

Strafford

Presenting a live 110-minute teleconference with interactive Q&A

Form 990: Responding to Key Changes in the Form and Regulations

Preparing to Report Foreign Investments and JV Assets,
Meet New Compensation Thresholds, and Tackle Other Challenges

WEDNESDAY, APRIL 25, 2012

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

John Panetta, Tax Shareholder, Non-Profit Services Group, Burr Pilger Mayer, San Francisco

Gary Bode, Owner, Gary Bode, Wilmington, N.C.

Rich Ruvelson, Director, Wipfli, Minneapolis

David Lowenthal, Tax Senior Manager, Blackman Kallick, Chicago

For this program, attendees must listen to the audio over the telephone.

Please refer to the instructions emailed to the registrant for the dial-in information. Attendees can still view the presentation slides online. If you have any questions, please contact Customer Service at 1-800-926-7926 ext. 10.

Conference Materials

If you have not printed the conference materials for this program, please complete the following steps:

- Click on the + sign next to “Conference Materials” in the middle of the left-hand column on your screen.
- Click on the tab labeled “Handouts” that appears, and there you will see a PDF of the slides for today's program.
- Double click on the PDF and a separate page will open.
- Print the slides by clicking on the printer icon.

Continuing Education Credits

FOR LIVE EVENT ONLY

Attendees must listen to the audio over the telephone. Attendees can still view the presentation slides online but there is no online audio for this program.

Attendees must stay on the line for at least 100 minutes in order to qualify for a full 2 credits of CPE. Attendance is monitored as required by NASBA.

Please refer to the instructions emailed to the registrant for additional information. If you have any questions, please contact **Customer Service** at 1-800-926-7926 ext. 10.

Tips for Optimal Quality

Sound Quality

For this program, you must listen via the telephone by dialing **1-866-873-1442** and entering your PIN when prompted. There will be no sound over the web connection.

If you dialed in and have any difficulties during the call, press *0 for assistance. You may also send us a chat or e-mail sound@straffordpub.com immediately so we can address the problem.

Viewing Quality

To maximize your screen, press the F11 key on your keyboard. To exit full screen, press the F11 key again.

Form 990: Responding to Key Changes in the Form and Regulations Seminar

April 25, 2012

John Panetta, Burr Pilger Mayer
jpanetta@bpmcpa.com

Gary Bode, Gary Bode CPA
gbode@ec.rr.com

Rich Ruvelson, Wipfli
rruvelson@wipfli.com

David Lowenthal, Blackman Kallick
dlowenthal@blackmankallick.com

Today's Program

2011 Changes To Form 990
[John Panetta and Gary Bode]

Slide 7 - Slide 28

Form 990-Related Issues From The Latest IRS Work Plan
[Rich Ruvelson]

Slide 29 - Slide 36

Persistent Problems From 2009, 2010 Tax Year Form 990
[Rich Ruvelson]

Slide 37 - Slide 40

Hot-Button Issues With Form 990 For IRS Examiners
[David Lowenthal]

Slide 41 - Slide 53

John Panetta, Burr Pilger Mayer
Gary Bode, Gary Bode CPA

2011 CHANGES TO FORM 990

Schedule F: Foreign Activities

- I. Part IV - Trigger question
 - A. Q 14 b new clause at end
 - B. Does organization have “aggregate foreign investments valued at \$100,000 or more”?
- II. Schedule F instructions
 - A. Value = Book value, not FMV
 - B. Report investments as a group on a regional basis - separate from other activities
 - C. Region = “Legal domicile of flow through entity,” i.e. country whose laws govern entity’s internal affairs

Schedule F: Foreign Activities (Cont.)

III. Schedule F

- A. Part I - Complete columns: a (region), d (investment) and f (amount rounded to nearest \$1,000)
- B. Part IV - Respond to questions about filing forms to report foreign activities (926, 5471, 3520, 8621, 8865, 5713)

Part X Balance Sheet: Reporting On Investments, Line 12

- I. Instructions: For all entities treated as partnerships for federal tax purposes, report on Line 12 organization's ending capital account per K-1 schedule

- II. GAAP will record FMV of interest in entity.

- III. Difference between GAAP and tax should be presented in Schedule O and captioned as to whether the difference affects unrestricted, temporarily or permanently restricted assets.

Schedule D, Part II: Conservation Easements

- I. Recent changes to Form 990, Schedule D, Part II
 1. No longer asks about residential developments and golf courses
 2. Now only relates to conservation easements
 3. Acreage of controlled easements is now defined as easements eligible for a Sect. 170 deduction (26 USC § 170 - CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS).
 4. Requires an explanation of, and/or a financial statement footnote, delineating the organization's conservation easements policies
 5. Expands the hours of conservation easement monitoring to include both staff and volunteers

Schedule D, Part II: Conservation Easements (Cont.)

- I. Where to look for guidance on conservation easements and Form 990, Schedule D, Part II reporting
 1. Internal Revenue Code and Treasury regulations
 - a. *170(h)(4)(B)*
 - b. *170(h)(4)(B)ii*
 2. Tax Court rulings
 - a. In 2012; the easement must be perpetual and not subject to amendments that can extinguish it by mutual agreement.
 3. State laws
 - a. State laws determine effect of the deed.
 - b. Federal law deals with the tax treatment.
 4. IRS instructions

Schedule D, Part II: Conservation Easements (Cont.)

- I. Schedule D, Part II, Line 1
 1. Purposes of conservation easements held
 2. Now limited to Sect. 170 definitions
 3. Form 990 evolves; Part XIV allows for a detailed explanation of any variant not specifically listed.

Schedule D, Part II: Conservation Easements (Cont.)

I. Schedule D, Part II, Line 2

1. Total number of conservation easements (held) on the last day of the tax year
2. Total acreage under control
 1. *Acreage is now limited to conservation easements qualified under Sect. 170.*
3. Number of conservation easements on a certified historic structure
4. Number of conservation easements included in (c) that were acquired after 8/17/06 and are not on a historic structure listed in the National Register

Schedule D, Part II: Conservation Easements (Cont.)

I. Schedule D, Part II, Line 3

1. Number of conservation easements modified, transferred, released, extinguished or terminated by the organization during the tax year
 1. Provide an explanation in Part XIV
 2. If an easement has been extinguished, it may not have been given in perpetuity. An extinguished easement could negate the charitable tax deduction of the donor and place the organization in jeopardy for accepting an inappropriate conservation easement.

II. Schedule D, Part II, Line 4

1. Number of states where property subject to conservation easement is located
 1. *Remember, the states control the deed. A higher number of states means more due diligence is required by the organization.*

Schedule D, Part II: Conservation Easements (Cont.)

I. Schedule D, Part II, Line 5

1. Does the organization have a written policy regarding the periodic monitoring, inspection, handling of violations, and enforcement of the conservation easements it holds?
 1. Inspection means being on-site.
 2. Violations could be federal, state or contractual.
2. The speaker's opinion only here: When the organization accepts a conservation easement, it incurs multiple responsibilities. I believe the IRS is actively discouraging continued donor rights, which could be part of a conspiracy to falsely claim charitable deductions. It also seems like they expect to pursue organizations that can't or won't take on the responsibilities incumbent with conservation easements.

Schedule D, Part II: Conservation Easements (Cont.)

I. Schedule D, Part II, Line 6

1. Staff and volunteer hours devoted to monitoring, inspecting and enforcing conservation easements during the year
 1. Note that the organization has to incur expense to track time for both staff and volunteers

II. Schedule D, Part II, Line 7

1. Amount of expenses incurred in monitoring, inspecting and enforcing conservation easements during the year
 1. I wouldn't recommend estimating this figure. The organization should implement a formal system to track this expense.

Schedule D, Part II: Conservation Easements (Cont.)

I. Schedule D, Part II, Line 8

1. Does each conservation easement reported on line 2(d) above satisfy the requirements of Sect. 170(h)(4)(B)(i) and Sect. 170(h)(4)(B)(ii)?
 1. Restrictions that preserve the entire exterior of a building (including the space above it) and prohibit any changes to the exterior that are inconsistent with the historical character
 2. Both parties agree in writing, under penalties of perjury, that the donee's exempt purpose is environmental protection, land conservation, open space preservation or historic preservation; and that the donee has the resources and commitment to enforce the restrictions.
 3. There are a qualified appraisal, photographs of the entire building exterior, and a description of all development restrictions relating to it (such as zoning laws, restrictive covenants, etc.).

Schedule D, Part II: Conservation Easements (Cont.)

I. Schedule D, Part II, Line 9

1. In Part XIV, describe how the organization reports conservation easements in its revenue and expense statement and balance sheet; and include, if applicable, the text of the footnote to the organization's financial statements that describes the organization's accounting for conservation easements.
 1. The IRS is looking for consistent financial reporting treatment across the entire Form 990. It does not proscribe that treatment *per se*.

Part VIII: Statement Of Revenue

- I. Report distributive share of investment income from joint ventures on specific lines
 - A. Line 3: Interest and dividends
 - B. Line 4: Income from investment of tax-exempt bond proceeds
 - C. Line 5: Royalties
 - D. Line 7: Gains

Glossary: Grants And Assistance

- I. For purposes of Part IX, lines 1-3; Schedule F (Form 990); and Schedule I (Form 990). Includes awards, prizes, contributions, non-cash assistance, program-related investments, cash allocations, stipends, scholarships, fellowships, research grants and similar payments and distributions made by the organization during the tax year.
- II. It does not include:
 - A. Salaries or other compensation to employees or payments to independent contractors, if the primary purpose is to serve the direct and immediate needs of the organization

Glossary: Grants And Assistance (Cont.)

- B. The payment of any benefit by a Sect. 501(c)(9) voluntary employees' beneficiary association (VEBA) to employees of a sponsoring organization or contributing employer, if such payment is made under the terms of the VEBA trust and in compliance with Sect. 505; or
- C. Grants or other assistance to affiliates or branch offices that are not organized as legal entities separate from the filing organization.

Compensation

- I. Reportable compensation for officers and employees includes compensation reported in Form W-2, boxes 1 (Wages) or 5 (Medicare wages), whichever amount is greater.
- II. Eliminates requirement to provide addresses of officers, directors, trustees and key employees
- III. Provides that compensation should be reported for the calendar year ending with or within the organization's tax year
- IV. Clarifies that the annual increase or decrease in actuarial value of a defined benefit plan should be reported in column (F) of Section A. But, any decrease should be disregarded when determining whether the individual's total compensation was more than \$150,000, for purposes of line 4.

Substantial Contraction

Revise definition of “significant disposition of net assets” to exclude grants or other assistance made in the ordinary course of the organization’s exempt activities to accomplish its exempt purposes

Elimination Of Advance Ruling Period

- I. Under the prior regulations, in applying for recognition of tax-exempt status, an organization could request either an advance ruling or a definitive ruling on its exemption under Sect. 501(c)(3).
- II. The final regulations eliminate the advance ruling process and provide instead that an organization is publicly supported (qualifying for public charity status) in its first five years if it can show, in its application for exemption, that it could reasonably be expected to receive the requisite public support during this period. Reg. §1.170A-9(f)(4)(vii)(B), Reg. §1.509(a)-3(c)(1)

Change In Public Support Computation Period

- I. The computation period for public support has been revised from a four-year period comprising the four years before the tax year being tested, to a five-year period ending with the tax year being tested.

- II. An organization that meets a public support test for a tax year is treated as publicly supported for that tax year and for the immediately succeeding tax year. An organization that doesn't meet the test may be at risk of being classified as a private foundation as of the first day of the succeeding tax year, if it also fails the public support test for that succeeding tax year. (Reg. §1.170A-9(f)(4)(vii)(B), Reg. §1.509(a)-3(c)(1))

Change In Public Support Computation Period (Cont.)

- III. An organization that fails a public support test for two consecutive tax years will be treated as a private foundation as of the beginning of the second year of the failure (i.e., its sixth tax year), only for purposes of Sect. 507, Sect. 4940 and Sect. 6033. It must file a Form 990-PF and will be liable for the net investment tax imposed by Sect. 4940 and, if applicable, the private foundation termination tax imposed by Sect. 507(c) for its sixth tax year.
- IV. The organization will be treated as a private foundation for all purposes beginning on the first day of the third consecutive tax year of the failure. Reg. § .170A-9(f)(4)(vii)(B), Reg. §1.509(a)-3(c)(1)

Change In Public Support Computation Period (Cont.)

- V. Previously, in computing the amount of public support it received, a Sect. 501(c)(3) organization was required to use the cash accounting method to report this on Schedule A (Public Charity Status and Public Support), even if it used the accrual method to keep its books. Under the final rules, a Sect. 501(c)(3) organization must compute its public support using the same accounting method that it uses to keep its books. Reg. §1.170A-9(f)(13), Reg. §1.509(a)-3(k)

Rich Ruvelson, Wipfli

FORM 990-RELATED ISSUES FROM THE LATEST IRS WORK PLAN

IRS Exempt Organizations 2012 Work Plan

- I. The 2012 work plan focuses on where the IRS is deploying resources in 2012. The projects are in addition to permanent determinations and examinations responsibilities, including ongoing process work as well as referrals.
- II. The IRS redesigned the Form 990 to promote transparency and compliance. The new form, which was effective in tax year 2008, has provided EO with a wealth of information on exempt organizations. EO has used this information to develop risk models to assess the likelihood of non-compliance by organizations, allowing more effective use of examination resources. In FY 2012, EO will incorporate information from the revised Form 990 in the following activities:

IRS Exempt Organizations 2012 Work Plan (Cont.)

I. Compliance

A. Political activity

1. As in any election year, EO will continue its work to enforce the rules relating to political campaigns and campaign expenditures. In FY 2012, EO will combine what it has learned from past projects on political activities with new information gleaned from the redesigned Form 990 to focus its examination resources on serious allegations of impermissible political intervention. As in the past, information from outside sources about political campaign intervention will be reviewed by a committee of career civil servants. In addition, other potential violations identified through risk modeling of Form 990 data also will be sent to the committee for evaluation. The committee will focus on identifying the cases to refer for examination. EO will further refine its risk models based on the results of examinations. EO will also ensure reporting and payment compliance with Sect. 527(f).

IRS Exempt Organizations 2012 Work Plan (Cont.)

I. Compliance (Cont.)

A. Form 990-T and UBIT

1. In FY 2012, EO will be looking at organizations that report unrelated business activities on Form 990 but have not filed a Form 990-T. In addition, EO will analyze Form 990-T data to develop risk models that will help identify organizations that consistently report significant gross receipts from unrelated business activities but declare no tax due. EO will use this work in connection with a coming UBIT project.

IRS Exempt Organizations 2012 Work Plan (Cont.)

I. Compliance (Cont.)

A. Governance

1. The new Form 990 has given the IRS a great deal of information about organizational governance practices. In FY 2012, the IRS will be using this data to look at connections between certain governance practices and tax compliance.

IRS Exempt Organizations 2012 Work Plan (Cont.)

I. Compliance (Cont.)

A. 501(c)(4), (5) and (6) self-declarers

- a. These groups (social welfare organizations; labor, agricultural and horticultural groups; and business leagues, such as a chamber of commerce) can declare themselves tax-exempt without seeking a determination from the IRS. EO will review organizations to ensure that they have classified themselves correctly and that they are complying with applicable rules. In FY 2012, EO will send a comprehensive questionnaire to organizations based on Form 990 filings to assess compliance in this area.

IRS Exempt Organizations 2012 Work Plan (Cont.)

I. Legislative implementation

A. Auto-revocation for non-filers continues

1. The Pension Protection Act of 2006 (PPA) required that almost all tax-exempt organizations file an annual return or notice with the IRS every year, and provided that any organization that does not file a required return or notice for three consecutive years automatically loses its tax-exempt status. The PPA required the IRS to publish and maintain a list of revoked organizations.
 - a. In early January 2012, EO incorporated the revocation list into Select Check (<http://apps.irs.gov/app/eos/>), a new online application that consolidates three separate search pages into a single entry point.
 - i. Users can find out whether an organization is eligible to receive tax deductible charitable contributions (Pub. 78 data); has had its tax-exempt status automatically revoked; and has filed a Form 990-N annual electronic notice (e-postcard).

IRS Exempt Organizations 2012 Work Plan (Cont.)

I. Legislative implementation (Cont.)

A. Requirements for tax-exempt hospitals

1. The Affordable Care Act of 2010 (ACA) added new requirements that tax-exempt hospitals must meet to maintain their tax-exempt status. The IRS is required to review the community benefit activities of hospital organizations at least once every three years. Accordingly, EO Exam formed and trained a “review of operations” group dedicated to completing the statutorily required community benefit reviews, which began in March 2011. These reviews are not examinations, and the group does not expect to contact hospitals while conducting the reviews. Moving forward, EO will use the information gathered from the reviews for research, reporting and compliance purposes; as well as to identify areas where additional guidance, education or Form 990 changes are needed. The IRS issued Notice 2011-52 in July 2011, to address the community health needs assessment requirements and related excise tax and reporting obligations applicable to tax-exempt hospitals. The IRS continues to work with Treasury and counsel to develop guidance on the new Sect. 501(r) requirements.
2. Schedule H, Part V, B questions are not optional, with the exception of 1-7 relating to community health needs assessments.
3. Attach audited financial statements

Rich Ruvelson, Wipfli

**PERSISTENT PROBLEMS WITH
2009, 2010 TAX YEAR FORM 990**

Areas Of Continuing Difficulty For Clients And Preparers

- I. Reporting of proportionate interest in joint venture or partnership
 - A. 2010 and prior years Form 990 Parts VIII, IX and X provided that information could be reported in accordance with the organization's books and records.
 - B. For 2011, the instructions provided that reporting be done using information from Forms K-1.
 - 1. In Announcement 2012-19, the IRS made reporting using K-1 information optional for 2011.
 - C. Note that Schedules R and H require reporting based upon information from Form K-1 for 2011.

Areas Of Continuing Difficulty For Clients And Preparers (Cont.)

- I. Public support
 - A. Frequently difficult for clients to understand
 - 1. "... But, we're a 501(c)(3)."
 - B. Final regulations implimenting Form 990 revisions, TD 9549
 - a. Elimination of advance ruling period
 - b. The timeline for determining public support is four prior years and reporting year.
 - c. Same method of accounting as used for Form 990 reporting
 - d. Failure to meet test for two consecutive tax reporting years results in private foundation status on first day of third year.
 - i. Subject to IRC sections 507, 4940 and 6033 the first day of the second year

Areas Of Continuing Difficulty For Clients And Preparers (Cont.)

I. Other areas

1. Updating program service descriptions and statistics
2. Fiscal year and calendar year compensation reporting
3. Determining contribution portion of fundraising event revenue
4. Unrelated business income activity determination
5. Fundraising events vs. everyday fundraising expenses
6. Fundraising events and "quid pro quo" question
7. Lobbying expenses of organizations resulting from dues payments to other organizations not required to report lobbying

David Lowenthal, Blackman Kallick

HOT-BUTTON ISSUES WITH FORM 990 FOR IRS EXAMINERS

Audit Selection



How Do You Get Selected For Audit?

- Random selection of return
- Whistleblower
- Media attention
- Compliance check
- Single issue identification

Examinations Stink!

- Human resources: Organization's time
- Energy: Organization's focus/emotion
- Professional fees: Organization's money

All true, even if examination yields no changes!

[Data] Mining



Data Mining (Cont.)

- Isn't that hazardous to your health and bad for the environment?
- Data mining – used by exempt organizations since 2003
- Currently developing initial data models for the “new 990”
- Goal: Move beyond single issue identification

Compliance Pitfalls



Blackman Kallick Blackman Kallick Blackman Kallick Blackman Kallick



Blackman Kallick

Compliance Pitfalls: Compensation

- Part VI, lines 15a & b: Make a proper disclosure of your process as it applies to the rebuttable presumption
- Part VII: Disclose everyone and make sure it's the prior year; make the hours consistent with comp studies; make sure the benefits are properly disclosed
- Schedule J, Part I: Answer the questions and make Part III disclosures
- Schedule J, Part II: Deferred comp; agree to Part VII

Compliance Pitfalls: Part VI, Governance

- For better or worse, the IRS thinks governance is the No. 1 indicator of exempt organization taxpayer behavior
- Appear to be a practitioner of good governance (as the IRS defines it)
- Use Schedule O to make required expositive disclosures

Compliance Pitfalls: Part VIII, Revenue Reporting

- Line 11 should have as a small a number as possible.
 - Big numbers on Line 11, which is described as furthering the exempt purpose or subject to statutory exclusion, suggest indecision.
 - Other revenue is not for – “I could not decide between lines 2, 5 and 8.”

Sales of inventory belong on line 10, not line 2.

Compliance Pitfalls: Part IX, Functional Expenses

- Understand the percentages: Of program service, admin and fundraising to total expenditures
- Line 24: Keep numbers as small as possible

Compliance Pitfalls: Other Considerations

- Part V: IRS makes more on employment tax audits than any other type of audit of exempt organizations.
- Part III: Complete this section; “I like numbers, not words” is not a valid excuse.
- Schedule O: IRS claims that lots of taxpayers do not complete Schedule O, even though it is required.
- Schedule F, Part IV: Make sure you understand these questions; the penalties for non-compliance are severe.



Point Of Caution

- No discussion is complete without my caution that this information is provided for educational purposes. It should not be considered formal tax advice.