



## Important Details Regarding Changes to Form 990

## UPMIFA Implementation Issues

*Learn more inside.*



## The New Form 990

### *Life Under the Microscope for Non-Profits*

By **Reed W. Risteen, CPA**  
*Partner, Blum Shapiro*

The IRS has released its draft of the long anticipated redesigned Form 990, and the new form has created quite a buzz within the non-profit community.

The IRS goals in revamping the form were as follows:

- Enhance transparency
- Promote tax compliance
- Improve governance by non-profits

The result is a massive form (65 pages including all schedules) that requires substantially more information than before, and asks leading questions in various areas of governance that may motivate non-profit organizations to adopt additional governance policies. Non-profit organizations may now feel as if they are being viewed under a microscope, and preparation of the form will require substantially more effort to complete for both the non-profit organization and its tax preparer.

#### **Effective Date**

The form is effective for calendar 2008 year-end. The IRS has provided some relief in that Form 990EZ, which has not been revised, may be filed for 2008 by non-profit organizations with gross receipts under \$1 million and total assets under \$2.5 million. These filing thresholds will decrease over the next two years.

*Please see The New Form 990 continued on page 2.*

## *FASB Reaches Tentative Conclusions Regarding Accounting for Endowments*

By **Marcus R. Harwood, CPA and Reed W. Risteen, CPA**  
*Partners, Blum Shapiro*

The Financial Accounting Standards Board recently reached tentative conclusions regarding the accounting for donor-restricted endowments now that the model Uniform Prudent Management of Institutional Funds Act (UPMIFA) is being adopted by states, replacing the prior Uniform Management of Institutional Funds Act (UMIFA). These conclusions will be published in FASB Staff Position FAS 117-a, Endowments of Not-for-Profit Organizations: Classification of Donor Restricted Endowment Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act (FSP 117-a), and related disclosures which is expected to be issued in late summer. For purposes of this article, an “endowment gift” is defined as a gift restricted by a donor for investment in perpetuity.

*Please see FASB Reaches Tentative Conclusions continued on page 5.*

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# The New Form 990

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## The Core Form

The form's structure consists of a "core" section applicable to all organizations, along with numerous schedules that apply to specific situations. The core section of the form is organized as follows:

- **Page one** consists of a summary of the organization's mission, significant activities and revenues and expenses, making it easier for the public to access key information.
- **Page two** contains more detailed information on the organization's program service accomplishments.
- **Pages three and four** contain a series of questions, the answers to which determine which schedules are required to be filed.
- **Page five** contains detailed questions regarding tax compliance, many of which are new.
- **Page six**, perhaps the most controversial page, contains many new questions concerning organization governance.
- **Page seven** requires information about the compensation of officers, directors, trustees, key employees, highest compensated employees and independent contractors.
- The remainder of the core form consists of financial information, including a statement of revenue, statement of functional expenses and balance sheet.

## Form 990 Schedules

- **Schedule A** – Public Charity Status and Public Support
- **Schedule B** – Schedule of Contributors
- **Schedule C** – Political Campaign and Lobbying Activities
- **Schedule D** – Supplemental Financial Statements
- **Schedule E** – Schools
- **Schedule F** – Statement of Activities Outside the United States
- **Schedule G** – Supplemental Information Regarding Fundraising or Gaming Activities
- **Schedule H** – Hospitals
- **Schedule I** – Grants and Other Assistance to Organizations, Governments and Individuals in the United States
- **Schedule J** – Compensation Information
- **Schedule K** – Supplemental Information on Tax-Exempt Bonds
- **Schedule L** – Transactions with Interested Persons
- **Schedule M** – Non-Cash Contributions
- **Schedule N** – Liquidation, Dissolution, or Significant Disposition of Assets
- **Schedule O** – Supplemental Information to Form 990
- **Schedule R** – Related Organizations and Unrelated Partnerships

## Governance Policies

Continuing with its past approach of asking questions about governance rather than requiring that organizations adopt certain policies, the IRS has added the following new questions:

- Are written minutes maintained for meetings of the board of directors and each committee with authority to act on behalf of the board?
- Are there written policies and procedures to ensure that chapters, affiliates or branches are operating consistently with the organization?
- Was Form 990 reviewed by the board of directors before it was filed?
- Describe the process used to review Form 990.
- Is there a written conflict of interest policy?
- Are board members required to disclose conflicts annually?
- Is compliance with conflict of interest policies monitored and enforced? If so, how?
- Is there a written whistle-blower policy?
- Is there a written document retention and destruction policy?
- Does the compensation determination process include:
  - Review and approval by independent persons?
  - Comparability data?
  - Contemporaneous documentation of deliberations and decisions?
- Were the above compensation policies followed for top executives? Other officers and key employees?
- Is there a written policy requiring the organization to monitor investments in or joint ventures with for-profit entities to ensure they don't endanger the organization's tax-exempt status?
- Does the organization make the following available to the public and, if so, how?
  - Governing documents?
  - Conflict of interest policy?
  - Financial statements?

## Tax Compliance

The tax compliance section of the core form requires responses to compliance questions in areas of concern that the IRS has focused on in the last few years, including:

- Required deductibility disclosures for "quid pro quo" contributions
- Filing of Form 1098C for vehicle contributions
- Making Forms 1023 (exempt application), 990 and 990T available to the public

- Filing of Form 8899 for contributions of qualified intellectual property
- Compliance with backup withholding rules

## Reporting Compensation

As in the past, compensation information is required for current and former officers, directors, trustees, key employees, highest compensated employees and independent contractors. However, this information was previously located both in Form 990 itself and the previous Schedule A, although Schedule A was only required to be filed by public charities. As a result, there was no disclosure by non-charities of highest compensated employees that were not considered to be key employees.

All compensation information is now centralized in Part VII of the core form, which is required to be completed by all non-profit organizations. The good news is that the threshold for highest compensated employees has been increased from \$50,000 to \$100,000.

Compensation was previously reported based on the organization's fiscal year, whereas now it will be reported based on the employee's W-2 (or independent contractor's 1099) for the calendar year that ends during the organization's fiscal year. This is one of the few areas where the new information requested will be easier to obtain than the information required before. In addition to taxable fringe benefits included on the reported W-2 or 1099 amount, the estimated value of nontaxable benefits will also be required to be reported.

In the event that former officers, directors, trustees, etc. received compensation, or if any person's compensation listed in Part VII of the core form exceeds \$150,000, Schedule J must also be completed.

Schedule J asks whether certain specific types of benefits (of concern to the IRS) were provided, ranging from first-class travel, travel for companions and housing allowances to health or social club dues. If any of these benefits were provided, the form asks whether the organization follows written policies regarding payment or reimbursement.

Schedule J also asks whether the organization requires substantiation of those benefits prior to reimbursement. It also asks several questions concerning the specific methods used by the organization to determine the top executive's compensation.

For persons required to be reported on Schedule J, compensation reported in the core form must be broken down into base compensation, bonus and incentive compensation and other compensation.

For public charities, there are several questions about whether any compensation is contingent on revenues or net earnings, and whether there are any other non-fixed compensation payments, in an attempt to discover potential private inurement.

## Activities Outside the United States

As part of the United States' homeland security effort, the IRS has been charged with the task of collecting information to aid in the war against terrorism. Schedule F has been designed to collect information on foreign activities, although the IRS has admitted that it is unsure as to whether the information currently required will be useful. We expect that this schedule may be revised as it becomes clear what information is most useful.

Schedule F is required to be completed if an organization has aggregate revenues or expenses exceeding \$10,000 from grant-making, fundraising, business or program service activities outside the United States. Information required includes a description of activities per geographical region and detailed information about individual foreign recipients of more than \$5,000.

### **Fundraising and/or Gaming Activities**

In terms of fundraising activities, if a professional fundraiser is paid more than \$5,000, detailed information on the fundraiser is required in Schedule G. If gross receipts from fundraising events exceed \$15,000 in total, detailed information is required in Schedule G for each event.

If gross receipts from gaming events exceed \$15,000 in total, detailed information is required in Schedule G for each event.

### **Tax-Exempt Bonds**

For organizations with tax-exempt bonds that were issued after 2002 and have a balance exceeding \$100,000, only basic information is required in Schedule K for 2008. However, starting in 2009 the entire schedule is required to be completed, which includes information about the use of proceeds, potential private business use and arbitrage. Some of this information could be difficult to obtain without the use of outside professionals.

### **Transactions with Interested Parties**

Detailed information is now required on Schedule L about loans to and from interested parties, grants benefitting interested parties and business transactions involving interested parties.

### **Grants and Other Assistance**

In addition to requiring more detailed information on each grant or other assistance exceeding \$5,000, Schedule I has questions on whether the organization maintains records substantiating grantees' eligibility, the selection criteria used and what the organization's procedures are for monitoring the use of grant funds.

### **Non-Cash Contributions**

Organizations receiving more than \$25,000 in non-cash donations of assets are required to complete Schedule M. This schedule keys in on areas of IRS concern, including donations of art, historical treasures and qualified conservation easements.

Consistent with other schedules, there are questions concerning organization policies in this area, such as the existence of non-cash contribution acceptance policies and the use of third parties to solicit, process or sell these items.

### **Related Organizations and Unrelated Partnerships**

Schedule R consolidates the reporting of transactions with:

- Disregarded entities (such as single member LLCs)
- Related tax-exempt organizations
- Related organizations taxable as a partnership
- Related organizations taxable as a corporation or trust

### **Planning for Filing the New Form**

With the 2008 filing approaching, now is the time to begin planning for the new form. We recommend that you consider the following:

- Identify what new information will be required.
- Identify the source of the information, including the responsible employee or department.
- Determine whether any new information-gathering procedures need to be implemented to capture the additional information required.
- Identify disclosures required under the new form that could cast a negative light on the organization, particularly the governance questions.
- Consider making changes or implementing new governance policies to remedy the potentially negative disclosures.

We would be happy to assist in the above activities.

Welcome to life under the microscope!



# FASB Reaches Tentative Conclusions

*Continued from page 1*

**This is particularly important in Connecticut as it enacted UPMIFA (without modification of the model language) on October 1, 2007.**

UPMIFA was the first attempt to set forth fiduciary responsibilities over the management of investment funds, including endowment funds. Its key concept was the identification of the historic dollar value of the gift as being the amount for which the fiduciary was responsible. Accordingly, in the absence of specific donor restrictions to the contrary, the original amount of the endowment gift was accounted for as permanently restricted. Investment income and gains and losses were classified as unrestricted. For example, a \$100,000 endowment gift without specific donor restrictions on the income earned would be reported as permanently restricted at the original amount forever, regardless of the investment income or gains retained over that amount over the years.

## Prudent investor standard leads to questions

UPMIFA represents a significant change as the historic dollar value concept was removed and replaced with a prudent investor standard. UPMIFA states that one of the factors fiduciaries should consider is maintaining the purchasing power of the funds.

This implies that some of the investment income and /or gains should be retained each year. What are the accounting implications of this concept?

In order to explore these issues, Blum Shapiro participated in a series of meetings with representatives of the Connecticut Attorney General's (AG) Office, law firms, national accounting firms, non-profit organizations and the Financial Accounting Standards Board (FASB). The initial goal was to determine the AG's interpretation of the act. To date, no official interpretation has been issued although there is a sense that organizations do have a responsibility to preserve the long-term viability of a fund. This responsibility may imply accumulating some investment earnings beyond the historic dollar value of the gift.

In light of the significance of the potential financial reporting implications of UPMIFA, the FASB issued a proposed FASB Staff Position on the subject. The proposal document took the position that each non-profit organization needs to determine its own legal responsibilities under UPMIFA, and, if it interpreted that maintenance of purchasing power, for example, was legally required, the annual retainage of investment earnings to preserve that power would be accounted for as an increase in permanently restricted net assets. The proposal also included significant additional disclosures.

The FASB received feedback from the drafters of the model UPMIFA act — attorneys, industry groups and others — who made a strong case that earnings on endowment gifts are legally restricted until appropriated for expenditure by the fiduciary. As a result, the FASB again deliberated on the issue and revised its accounting guidance. The FASB's current position is that, in UPMIFA states, investment earnings retained in excess of the original gift amount should be presented as temporarily restricted until they are "appropriated for expenditure," which, in most cases means when they are spent. It continues to be each organization's responsibility to interpret its legal responsibilities concerning the expenditure of endowment earnings.

Because community foundations are also managing invested funds in a fiduciary capacity, they would also be subject to UPMIFA. However, due to their maintenance of variance power over gifts received, the accounting implications of FSP 117-a on community foundations are not clear at this time.

The FASB also decided to eliminate some of the proposed disclosures and to delay implementation from June 30, 2008 fiscal years to December 31, 2008 fiscal years.

In discussions with the FASB, they point out that, for UPMIFA states, the law has already changed, and, for that reason, non-profit organizations may want to implement early. However, we believe the compliance with UPMIFA by the auditee is separate and distinct from the accounting conventions proposed by FSP 117-a. In addition, we do not recommend early adoption before the final version of FSP 117-a is released as it is possible further changes could be made by FASB.

## Implementation Issues

Organizations will be required to make the following disclosures in their financial statements:

- The governing board's interpretation of the law that underlies the organization's net asset classification
- The organization's spending policy
- The organization's investment policy
- Tabular disclosure of endowment fund activity that roll forward the unrestricted, temporarily restricted and permanently restricted components of an organization's endowment

The FASB has provided examples of these disclosures in an appendix attached to FSP 117-a.

Compliance with the provisions of FSP 117-a will require organizations to analyze activity associated with their endowment funds. Organizations that pool their funds into a single portfolio may be required to allocate the return generated by the portfolio to each fund and track amounts appropriated for expenditure by fund in order to determine the amount of investment earnings that have accumulated over time and not yet been appropriated for expenditure. In the absence of further donor restrictions, these unappropriated earnings are most likely currently classified as unrestricted net assets and will be reclassified to temporarily restricted net assets upon adoption of FSP 117-a. This change in the accounting treatment of investment earnings is expected to be applied retroactively.

In addition to these accounting and financial reporting challenges, organizations should review their investment and spending policies in order to ensure that they are consistent with UPMIFA's guidance which is designed to encourage preservation of the long-term viability of endowment funds, rather than simply maintaining the historic dollar value of permanently restricted gifts.

UPMIFA and implementation of FSP 117-a will present significant challenges to some organizations. We encourage all non-profit organizations to consider these issues and to contact a member of our Non-Profit Services Group to discuss this matter further.

# We have expertise in providing the following services to non-profits:

## Audit Services

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- Federal and state single audits
- HUD audits
- CHEFA compliance letters
- Federal indirect cost rate audits
- Internal auditing
- Fraud investigations
- Special audits
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- Employee benefit plan audits — both full and limited scope

## Tax Services

- Preparation of Federal forms 990/990T and 990PF
- Preparation of State form PCUREG-01
- Application for exempt status (Forms 1023 and 1024)
- Preparation of Federal form 8734 (to affirm advance tax-exempt determination)
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- Sales and use tax planning
- Form 5500 reports

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- Temporary or permanent placement of finance employees

## Technology Consulting

- Accounting software selection and implementation
- Accounting system design (chart of account structure)
- Strategic technology planning
- Hardware selection security assessment

## BlumShapiro

West Hartford Office  
29 South Main Street  
West Hartford, CT 06107

Southport Office  
2960 Post Road  
Southport, CT 06890

blumshapiro.com

For more information, please contact one of the following partners from our Non-Profit Services Group.

**Lori M. Budnick, CPA, Partner**  
860.561.6828  
lbudnick@blumshapiro.com

**Reed W. Risteen, CPA, Partner**  
860.561.6848  
rristeen@blumshapiro.com

**Joseph A Kask, CPA, Partner**  
860.570.6372  
jkask@blumshapiro.com

**Darrell G. Pataska, CPA, Partner**  
860.561.6835  
dpataska@blumshapiro.com

**John A. Zinno, CPA, Partner**  
860.561.6896  
jzinno@blumshapiro.com

**Marcus R. Harwood, CPA, Partner**  
860.570.6474  
mharwood@blumshapiro.com