempt or non-exempt). Line 12 asks whether the organization has a

written policy that requires the organization to safeguard its exempt status with respect to its transaction and arrangements with related organizations. Both questions seem to imply that an organization is somehow remiss if it lacks written policies or procedures of the type described. In our experience, freestanding written policies or procedures to address those issues are uncommon. When an organization enters into arrangements of the type contemplated by Lines 11 and 12, it is common practice to seek advice of counsel on a legally sound and appropriate course of action. We find that such arrangements are not entered into lightly by most organizations.

Furthermore, a new set of essentially generic policies – crafted in a vacuum to enable an organization to answer "Yes" to a question on Form 990 – is unlikely to provide any meaningful benefit to a board or an organization. And for many organizations, the contemplated policies would be irrelevant in any event, simply because the contemplated issues either do not arise at all or arise with great infrequency. What is important, we believe, is that boards receive orientation and that boards and senior staff receive periodic training to heighten awareness of an array of key legal issues (e.g., private benefit, private inurement, commerciality and unrelated business income tax).

Part VIII.

Line 6. We propose that Lines 3a and 3b of Part VII-A of Form 990-PF (the excess business holdings questions for private foundations) be adapted to Part VIII, Line 6 of the proposed Form 990.

Line 6 asks each supporting organization and each sponsoring organization of donor advised funds to report whether the supporting organization or a donor advised fund had excess business holdings during the year. This question does not address the circumstances in which excess business holdings may not result in the imposition of an excise tax (e.g., if the holdings have been donated during the preceding five years or if the holdings are "grandfathered") and, as such, the question is misleading by suggesting that an organization may be liable for the excise tax on excess business holdings when it is not. The approach used in Form 990-PF is more nearly reflective of the legal issues associated with an organization's ownership of excess business holdings.

Lines 13a and 13b.. We propose that Part VIII, Lines 13a and 13b be harmonized with one another. For example, there could be one question, asking simply this: "How many Forms 8282 did the organization file during the tax year on account of the sale, exchange or other disposition of tangible personal property?"

Line 13a asks whether the organization sold, exchanged or otherwise disposed of tangible personal property for which it filed Form 8282. If the answer to Line 13a is "Yes," Line 13b asks the organization how many Forms 8282 the organization filed during the tax year. The second question does not necessarily follow from the first, because Form 8282 is required for all

donated property (other than cash and publicly traded securities) that is disposed of within three years of the gift, not just tangible personal property. It appears that the "disconnect" between Lines 13a and 13b may simply have been a drafting error.

Schedule D, Part IX

The heading of Part IX reads: **Organizations Maintaining Donor Advised Funds *Or Other Similar Funds or Accounts"*** (emphasis added). That heading is confusing, particularly because the Pension Protection Act of 2006 goes to great lengths to define donor advised funds. *See* IRC Section 4966(d)(2). We propose deleting the clause, "Or Other Similar Funds or Accounts."

Schedule D, Part X

Instructions. We propose that the instructions to Schedule D, Part X be revised to reference SFAS 116 (discussed below) and otherwise contextualize the questions being asked in Part X.

Lines 1 and 2 of Schedule D, Part X ask whether the organization reports revenue or assets on account of contributions of art, historical treasures or similar assets. The answer to those questions depends on an organization's application of SFAS 116.[1] If an organization answers "No" to Line 1 or Line 2, it ordinarily would be required by SFAS 116[2] to provide certain financial statement disclosures. Additionally, an organization might answer "Yes" to one or both of those questions simply because it does not recognize revenue or an asset on account of *all* the art, historical treasures or similar assets received or held by it. In that event, the organization might also be required to provide certain financial statement disclosures, to account for the art, historical treasures and similar assets that it does *not* treat as revenue or an asset for accounting purposes. Those financial statement disclosures, in turn, are requested in Line 3.

We believe it would be helpful to all users of Form 990 if the instructions to Schedule D, Part X provided an explanation of SFAS 116 sufficient to indicate that answering "No" to Lines 1 and 2 is consistent with generally accepted accounting principles, provided appropriate disclosure (the disclosure requested in Line 3) is contained in the financial statements. The instructions could also explain that some organizations may make the disclosure requested in Line 3 when they have answered "Yes" to Lines 1 and 2. We are concerned that the

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1 The proposed instructions for the main part of the new Form 990 (page 8, Accounting Methods) (the "Proposed Main Instructions") preserve the language of the current instructions, stating that that an organization should "generally use the same accounting method on the return to figure revenue and expenses that it regularly uses to keep its books and records." The Proposed Main Instructions, like the current instructions to Form 990, make specific reference to SFAS 116 and appear to accept the use of SFAS 116 principles for tax reporting purposes. However, neither the Proposed Main Instructions nor the proposed instructions for Schedule D, Part X explain the aspects of SFAS 116 applicable to the accounting treatment of works of art, historical treasurers and similar assets.

2 *See* SFAS 116, paragraphs 11-13 and 26-27.

present lack of contextualization will leave some readers of Form 990 (possibly including some organizations seeking to complete the form) confused about the import or intention of Schedule D, Part X.

Line 3. We propose that Schedule D, Part X, Line 3 be revised to request "the text of the note, if any, to the organization's audited financial statements which describes the organization's treatment for accounting purposes of its holdings of art, historical treasures and other similar assets." We note that the amount of space provided for the response may be inadequate for some institutions to quote the note in its entirety.

Line 3 requests the "text of the footnote to the organization's audited financial statements that discusses the organization's holdings of art, historical treasures and other similar assets." That question could be framed more precisely to account for certain standard terminology employed in financial statements ("note" rather than "footnote") and for certain variable factors (e.g., the possibility that an institution does not have audited financial statements or that it is not required to have a note in its financial statements concerning its collections). Additionally, the word "discusses" does not capture the essentially descriptive quality of typical financial statement notes.

Schedule F, Part I

Line 5. We propose that Schedule F, Part I, Line 5 be deleted.

Line 5 requests a listing of all foreign individuals and organizations that received a grant or assistance and are related (by blood, marriage, adoption or employment) to any person "with an interest" in the donor organization, such as a "donor, trustee, creator, highly compensated employee, or member of the selection committee." We do not see the rationale for this disclosure item. Is the IRS concerned about excess benefit transactions under IRC Section 4958? If so, other aspects of the proposed (and existing) Form 990 address IRC Section 4958 issues. Is the question intended to provide added transparency? If so, there is no prohibition (nor should there be) on grants being made to an organization where some relationship exists, say, between a staff member of that organization and a donor, trustee or staff person of the grantor organization. If the concern is conflicts of interest, the organization has already responded as to whether it has a conflict of interest policy, and, in any event, the rules governing conflicts of interest reside in state law and, to some degree, in IRC Section 4958. Finally, this question is so broad that every organization that makes grants or provides assistance (e.g., emergency relief or microcredit lending) to foreign organizations or individuals will need to maintain up-to-the-minute family and employment trees of all donors, trustees, staff, selection committee members, etc., even in cases where no one with a conflict of interest participates in the decision-making process resulting in a particular grant of money or assistance. This surely cannot be the intent or desired result of asking this question, and it surely does not represent "best practices."

Schedule F

Specific Instructions. In the Specific Instructions to Schedule F, we propose that the definition of "recipients located in a foreign country" be limited to foreign organizations that are not recognized as exempt organizations described in Section 501(c).

The term "recipients located in a foreign country" is defined, in subdivision (2) of the first sentence of the second paragraph of the Specific Instructions, to include any organization if at least one-half of its activities take place in a foreign country or are directed to persons in a foreign country. In other words, an organization filing Form 990 would be required (in order to decide whether Schedule F applies and in order to complete it if does) to determine the degree to which each grantee organization receiving more than $5,000 – even a grantee recognized as an exempt organization described in IRC Section 501(c) – conducts activities outside the U.S. or directs its activities toward non-U.S. persons.

The Internal Revenue Code and the Treasury Regulations impose special requirements for grants by private foundations to foreign organizations that lack Section 501(c)(3) status. *See* IRC Section 4945(d)(4). There also has been an increasing focus on the practices of public charity grantmaking abroad to assure that charities "know their non-U.S. grantees." The Specific Instructions to Schedule F, in effect, would create an entirely new legal requirement, one that does not exist in the law – i.e., that organizations that file Form 990 (a) undertake an analysis of where grantees described in IRC Section 501(c) perform their work and (b) report this information to the IRS. This is not only a remarkably burdensome activity, but more importantly, it appears to create a new legal obligation for which there is no corresponding basis in law. We question the imposition of such a burden, and we question the appropriateness of requiring U.S. organizations (in effect) to investigate grantees already recognized by the IRS as tax-exempt and report to the IRS about the non-U.S. activities of those grantees.

Schedule M

Instructions and Lines 1 through 3 and Line 19. Our multiple proposals concerning the Schedule M Instructions and Lines 1 through 3 and Line 19 appear below, under the heading "Proposals."

The subheading on the first page of Schedule M says it is to be completed by organizations that "report more than $5,000 of non-cash contributions on Form 990, Part IV, line 1g." However, the proposed instructions to Schedule M are more expansive and state, *in addition*, that Schedule M must be completed by any organization that received "any contributions of art, historical treasures or similar assets, or qualified conservation contributions, regardless of whether it reported any revenues for such contributions in Part IV." Hence, there is an inconsistency between the subheading on the first page of Schedule M and the instructions to the Schedule.

Confusion about the intended scope of Schedule M is exacerbated by the request in Columns (b) and (d) of Part I of Schedule M for "Revenues reported on Form 990, Part IV, line 1g" and "Amount reported on Form 990, Part VI." A university, museum, library, botanical garden, historical society or other organization that excludes art, historical treasures and similar assets from its statement of revenues and its balance sheet under SFAS 116 (described above) would ordinarily report no revenue or assets on account of the donation of art, historical treasures and similar assets. Hence, the implication of the Column (b) and (d) headers is that donations need be reported only to the extent they are associated with revenue and/or assets that are reflected in an organization's financial statements and, in turn, in its Form 990. We would view that to be the more appropriate interpretation of Schedule M, consistent with other reporting requirements of Form 990, were it not for the confusing instruction to Schedule M that is quoted above.

Schedule D, Part X will require universities, museums, libraries and other collecting institutions to disclose whether their art, historical treasures and similar assets are treated as revenues or assets for purposes of Form 990 and will require disclosure of any financial statement note explaining the treatment of such assets. Schedule D, Part X is sufficient (particularly if the accompanying instructions are revised in the manner proposed above) to put the IRS and other readers of Form 990 on notice that certain SFAS 116 principles have been applied to the manner in which the collection is reported for accounting purposes. It is unclear what further benefit is added if Schedule M requires disclosure of the quantity (Column (a)) of contributions whose value need not be disclosed in any event. Is it meaningful to know that an organization received 100 works of art during the year for which there is no reportable value? Or is it sufficient simply to know (per Schedule D, Part X) that the organization does not treat certain art, historical treasures and similar assets as revenue or assets and has made a financial statement disclosure to that effect, in accordance with generally accepted accounting principles? We submit that the latter form of disclosure is sufficient.

Proposal. We propose that the instructions to Schedule M be modified to be consistent with the subheading on the first page of Schedule M, thereby making it clear that Schedule M is applicable *only* to non-cash contributions that *are* reported as revenue elsewhere on Form 990. That approach is consistent not only with SFAS 116 and the reporting conventions followed elsewhere in Form 990, but also with ethical codes in the museum sector[3] and the laws

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[3] *See, e.g.,* Code of Ethics, American Association of Museums ("Proceeds from the sale of ... collections are to be used consistent with the established standards of the museum's discipline, but in no event shall they be used for anything other than acquisition or direct care of collections."); Association of Art Museum Directors, Code of Ethics ("the monies... received from the sale of any accessioned work of art must be used only to acquire other works of art").

of at least some states[4] that effectively prevent many institutions from using items in their collections as financial assets.

If Schedule M is confined only to non-cash contributions reported elsewhere as revenue, we question whether it is any longer necessary to have three "Art" categories (Lines 1 through 3) and a category for "Collectibles" (Line 19). Hence, we propose that Lines 1 through 3 and Line 19 be collapsed into a single line, covering all "Art, historical treasures, and collectibles." If the IRS nonetheless wishes to collect data on the number of fractional interest gifts of art (Line 1), it could do so simply by adding a new Line (later in Part I of Schedule M) that asks whether the organization accepted any fractional interest gifts of art. A "Yes" or "No" answer would avoid the need to delve into valuation questions about fractional interests that, under SFAS 116, may not be recognized as revenue in any event.

Alternatively, if the current instructions are retained, they should be modified to indicate more clearly that revenue and values used for accounting purposes may be used for purposes of completing columns (b) and (d).

In all events, we urge the IRS to continue its long-standing practice of respecting SFAS 116 and *not* requiring organizations to report revenue or an asset value in respect of art, historical treasures and other similar assets whose value is not reported for financial accounting purposes. It would impose an unreasonable burden on universities, museums, libraries, and other collecting institutions if they were required to obtain valuations of the property in their collections. Moreover, a practice of requiring collecting institutions to assign a fair market value to the collection would be contrary to the well-established policies behind SFAS 116 and the ethical rules noted above, all of which support the principle that institutional collections are not rightly viewed as financial assets. The proper financial reporting of institutional collections was intensively studied by the Financial Accounting Standards Board (or "FASB") and the community of universities, museums, libraries and other collecting institutions during the late 1980s and early 1990s, and the ample record developed at the time demonstrates the wisdom of the approach ultimately adopted in SFAS 116.

Line 23. We propose that Schedule M, Part I, Line 23 be modified to seek the number of Forms 8283 for which the organization during the tax year completed *Part IV, Donor Acknowledgement.*

Line 23 asks for the number of Forms 8283 received by the organization for contributions for which the organization completed *Part IV, Donor Acknowledgement.* This question does not make it clear during what period the organization must have completed Part IV

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[4] *See, e.g.,* Rules of the Regents, Section 3.27(f)(7), N.Y. Education Dept., published in Law Pamphlet 9, Appendix B (requiring a museum chartered by the New York State Education Department to apply the proceeds of deaccessioning only to the "acquisition, preservation, protection or care of collections").

of Form 8283. Hence, if an organization received Form 8283 from a donor during the tax year but did not complete Part IV of Form 8283 until the following tax year, it is unclear whether the form is covered by Line 23.

Line 29. We propose that Schedule M, Part I, Line 29 *either* be deleted *or* be reframed to ask whether the organization received any contributions of tangible personal property that it agreed to hold for a fixed term of three years or more. If the latter alternative is selected, the instructions should explain that Line 29 does not apply to gifts that are subject to retention in perpetuity, for the life or lives of particular individuals, or during any other period that is not fixed and determinable on the date of the gift.

Line 29 asks whether the organization received during the year any contribution of property that it must hold for at least three years from the date of the contribution. It appears that this question is asked on account of the three-year rule for "related use" gifts of tangible personal property. Under that rule, per IRC Section 170(e)(7) (as enacted by the Pension Protection Act of 2006), the charitable income tax deduction (to the extent in excess of the donor's basis) is ordinarily "recaptured" if a gift of tangible personal property is sold within three years of the gift. Line 29, therefore, seems to seek information that may provide an indication to the IRS that an organization is entering into agreements with donors to hold property just long enough (i.e., for not less than three years) to ensure that the property is outside the reach of the new IRC Section 170(e)(7).

Our concern is that Line 29 casts too broad a net (if the purpose is the one we surmise), because it will require charities to include in the figure (a) gifts of real property and securities that are donated on condition that they be retained for periods longer than three years (even though such gifts are not subject to the "related use" rules and IRC Section 170(e)(7)) and (b) gifts of tangible personal property that must be retained in perpetuity, for the life of particular individuals or until the occurrence of a particular event – i.e., gifts that must be retained for reasons utterly unconnected with any desire to avoid the effects of IRC Section 170(e)(7).

We note that there may legitimate reasons for an organization to agree to retain a gift for a fixed period of time. For example, a donor and a museum might agree that a new generation of curators ought to have the flexibility to evaluate whether retention is any longer appropriate and agree that a fixed term of years is the best way to calculate when a new generation of curators will be in place. Or a museum and an elderly donor might agree that retention for a fixed term of years is an appropriate compromise between retention in perpetuity (which the museum believes to be too long a period of time) and retention for the donor's remaining lifespan (which the donor believes to be too short a period of time). We note, too, that a fixed term of many years (e.g., a 15-year or 50-year term) would not ordinarily be adopted as an "end-run" around the three-year rule of IRC Section 170(e)(7). The IRS, we assume, is concerned about terms that last for, say, three years and one day.

Accordingly, even if Line 29 were reframed (as per our second alternative proposal above), it would still cast a net that requires an organization to report gifts that, in fact, must be retained by charity for a fixed period for perfectly legitimate reasons. We urge the IRS to keep that consideration in mind as it evaluates Line 29. It may be that there is no meaningful purpose served by requesting information of the type contemplated by Line 29, in which case it would be preferable on balance, we believe, if Line 29 were simply deleted.

Again, we appreciate the opportunity to comment on the proposed Form 990 and the Instructions.

Yours truly,

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