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To:	*TE/GE-EO-F990-Revision;
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Subject:	Council on Foundations Comments on Draft Form 990 Instructions
Date:	Friday, May 30, 2008 6:25:32 PM
Attachments:	08 Final COF Cmts 990 Instr.pdf

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COUNCIL *on* FOUNDATIONS

May 30, 2008

Via E-mail Transmission

Lois G. Lerner
Director of the Exempt Organizations Division of the IRS

Ronald J. Schultz
Senior Technical Advisory to the Commissioner of TE/GE

Form 990 Redesign
Internal Revenue Service
1111 Constitution Ave, NW
Washington, DC 20224

Dear Ms. Lerner and Mr. Schultz

These comments are offered on behalf of the Council's community foundation and public charity members. We have generally tried to focus our comments on the revised form and instructions as they impact organizations that hold and invest endowments and carry on their charitable activities primarily by making grants to others. We anticipate that you will receive many detailed and thoughtful comments from other organizations and our omission here of some issues that others may raise should not be taken to mean that the Council disagrees with those points.

The comments that follow include discussions of key substantive areas of concern to the Council and its public charity members as well as comments and suggestions that are of a more technical nature. In general, we have tried to address these in the order in which they appear on the core form and its schedules. In summary, however, the Council's key issues are:

- Clarifications with respect to the instructions for line 9 of Part V of the core form (regarding donor advised funds), discussed below under "Comments on Core Form – Part V," and with respect to the reporting of funds that are similar to donor advised funds, discussed below under, "Comments on Schedule D Instructions, Part I"
- Clarifications with respect to the instructions for reporting travel and entertainment expenses for government officials, discussed below under, "Comments on Core Form – Part IX"
- Clarifications with respect to reporting grants and other forms of economic assistance that benefit interested persons, discussed below under, "Comments on Schedule L"

Although our substantive concern with each of these three key issues is different, the three do have some points of commonality. In each, the IRS is asking filers to report transactions that, in

general, are not prohibited, not directly regulated, and not abusive. In the Pension Protection Act of 2006, Congress acted to regulate donor advised funds – the Act did not regulate any funds that may be "similar" in some way. Public charities are not barred from paying the travel expenses of government officials, or from providing them with meals, and often such payments appropriately and significantly further the charity's mission. The group of individuals defined as "interested persons" are not thereby barred from receiving benefits from their charitable organizations on the same basis as any other person that the charity serves. We do appreciate IRS concerns regarding abuses. Nevertheless, as these requirements are currently drafted, most transactions reported will be perfectly appropriate and will not confer improper benefits on anyone – and truly abusive transactions will be hidden in the haystack of reported transactions. Accordingly, we believe these reporting requirements should be tailored very narrowly to try to eliminate as much as possible the reporting of transactions that are not abusive.

The second area of commonality is that in each case, the required reporting is not without cost. It takes time and effort to design systems to capture the data to be reported and it takes time and effort to collect the data. We believe that time and effort will be considerable in the areas we have identified as key. Even the least burdensome – determining which funds are similar in character to donor advised funds – may require sponsoring organizations to duplicate the considerable time and effort they expended in the last quarter of 2006 to determine which of their funds did fit within the statutory definition.

The third area of commonality is that the instructions in all three key issue areas are nonexistent, vague or imprecise in key respects, or sweep unnecessarily broadly. We do not say this to demean in any way the extraordinary effort that IRS officials have made in undertaking this substantial redesign of the Form 990. We mean only to point out that these areas require significant attention before the instructions are made final.

The final area of commonality is that due to the imprecision of the instructions and the sweeping nature of the information requested, filers will respond in a wide variety of ways. The most conscientious will develop new, and costly, systems for capturing reportable information, while others will simply ignore the questions or provide superficial responses. This penalizes those trying hardest to comply completely. Those who choose not to comply or to comply in less comprehensive fashion are likely to go undetected and unsanctioned because the very reasons that make the requested information difficult to collect will also make it difficult for the IRS to audit. Finally, unless instructions are clear and precise, even conscientious organizations will reach vastly different conclusions about what must be reported, making the reports of little use either to the IRS or to those who try to draw comparisons among the organizations that file Form 990.

Comments on Core Form Instructions

Core Form – Part IV

Line 6 – Maintenance of Donor Advised Funds and other accounts: The instructions direct the filer to the Glossary for a definition of the funds and accounts to be reported, but the Glossary only defines donor advised funds. Such definition does, however, describe funds excepted by statute from the definition of donor advised fund. If the intention is for filers to answer "Yes" and complete Schedule D if they maintain any fund that either (a) meets the definition of a donor advised fund or (b) would be a donor advised fund, but for the fact that it is specifically excepted from such definition by statute, the instructions should clarify this. In addition, consider revising the question on Line 6 to refer to "donor advised funds or any **similar** accounts" both for clarity and for consistency in terminology with Schedule D. Finally, please see our comments on Schedule D, below, with regard to determining which, if any, funds should be considered "similar" to donor advised funds for reporting purposes.

Line 29 – Non-Cash Contributions: The instructions include the statement: "Do not include contributions of services or contributions to the capital of the organization." Please clarify the filers to which the latter part of the instructions applies. Some charitable organizations may find the statement confusing and attempt to apply it to contributions to endowments.

Line 37 – Conducting Exempt Activities Through Unrelated Partnerships: Please see the Council's comments on Schedule R, below.

Core Form – Part V:

Line 8 – Disclosure of Excess Business Holdings: Neither the instructions nor the glossary defines the term "excess business holding." In addition, the instructions direct filers to "see the Glossary to determine who is considered a disqualified person for purposes of determining the excise tax on excess business holdings for a donor advised fund." However, the Glossary provides only the general definition of a disqualified person for purposes of section 4958, and does not explain that for purposes of applying section 4943 to donor advised funds, the term "disqualified person" is limited to donors and donor advisors, their family members, and entities 35% controlled by either of the foregoing.[1] The instructions should also explain the meaning of the term "disqualified person" for purposes of applying section 4943 to supporting organizations.[2]

Line 9a – Section 4966 Taxable Distributions: The instructions for Line 9a include a "Tip," which states in part that any distribution to any individual is taxable, "whether a grant, reimbursement, payment of compensation for services, or other distribution," unless it falls within one of two exceptions. We think this tip is inaccurate in that overstates the prohibition on

[1] §4943(e)(2).

[2] See §4943(f)(4).

distributions to individuals. As drafted, it sweeps in amounts paid for goods and reasonable compensation for services, as well as legitimate reimbursement of expenses, which we do not believe are prohibited by section 4966. We believe it is important to carefully distinguish between section 4966, which prohibits "distributions" to individuals without regard to whether the recipients are related to an advised fund's donor or advisor, and section 4958(c)(2), which bars grants, loans, compensation and similar payments to donor advisors and persons related to them. By conflating the two separate requirements, the tip imports into section 4966 the more rigorous limitations of section 4958(c)(2), a position that we believe lacks support in either the statutory language or the accompanying Technical Explanation.[3] In fact, this tip appears to disallow payments made to individuals pursuant to bona fide sales and leases of property which the Technical Explanation specifically states are not prohibited by section 4958. We do not believe Congress would have taken pains to ensure that organizations knew that these transactions with disqualified persons were not prohibited by section 4958 if they had forbidden them under section 4966.

In correspondence dated August 16, 2006, the Council asked Treasury and the IRS to clarify that the term "distribution," as used in section 4966, includes only transactions that are wholly or partially gratuitous in character. Comments filed last June by the American Bar Association's Tax Section agreed with this basic position and advanced several arguments supporting the Council's proposed definition. These included: i) the desirability of an interpretation that is consistent with section 4945; ii) that section 4967 appears to use the term with this meaning; and, iii) the desirability of consistency between sections 4966 and 4967.[4]

The definitional issue concerning the meaning of "distribution" is a key issue for the Council and its members. We do not believe it should be resolved in the context of instructions to Form 990. Accordingly, we urge you to revise the tip by deleting the characterization of distribution as including compensation for services and reimbursement of expenses. As revised, the tip would state, "A distribution from a donor advised fund to an individual is subject to an excise tax under section 4966~~, whether a grant, reimbursement, payment of compensation for services, or other distribution,~~ unless it is excepted ..."

In addition, there are a couple of technical errors in the instructions as well. In the first paragraph, filers are referred to the Glossary for a definition of "taxable distribution," but the Glossary has no such term. Later, the Tip incorrectly states that distributions to non-charitable organizations from a donor advised fund may avoid becoming subject to tax *either* because they are made for a charitable purpose *or* because the sponsoring organization exercises expenditure responsibility for the distributions. In fact, distributions from a donor advised fund to non-charitable organizations are subject to tax under section 4966 unless the distribution has a charitable purpose *and* the sponsoring organization exercises expenditure responsibility over the distribution.[5] Finally, the instructions use the phrase "individual educational grant program" to

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[3] Staff of the Joint Committee on Taxation, *Technical Explanation of H.R. 4, the "Pension Protection Act Of 2006," as Passed by The House On July 28, 2006, and as Considered by the Senate on August 3, 2006,* JCX 38-06, August 3, 2006 ("Technical Explanation").

[4] ABA Section of Taxation, Comments in Response to IRS Notice 2006-109 on the Application of the Pension Protection Act of 2006 to Donor Advised Funds and Supporting Organizations, June 4, 2007

[5] See §4966(c)(1)(B).

describe the section 4966(d)(2)(B)(ii) exemption. This is unduly limiting since the exemption actually excludes grants for travel, study and similar purposes, a category that includes, for example, grants to support research. We recommend using the statutory language.

Line 9b – Distributions to donor, donor advisor, or related person: Line 9b inquires about payments to donor advisors and related persons. The instructions for this line also should be corrected by deleting the term "distribution" and the reference to line 9a for the meaning of that term. Instead, the instructions should state that organizations should answer "yes" if they provided a grant, loan, compensation, or similar payment to a donor advisor or a related person. This change would make the instructions track the language of section 4958(c)(2).

The "tip" for line 9b informs filers of the possible penalties under section 4967 if a donor advisor or related party receives a benefit as a result of a distribution from an advised fund. The tip should be revised to include the qualification that penalty taxes are triggered only by the receipt of benefits that are "more than incidental." This change will make the tip accurately reflect the language used in section 4967.

We do not interpret the instructions for line 9b to require sponsoring organization filers to report benefits that might trigger section 4967 penalties and we believe this is appropriate since in most cases the sponsoring organization will not be in possession of this information.

Core Form – Part VI

Line 12a – Conflict of Interest Policy: The Council believes that the instructions appropriately distinguish between true legal conflicts of interest – those where an individual may benefit financially from a decision and the competing duties that sometimes arise when an individual sits on the board of more than one organization. However, we suggest that the instructions make clear that while an organization may answer yes on line 12a if its policy does not address situations that present the appearance of a conflict, organizations may voluntarily choose to include provisions in their conflict of interest policies that do address appearance questions.

For grantmakers, the most common situation in which there is an appearance of a conflict of interest occurs when one of the grantmaker's board members is also on the board of a prospective grantee. We suggest an additional example as follows:

> **Example**: D is a volunteer member of the governing body of B, which carries out its charitable purposes primarily by making grants to other charities. D is also a volunteer member of the governing body of C, which offers tutoring and other programs to at-risk youth. Both B and C are 501(c)(3) public charities. C has applied for a grant from B, which will be discussed at an upcoming board meeting. While D may have the appearance of a conflict of interest with respect to the grant request, the conflict does not involve a material financial interest of D.

Line 15 – Process for Determining Compensation: Line 15b asks whether the process for determining compensation of officers other than the CEO and key employees of the organization included, inter alia, review and approval by independent persons. However, the instructions make clear that filers may answer yes with respect to this line only if they followed the full rebuttable presumption process for those positions, including review and approval by the governing body or a compensation committee. We believe that most boards delegate to the CEO decisions about compensation of most, if not all, subordinate officers and key employees. Accordingly, we recommend that the instructions for line 15b be revised to permit organizations to respond affirmatively when the CEO is independent of the persons whose salary he or she determines.

Line 16 – Joint Venture Policy: See the Council's comments on Schedule R below.

Core Form – Part VII – Compensation of Officers, etc.

Directors: Section A requires that filers report the average number of hours per week worked by members of the filer's board even if the directors are not compensated. While this is not a change from the existing requirement, we do not understand why it is necessary to report hours worked for persons who receive no compensation. Reporting a nominal figure (e.g., 1 hour a week) apparently satisfies the requirement but directors who devote more than the nominal amount of time sometimes feel insulted, a problem that will grow worse as filers provide copies of Form 990 to boards. The result is that filers establish systems for recording or estimating actual time, an otherwise pointless exercise. We recommend allowing filers to mark the box for hours worked N/A if Boxes D, E, and F all contain a zero.

Key employees: The Council believes that the proposed $150,000 threshold for reporting compensation for key employees strikes the appropriate balance for increasing the transparency of compensation reporting, without unnecessarily burdening organizations with additional reporting requirements where salaries are likely to be at reasonable.

Health benefits: We found the direction to report the "value" of health benefits provided by the employer to be confusing. Value is subjective and would vary depending on an employee's medical history and current needs. However, the remainder of the paragraph suggests that the amount to be reported is the total of employer contributions and employee contributions (if excluded from taxable income). We suggest modifying this instruction accordingly.

Core Form – Part IX – Statement of Functional Expenses

Line 11d and 11g – Lobbying Fees and Other Fees for Services: The instructions to line 11g state that fees paid for advocacy services that are not lobbying should be reported on line 11g. This information should also appear in the instruction for line 11d as well. In addition, the instructions for line 11d indicate that fees paid for "legislative liaison services" should be reported on this line together with fees paid for lobbying. The term "legislative liaison services" is undefined, but appears to cover fees paid for services that are not lobbying since otherwise the

inclusion of the term would be extraneous. However, the inclusion of non-lobbying fees together with lobbying fees on line 11d will make it impossible for the Service to determine what amount was spent on lobbying activity. Therefore, we recommend that legislative liaison services, like non-lobbying advocacy services, be reported on line 11g and the instructions for both lines be revised to reflect this. Amounts reported for lobbying activity on Schedule C could also be cross referenced to line 11d. Finally, the instructions should clearly state that organizations that have made the section 501(h) election may rely on the definitions in section 4911 and its implementing regulations in determining whether a payment is for lobbying or for advocacy that is not lobbying.

Line 18 – Payments of Travel or Entertainment Expenses for any Federal, State or Local Official: The Council is aware that the IRS modified the instructions for line 43 (Other Expenses) in the 2006 990 by adding a reporting requirement for reporting travel and entertainment expenses paid to government officials and that this instruction also appeared in the instructions for the 2007 990. We are uncertain how many organizations paid attention to the new requirement, however, since there was not a new line added to the form and "What's New" for 2006 simply referred to changes in the instructions for line 43. In any case, for the reasons we will now discuss, we believe the IRS should substantially revise the instruction for new line 18 to narrow the group of public officials with respect to whom reporting is required.

Absent significant modifications, the reporting required by the instructions on this line creates very burdensome recordkeeping requirements for filers. This burden stems from three factors: 1) the adoption of section 4946(d) as the standard for determining who is a government official; 2) the fact that organizations may pay travel or entertainment expenses for persons who are government officials for reasons unrelated to their public office and without the knowledge that the persons in question are government officials; and 3) the inclusion of family members, as defined in section 4946(d) in the reporting requirements

Use of Section 4946(c) to Define Government Officials Covered by the Reporting Requirements: Private foundations have struggled for many years with some aspects of the section 4946(c) definition. Subparagraphs (1) (2), (3), and (7) of the definition are clear and precise:

- All persons holding elective public office in the executive and legislative branches of the federal government (section 4946(c)(1))
- All persons in the executive and judicial branches of the federal government who were appointed to their office by the President (section 4946(c)(2))
- All persons holding positions in the executive, legislative, and judicial branches of the federal government who are either Schedule C or who are paid at a rate equal to the lowest rate of basic pay for the Senior Executive Service (section 4946(c)(3))
- Any member of the Internal Revenue Service Oversight Board (section 4946(c)(7)

The remaining three subparagraphs defining a covered official, however, all pose problems due to the application of salary thresholds that either have not been adjusted for inflation since 1969 or received an adjustment that did not reflect inflation. In addition, to decide whether a state or

local government official is covered by the definition, filers must make a somewhat subjective determination of whether the person occupies a public office.

- All employees of the House of Representatives or the Senate of the United States are government officials if they receive compensation at an annual rate equal to $15,000 a year (section 4946(c)(4)).
- All elected and appointed officials of the executive, legislative, and judicial branches of state governments, their political subdivisions, US possessions, and the District of Columbia are government officials if they are compensated at an annual rate of $20,000 or more (section 4946(c)(5).
- All persons who are personal or executive assistants or secretaries to any government official are also government officials (section 4946(c)(6)).

Congress established the salary threshold for subparagraphs (4) and (5) at $15,000 in 1969. Although Congress increased the original $15,000 threshold for subparagraph (5) to $20,000 in the 1986 Tax Reform Act, this increase did not account for inflation between 1969 and 1986. A simple inflation adjustment from the 1969 threshold would increase it to approximately $88,000 today and would come closer to differentiating between employees who are in positions where they are likely to have substantial influence over policy decisions from those who are performing administrative, clerical or maintenance functions. However, as things stand, nearly anyone employed by the House or the Senate must be considered a government official.

The section 4946 regulations mitigate the otherwise sweeping coverage of section 4946(c)(5) – state and local officials – by providing that a person must also hold a "public office" before he or she will be considered to be an elected official. While this is a helpful adjustment that narrows the class of covered officials, whether a position is a public office is a facts and circumstances test that is necessarily somewhat subjective as the "essential element" is "whether a significant part of the activities of a public employee is the independent performance of policymaking functions."[6] The difficulties that can arise in applying this test were illustrated recently by the Service's own difficulty in properly classifying an elected state district court judge as a government official.[7]

As the foregoing demonstrates, a very large group of individuals must be considered to be government officials under section 4946(c). The class currently includes many persons, such as low-level clerical staff employed by the House or the Senate, that most persons would not think of as government officials. The same is true for state and local officials and is further complicated by the fact that many state and local officials serve as such on a part-time basis.[8] As

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[6] Treas. Reg. 53.4946-1(g)(2)(i).

[7] PLR 200604034 withdrawing the determination in PLR 200542037 that an elected state district court judge was not a government official under section 4946(c)(5) (PLR 200604034, apparently incorrectly, describes the judge in question as a federal district court judge, perhaps another indication of the confusion surrounding the definition of a government official).

[8] The salary threshold is expressed as a rate rather than an absolute dollar amount. Accordingly, compensation paid to part-time officials must be multiplied out to determine whether it exceeds the $20,000 threshold.

a consequence, the individuals in question usually have another job and often that job is one that is full time increasing the probability that speaking invitations, for example, will be based on the person's day job and may be extended in ignorance of the fact that the person also holds a part-time government post.

> **Example**: Mary Jones is the dynamic young leader of a human services organization. The organization's innovative programs for young offenders have substantially reduced the rate at which these young persons commit new crimes. A national organization invites Ms. Jones to speak at its conference so that others may learn more about her programs and how they can be replicated. The national organization pays Ms. Jones' travel costs to and from the conference and provides meals while at the conference. The total exceeds the reporting threshold. The national organization is not aware that Ms. Jones is also a member of the school board in her local community for which she receives a modest stipend that nonetheless exceeds an annual rate of $20,000 a year.

The inclusion of family members is a further substantial broadening of the class of persons for whom reporting would be required. Although the instructions reference the definition of family member found in section 4946(d), family members of government officials are not treated as disqualified persons with respect to a private foundation. Only the officials themselves are disqualified. Consequently, private foundations have never had to face the task of trying to track family member relationships. Including family members in the class for which reporting would be required also substantially increases the number of persons who may, for example, be asked to provide consulting services or speak at conferences based only on their individual skills and talents, with the tax-exempt organization not knowing or having any reason to know that they are related to a government official.

> **Example**: The facts are as above except that Ms. Jones is not a member of the school board, but her mother is the mayor's secretary.

It may be possible for smaller organizations to keep track of travel and entertainment expenses for government officials that the organization knows are government officials and to include reporting for the official's spouse or another family member if he or she is accompanying the official. Larger organizations may find even this a challenge, however, given the breadth of the definition of government official and the number of employees who may be interacting with them. Instituting systems that would identify persons as government officials or members of an official's family would be considerably more burdensome, requiring, as it would, a lengthy explanation of what is a government official (see above) that would need to be administered to any individual for whom an organization may pay travel expenses or provide.[9]

We recommend that the IRS revise the instruction to adopt a much narrower definition of government official than the one presently found in section 4946 by:

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[9] The instructions require the maintenance of records concerning all meals and transportation provided to government officials even if the expenditure is below the threshold for reporting on Form 990.

- Limiting state officials to those holding elective office
- Eliminating local government officials entirely
- Also eliminating the category of secretaries, personal assistants and executive assistants
- Establishing realistic salary thresholds that reflect 2008 compensation levels (which the IRS should then adjust periodically).

We also recommend eliminating any requirement to report with respect to family members unless they accompany the official on the trip or at the meal.

We believe these recommendations strike a reasonable balance between the interest of the IRS in increasing reporting about travel and entertainment provided to government officials with the burden the instructions otherwise place on organizations to track and determine whether individuals are government officials or members of the family of a government official.

Comments on the Draft Instructions for the Schedules

Schedule A – Public Charity Status and Public Support

Part I – Line 8: Most community foundations now are structured as a single nonprofit corporation. It would reduce reporting confusion if the instructions for line 8 added that community foundations in corporate form should check box 7 rather than box 8.

Part I – Lines 11a to 11d: We urge the IRS to make the voluntary redetermination process described in the Tip mandatory and to establish a date certain by which supporting organizations must seek a redetermination of their status.

Part I – Lines 11f – Type of Supporting Organization: The tip appears inaccurate in that it indicates that organizations may request a determination letter that describes it as a Type III – Functionally Integrated organization, but does not state that the IRS is only issuing such determination letters if the organization meets the additional standards set forth in Announcement 2007-87, the Advance Notice of Proposed Rulemaking and Request for Public Comment on Proposed Payout Requirement for Type III Supporting Organizations that are not Functionally Integrated, 2007-40 I.R.B. 753 (Aug. 2, 2007).

Schedule D – Supplemental Financial Statements

Part I – Organizations Maintaining Donor Advised Funds or Other Similar Funds or Accounts

Beginning with the 2006 Form 990, the form has included a question asking filers not just whether they maintain donor advised funds but also whether they maintain, "any accounts where donors have the right to provide advice on the distribution or investment of amounts in such funds or accounts." Neither the instructions to the 2006 990 nor the draft instructions for the

revised 990 include any explanation of the standard an organization should use to determine when a fund that does not meet the definition of an advised fund should nonetheless be reported in lines 1-4 of box b.

Staff of the Joint Committee on Taxation devoted considerable thought to crafting a definition of donor advised fund. Section 4966(d)(2)(A) provides that a fund is a donor advised fund if it is separately identified by reference to contributions of a donor or donors; owned and controlled by a sponsoring organization; and a donor (or any person appointed or designated by the donor) has, or reasonably expects to have, advisory privileges with respect to distributions or investment by reason of the donor's status as a donor. Component parts of the definition included two statutory exemptions. The first exempts funds that make distributions only to a single identified organization or governmental entity. As the Joint Committee staff's technical explanation makes clear, such funds may be named for a donor and the donor may have advisory privileges regarding distributions without the fund being classified as donor advised.[10] The second exception is for funds that make grants to individuals for travel, study and similar purposes as long as the fund's advisor provides advice only as a member of a committee that is appointed by the sponsoring organization, the donor does not control the committee, and the committee follows procedures that have been preapproved by the sponsoring organization's board and which are consistent with the requirements of section 4945. The legislation also authorized Treasury to grant additional exemptions in appropriate circumstances.

The Joint Committee Staff's Technical Explanation supplemented the definition of donor advised fund with examples of funds that are not donor advised because they do not meet the statutory definition. Chief among these are an organization's general fund and funds that pool contributions of many donors and do not provide individualized accounting for any individual donor. These funds are not donor advised funds because they lack one or more of the basic characteristics of an advised fund – a fund created by a gift from an individual donor (including funds created by a family or a business) for which the donor, or someone the donor appoints, is the advisor.

We believe the instructions should follow this basic line of demarcation. Funds that should be reported as "other" are funds that would be classified as donor advised but for the fact that they fall within one of the statutory exceptions (or an exception granted by the Secretary). Thus funds that make distributions to a single charity would be reported as "other" if the fund's donor provides advice with respect to investments or distributions. Similarly, scholarship funds that meet the exemption requirements would be reported as "other" if the fund's donor or a person the donor appoints serves on the selection committee. The instructions should then provide that funds that do not meet the basic definitional requirement to be an advised fund are not required to be reported in lines 1-4, box b. This would be the case even though there may be instances when sponsoring organizations make use of volunteer committees in advising about distributions and the committees include some donors.

In the absence of clarification in the instructions, we will continue to advise our members to categorize funds as we have described above. However, without clarity in the instructions, there

[10] Technical Explanation at 345.

is little reason to believe that the IRS will receive useful information with respect to the second part of the question because organizations are reaching differing conclusions about what should be reported. We also urge the IRS to move forward promptly in addressing definitional issues raised in the many comments that have been filed on donor advised fund issues arising from the enactment of the Pension Protection Act of 2006.

Part I, Line 3: The instructions are to report total "grants" from donor advised and similar funds. Some advised funds make expenditures for charitable purposes that are not grants. The instructions should be revised to include any expenditure for the charitable purposes of the fund.

Part III – Organizations Maintaining Collections of Art, Historical Treasures or Other Similar Assets

Organizations that do not normally "maintain" collections of art or similar assets, but which do accept such items as gifts, may be confused by line 5 of Part III, which asks whether an organization solicits or receives art to be sold. Based on the wording of the checklist question (Line 8 of Part IV of the core form), we believe that the maintenance of a collection is a predicate to filling out Part III and our understanding is bolstered by the fact that line 30 of the checklist specifically asks about whether an organization receives such gifts and directs filers to Schedule M to supply additional information. We think the instructions for Part III could be strengthened, however, by a clear statement that it is required only for museums and similar organizations that maintain collections of art and that organizations that accept gifts of art, but do not maintain them in a collection, should not complete Part III, but should report those gifts on Schedule M.

Part V – Endowment Funds

Lines 1 – 4 – Definition of Endowment: The new reporting requirements with respect to endowments should give the IRS a more complete picture of the magnitude of endowments held by public charity and of their policies with respect to using distributions from endowment to support current activities. However, we are concerned that use of the definitions found in FASB 117 will lead to a significant understatement of the size of endowments and may generate unnecessary audits when organizations thought to hold endowments report that they do not. For example, although community foundations typically hold endowments, some of them very substantial, most of their accountants classify all of their funds as unrestricted either because the community foundation's organizing documents give it a limited power to invade corpus or because the variance power gives it the right to alter a fund's purpose in certain limited circumstances.

We recommend, instead, that the instructions use the definition found in section 2(2) of the Uniform Prudent Management of Institutional Funds Act (UPMIFA).

> 'Endowment fund' means an institutional fund or part thereof that, under the terms of a gift instrument, is not wholly expendable by the institution on a current

basis. The term does not include assets that an institution designates as an endowment fund for its own use.

This definition is now the governing law in 22 states and the District of Columbia and is under consideration in another 10. We believe that it should be the basis for reporting endowments on Form 990.

Line 1f – Administrative Expenses: Please clarify what is to be reported here. Are these overhead costs, such as investment management fees, that are directly attributable to the endowment or is the number on this line supposed to reflect distributions from the endowment to support expenses reported on the core form in Part IX column (C) (Management and General)? If the latter, should administrative expenses also include any support from the endowment for fundraising expenses (column (D))? If line 1f reports only costs directly attributable to the endowment, should amounts reported on lines 1d and 1e include associated management, general, and fundraising costs?

Line 3a – Endowment funds held and administered by related and unrelated organizations. Community foundations typically hold two types of funds for the benefit of another charitable organization. Funds referred to as "agency endowments" are created by transfer of assets from a charitable organization that names itself as the fund's beneficiary. Pursuant to the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 136, these funds are classified as assets with a corresponding liability in the community foundation's audited financials. The transferring charity, if following GAAP, will report the present value of its expected future income stream as an asset on its books. Despite this accounting treatment, the transaction in which the funds are transferred is a completed gift and, as a matter of law, the transferred assets are the property of the community foundation and are included in assets on the community foundation's Form 990. For purposes of Form 990 reporting, the community foundation reports distributions to the transferor charity as a grant and we believe the charity should be recording the grant as contributions income. The instructions should confirm that this is how these transactions should be reported, as the accounting treatment has led to considerable confusion among charities that are the designated beneficiaries of agency endowments.

Community foundations also hold funds created by gifts from a donor or donors who have designated a particular public charity or charities as the beneficiaries of the fund. In these cases, the accounting treatment is the same as the funds' legal status – they are reported in audited financials as assets of the community foundation solely (assuming there has been adequate disclosure of the community foundation's variance power) and do not appear on the books of the designated charity. There has been less confusion about the proper recording of distributions as grants by the community foundation and contributions income by the recipient, but the instructions could also note that this is the correct way in which to report these distributions as well.

Schedule F – Statement of Activities outside the United States

In general, the Council has few comments on the revised Schedule F and its instructions. We appreciate the changes that the Service has made in response to comments by us and others on this form.

Part II, Line 1, Columns (e) and (f) – Cash Grants: It is unclear whether these two columns require reporting on a cash basis even if the organization is otherwise completing the form on an accrual basis. The instructions should clarify this.

Part II, Line 2: This line reports the number of foreign grantees in three categories:

- Those that have IRS determination letters recognizing that they are described in section 501(c)(3)
- Those "that are recognized as a charity by a foreign country"
- Those for which "the grantee or counsel" has provided a section 501(c)(3) equivalency letter

Assuming the second category above was intended to encompass only those foreign determinations of charity status that are recognized by the US under a tax treaty, we recommend modifying the instruction to so state, noting that, at present, such treaties exist only for Canada, Mexico and Israel. If grantees recognized by other countries are to be included here, the instructions should be modified to provide standards for determining which countries should be included and, keeping in mind that charity is a common-law concept, should state whether grantees recognized as nongovernmental organizations should be included in the total.

The instruction summarized in the third bullet above should be modified to reflect the requirements of Rev. Proc. 92-94. We suggest this wording: "for which the grantmaker has made a good faith determination, based on an affidavit from the grantee or the opinion of counsel, that the grantee is the equivalent of a public charity."

We also recommend adding two additional categories to this line with the proviso that grants must further a charitable purpose:

- International organizations designated as public charity equivalents by Executive Order pursuant to 22 USC 288
- Foreign governments, agencies and instrumentalities

Part III – Grants to Individuals: The instructions should clarify reporting obligations in two common situations:

- Grants to US residents to support an activity that will be carried on outside the United States, such as scholarships for students to study at a foreign university or a grant to enable an academic to attend an international conference in his field of study

- Grants to foreign individuals to support an activity that will be carried on inside the United States, such as scholarships to enable a foreign resident to attend a US university

Should both reported on Schedule F, both on Schedule I, or one on Schedule F and one on Schedule I?

Schedule G – Fundraising or Gaming Activities

Part I, Line 2a – Fundraising Activities: The instructions appear not to match the form with respect to the inclusion or exclusion of officers, directors, trustees or key employees on line 2a. If the intent is to require reporting on line 2a for contractual relationships with officers, directors, trustees or key employees that are in addition to the compensation they receive for the performance of their normal job functions, the instructions should clearly state this.

We also recommend that the instructions make clear that reporting is not required for agreements with volunteers.

Part I, Line 3 – State Registration: It is our understanding that state registration requirements apply in 39 states and the District of Columbia. The instruction with respect to multistate filers should be revised to state that they may answer "All States and the District of Columbia" instead of "All 50 States."

Schedule I – Grants and Other Assistance to Organizations, Governments and Individuals in the United States

Part I, Line 2 – Process for Monitoring Grant Funds in the United States: The instructions for line 2 imply that grantmakers must have processes in place for monitoring the use of grants even when those grants are made to domestic public charities. Grantmakers that award significant grants to support a particular project activity of the grantee's generally will have monitoring systems in place to document that the grant was used for the purpose specified in the grant agreement. However, many grantmakers make grants for the general support of the grantee organization, or small grants for a particular purpose, and do not monitor the use of those funds, relying, instead, on the grantee's independent obligation to expend grant funds only for charitable purposes. Many general support grants are quite small in amount and would be uneconomical for both grantmaker and grantee if monitoring was necessary. The instructions should ask grantmakers to describe their monitoring systems, but should also acknowledge that monitoring is not required for grants to domestic public charities.

Part II, Column (h) – Purpose of the Grant: Paralleling the comment above, the instructions should permit the use of the phrase "general support" for grants made for the general support of a public charity. We are aware that the language used in the instruction is largely unchanged from the current instructions. However, in our experience, the current instructions are often ignored or

grantmakers construct a general purpose for the general support grant by reference to the general activities the grantee undertakes.

Schedule L – Transactions with Interested Persons

Part III – Grants or Assistance Benefiting Interested Persons: While we appreciate the modifications made to this section in response to our earlier comments, we continue to believe that the information sought will be extremely burdensome for filers to obtain and in most cases will describe transactions that are not abusive in any way. In addition, as discussed further below, we are concerned that the broad scope of the requirement as currently drafted would invade the privacy of persons needing charitable services or force them to forego services in order to keep their needs confidential. Thus, the administrative and possible human costs required to comply with this disclosure requirement may vastly outweigh any potentially useful information to be gained from it. We recommend, therefore, that the scope of the required disclosure be narrowed, in order to reduce the costs of compliance and to better focus reporting on transactions most likely to be abusive. Specifically, we recommend that the IRS (a) limit the definition of "interested person" with respect to whom reporting is required, (b) establish a threshold benefit level, below which reporting is not required; and (c) not require reporting of any benefits received by an "interested person" solely as a member of the charitable class the organization serves if it is provided on the same terms as provided to others in the class.

Reporting Requirements: The instructions require filers to report: "each grant or similar assistance (including provision of goods, services, or use of facilities) provided by the organization to an interested person," unless the interested person provides consideration in return. The instructions also exclude services provided in furtherance of the purpose of a grant from being treated as consideration for the grant.

Interested persons are:

- Officers, directors, trustees, and key employees
- Substantial contributors
- Members of the organization's selection committee
- Family members of any of the above
- 35 percent controlled entities of the above
- All employees of all substantial contributors, and their children
- All employees of all entities 35 percent controlled by substantial contributors, and their children

Excluded from reporting are:

- Transactions reported elsewhere on Schedule L (excess benefit transactions and loans)
- Business transactions with interested persons for full and fair consideration (also reported elsewhere on Schedule L)
- Section 132 fringe benefits

- Grants to a substantial contributor's employees (and their children) awarded on an objective and nondiscriminatory basis, using pre-established criteria and review by a selection committee, and generally conforming to the requirements of section 53.4945-4(b) of the Regulations

Broad Scope of Disclosure: The instructions provide that filers must disclose all forms of assistance to those the organization identifies as interested persons. For the Council's membership, this will generally take the form of cash assistance in the form of grants, awards, prizes and assistance provided to alleviate hardship and economic need. However, the disclosure requirement clearly also applies to the broad range of charitable organizations for which the provision of services is the focus of their charitable activities. We are concerned that many charitable organizations may not realize that these reporting requirements apply to them. The relocation of the requirement to Schedule L may help in this regard, but we recommend that the instructions provide some examples of how this reporting requirement might apply to a charity that is not a grantmaker.

In this connection, we urge the IRS to reconsider these sweeping disclosure requirements that will reveal information about interested persons that is a substantial invasion of their privacy and that may cause them, in some cases, to forego receiving services they need in order not to have the fact that they received them disclosed to the public. For example, someone who has been raped may decide not to seek needed counseling from a rape crisis center – a service the center provides free of charge to all rape victims – if the fact that she received the services, and, therefore, the fact that she has been raped, must be reported on Form 990 due to her status as a granddaughter of one of the center's board members. Given the sensitive personal nature of many of the services offered by charitable organizations, it is not difficult to imagine many other examples where the harm done to individuals will far outweigh any possible benefit from reporting transactions the vast bulk of which will not violate any law nor confer an impermissible private benefit on anyone.

In considering the burden this new reporting requirement will impose on filers it is important to keep in mind that section 4958 already prohibits excess benefit transactions with those persons who have substantial influence with respect to an organization and that, at a minimum, this includes officers, directors, trustees, the organization's CEO and its CFO. Key employees and substantial contributors may also be substantial influence persons, depending on a facts and circumstances analysis. Recognizing, however, that substantial influence persons may be drawn from the organization's charitable class, the section 4958 regulations provide that economic benefits provided to substantial influence persons solely because they are members of the charitable class that the organization serves will not constitute an excess benefit transaction.[11]

The new reporting requirement, then, does two things:

- It requires reporting transactions with substantial influence persons that are exempted from the sanctions provided by section 4958 because the benefits were based solely on membership in the charitable class

[11] Treas. Reg. § 53.4958-4(a)(iv)(4).

- It creates a new group of persons, who are not substantial influence persons, but for whom reporting will be required

It is not clear from the instructions whether persons in the second group are persons that the IRS believes may have substantial influence on the organization as a whole despite their not being so classified by the organization itself or whether the IRS is attempting to define a group of persons who might have substantial influence in connection with a particular transaction because the person (or a relative) provided the financial resources used in the transaction or is a member of a committee that makes recommendations or decisions with respect to a particular transaction or set of transactions. We think the latter makes more sense and this interpretation would help to narrow the group of transactions required to be reported.

Ambiguity Regarding Transactions that Must Be Reported: It is not clear from the instructions whether, and to what extent, organizations must report assistance provided to interested persons when the organization charges recipients a fee for the services or goods provided. This will be a key issue for filers who are service providers because there is almost always some element of subsidy when a charitable organization provides services in furtherance of its mission.

There are at least three possibilities for the transactions that must be reported. First, the filer must report all transactions in which the return consideration is less than the fair market value of what is provided. In that case, the organization would, we presume, report the amount of the subsidy provided to the interested person in column (c). Second, the filer reports only when the interested person pays an amount that is less than what the organization customarily charges other beneficiaries, or other beneficiaries like the interested person, with the difference reported in column (c). Third, the organization is not required to report if the interested person pays any amount, including a nominal sum, for the benefit he or she receives. This last, that organizations report only if the interested person pays nothing in exchange for the benefit, is how we interpret the existing instructions, but we suspect this may not have been the intent. This should be clarified in the final instructions.

Inappropriate Disclosure of the Identity of Substantial Contributors: The information reported in Part III must include the name of the interested person, the nature of the relationship between the interested person and the organization, and the amount of the grant or type of assistance. Thus, reportable assistance provided to a person who is a substantial contributor must name the individual and identify him or her as a substantial contributor. However, sections 6104(b) of the Code bars the Secretary from disclosing the name and address of any contributor to an organization (other than a private foundation) and section 6104(d)(3) exempts the names and addresses of contributors from the otherwise applicable disclosure requirements. Accordingly, if the final instructions continue to include substantial contributors in the list of interested persons, the Service will need to provide for appropriate redaction of Part III. We would interpret redaction in this case as also applying to the names of family members of a substantial contributor since the substantial contributor's identity could often be inferred from the disclosure of the person's relationship to the organization that is required in column (b). For example, assistance to the son of a substantial contributor presumably would require naming the son in column (a) and, in column (b), identifying his relationship as "son of substantial contributor."

This problem could be eliminated by dropping substantial contributors from the list of interested persons.

Inappropriate Definition of Substantial Contributor: The instructions refer filers to section 507(d)(2) for the definition of substantial contributor. Under section 507(d)(2), a substantial contributor is any person who contributed more than the greater of $5,000 or 2 percent of the total contributions the organization received in a year. Under section 509(d)(2)(B)(iv), anyone who is a substantial contributor retains that status permanently.[12] However, organizations described in section 170(b)(1)(A)(vi) have never been required to maintain historical records of their substantial contributors and it would be difficult or impossible to try to recreate those lists.

If the IRS decides to retain substantial contributors in the group of interested persons with respect to which transactions must be reported in Schedule III, we recommend that for organizations described in section 170(b)(1)(A)(vi), the instructions limit the definition of substantial contributor to current contributors – those individuals who appear on the list compiled in determining the amount to be reported on line 5, Part II, Schedule A. Limiting the list to current substantial contributors would be consistent with their treatment in determining public support and would be consistent with their treatment in the regulations implementing section 4958. Under those regulations, substantial contributor status is a fact tending to show that a person has substantial influence over the organization, but in determining who is a substantial contributor, the regulations direct the organization to take into account only contributions received during the current year and the four previous years.[13] Presumably, organizations (e.g., hospitals and universities) not presently required to complete the support schedule in Schedule A will need to follow an equivalent process in order to determine their substantial contributors and the instructions should direct them on how to accomplish this.

Employees of a Substantial Contributor or 35-percent Controlled Entity: The instructions state that all of the employees and the children of employees of a substantial contributor must be considered to be interested persons. We recommend that the instructions limit the group that must be so considered to only employees, and children of employees, who receive a reportable benefit from a program or a fund established to provide benefits to the substantial contributor's employees and dependents. If filers must also track this entire group of persons with respect to whether they receive benefits under other programs and funds, the paperwork burden will increase exponentially even though there would seem to be little reason to be concerned with improprieties in programs over which the employer has no particular influence.

The instructions exclude from reporting grants to a substantial contributor's employees (and their children) awarded on an objective and nondiscriminatory basis, using pre-established criteria and review by a selection committee, and generally conforming to the requirements of section 53.4945-4(b) of the Regulations. There is no comparable exclusion for employees of 35 percent

[12] While section 509(d)(2)(C) offers a process by which a substantial contributor to a private foundation can shed that status, there is no similar process for public charities.

[13] Treas. Reg. § 53.4958-3(e)(2)(ii) and Example 13.

controlled entities. We don't see any reason why the exclusion should not also include this group of employees.

Related Party Status of Committee Members: We recommend revising the instructions to make clear that committee members are interested persons only with respect to awards that the committee makes or recommends. Although the instruction apparently assumes that a charity would have only a single selection committee, many community foundations have numerous committees that evaluate applicants for scholarships, for prizes and awards, and, in some cases, for assistance to alleviate hardship and distress. There doesn't seem to be any reason why a committee member should be treated as an interested person for purposes of awards made or recommended by other committees.

Three Ways to Limit Reporting and Make It Meaningful: The first and most obvious way is to establish a threshold below which reporting is not required. Part IV of the schedule, for example, establishes a $10,000 per transaction threshold below which reporting is not required for business transactions involving interested persons. Schedules I and F use a $5,000 threshold for reporting grants. Payments or receipts exceeding $15,000 are required to trigger reporting on Schedule G. A $10,000 floor would be consistent within the form, would sharply reduce the reporting burden, and would focus the attention of the IRS and anyone interested in the organization on large transactions with persons who are insiders (or are deemed to be so by the reporting requirement).

Second, as we have noted in several places above, limit the number of "interested persons" with respect to which reporting is required. We think reporting should be limited solely to those persons who are substantial influence persons with respect to the organization. This is a much smaller class than will result if the reporting requirement includes all substantial contributors and members of their families, all committee members and members of their families, and the two groups of employees and their children. The instructions could make clear that the direction on the form to report with respect to substantial contributors applies only with respect to substantial contributors who are substantial influence persons.

Third, do not require reporting when the benefit the interested person receives is provided to the interested person solely as a member of the charitable class the organization serves and is provided on the same terms, or no more favorable terms, than as provided to others. Consider also excluding all grants for travel, study and similar purposes that are awarded using an objective and nondiscriminatory process that has been approved in advance by the organization's board of directors and that generally conforms to the process outlined in section 53.4945-4 of the regulations.

Schedule M – Non-Cash Contributions

Line 32a – Use of Third Parties to Solicit, Process or Sell Non-Cash Contributions: We urge the IRS to target this question more narrowly to avoid requiring filers to describe routine, arms-length arrangements in Part II, such as arrangements with securities brokers to dispose of gifts of publicly traded securities or agreements with real estate brokers to dispose of gifts of real

property. In the alternative, the instructions should make clear that these arrangements can be described in summary form, as there seems to be little benefit gained by reporting details of these ordinary, and perfectly legitimate, transactions.

Schedule R – Related Organizations and Unrelated Partnerships

Part VI - Reporting with Respect to Investments in Entities Taxed as Partnerships:

These comments address four inter-related pieces of the draft instructions for Form 990:

- Core Form Part IV, line 39, which inquires about the conduct of exempt activities through unrelated partnerships;
- Schedule R, Part VI, where information about those partnerships is disclosed;
- Schedule D, Part VII (which feeds Core Form Part X, line 12), reporting investments in securities that are not publicly traded
- Core Form Part V, line 16 which inquires about a filer's joint venture policy

Part IV, line 39 and Schedule R – Reporting Certain Partnership Activities: For Part IV, line 39 and Schedule R, Part VI, it is unclear whether the Service is requesting information only about joint ventures and partnerships, such as hospital joint ventures, engaged in by a filer to carry on the activities for which it has received tax exemption, or whether some investments in partnerships must be reported on Schedule R as well as on Schedule D. Line 39 of Core Form Part IV asks, "Did the organization conduct more than 5 percent of its exempt activities through an entity that is not a related organization and that is taxed as a partnership? If yes, complete Schedule R, Part VI" (emphasis supplied). This appears to mean that supplemental information is required on Schedule R only if the return filer is participating in an unrelated partnership in order to carry on its charitable purposes. Similarly, some of the instructions for line 16 in Part VI of the Core Form, which inquires whether the filer invested or participated in a joint venture with a taxable entity, imply the same result in asking whether the filer has a policy that requires negotiation with other members of the partnership to secure terms that will protect the exempt party's tax exemption, giving examples, such as that the venture will give primacy to exempt purposes over maximizing profits and will not engage in activities that will jeopardize the exempt partner's tax status. These safeguards are among those that have been put in place in hospital joint venture arrangements, but would not be appropriate (or needed) in an investment partnership where the exempt entity is not a general partner (or a managing director of an LLC).

The Part IV line 39 instructions, however, as well as those for Part V line 16 and Schedule R part VI appear to require reporting some investments in partnership-type structures on Schedule R. Thus, the Part IV line 39 instructions tell filers that they need not report unrelated partnerships whose sole purpose is passive investments, implying that partnerships that receive income from trade or business activities must be reported. The Schedule R instructions also seem to lead to this result. The Part VI instructions first establish an activities test – reporting is required for any partnership if the filer conducts more than 5 percent of its activities (measured by either revenue or assets) through an unrelated partnership. Unlike the question on line 39, the Schedule R instructions do not state that these activities must be exempt activities. The instructions then tell

filers that they may disregard partnerships where at least 95 percent of the income the filer receives from the partnership is passive in character – interest, dividends, royalties, rents and capital gains (disregarding the debt-financing rules). Again, apparently investments in entities taxed as partnerships that receive 5 percent or more of their income from an active trade or business are reportable even if the filer holds only a limited partnership interest in the venture (or a similar interest in an LLC) and has entered into the arrangement purely for investment purposes.

The number of such entities required to be reported is likely to be small. Partnerships are reportable only if income from the partnership is five percent or more of the filer's total revenue or assets invested in the partnership are 5 percent or more of the filer's total assets and income from such a venture would be subject to the unrelated business income tax. Nonetheless, we think the Service should revise the instructions for line 39 and the schedule to exclude all investments in entities taxed as partnerships where the interest held is a limited partnership (or similar interest in an LLC) and the arrangement is entered into solely for investment purposes. Excluding these partnership interests from Schedule R does not mean that they will not be reported. Partnership interests held for investment purposes must be reported in Part VII of Schedule D if the interest is 5 percent or more of total assets. While Schedule D reporting is based solely on an asset test, we don't think the additional income test applied in Schedule R is particularly relevant as a measurement of investment activity.

Part VI, line 16 – Joint Venture Policy: As noted above, this line asks filers whether they engage or invest in joint ventures or similar arrangements with taxable entities and, if they do, whether they have a written policy that safeguards their exempt status with respect to such arrangements. This question seems to us to be even more clearly directed at arrangements where a tax-exempt entity is partnering with one that is taxable to accomplish a charitable purpose of the tax-exempt. However, the instructions incorporate the same "passive income" test used in the instructions to Schedule R. This raises the question whether a tax-exempt organization that acquires limited partnership or similar interests in entities taxed as partnerships that carry on an active trade or business must have a policy of the type described even though as a limited partner the tax-exempt investor is not actively engaged in the underlying trade or business and the suggested safeguards make little sense. We recommend that the instructions for line 16 be revised to make clear that the question should be answered yes only when the filer engages in the arrangement in order to accomplish one or more of its charitable purposes or if the filer is a general partner or managing director for the venture.

S corporations: Although S corporations are passthrough entities, they are not partnerships for federal tax purposes. Accordingly, we read the instructions as not requiring reporting for interests in S corporations. The instructions should make this explicit.

Timing of measurement: In the example, the filer uses information from the K-1 supplied by the partnership as the numerator and total revenue and assets "for its tax year" as the denominator. The instructions should specifically state that the organization should use this methodology in making the calculation and should also inform filers whether this methodology may be followed when the partnership and the filer have different tax years (or should address how to make the calculation when tax years are different).

Filers must make both calculations: Reporting apparently is required if an interest in a partnership exceeds either the income threshold or the assets threshold. However, this is clearly stated only in the example. It should be incorporated in the instruction, although, as noted, we question the utility of an income measurement for partnership interests acquired for investment purposes.

As a final comment, we noted numerous places in the instructions that refer the reader to a particular section of the Code for more information. Please consider reproducing those sections or provide links to them.

Thank you for the opportunity to comment on the draft instructions.

Respectfully submitted,

Janne G. Gallagher
Vice President and General Counsel

From: Michael E. Malamut
To: *TE/GE-EO-F990-Revision;
Subject: Malamut IRS Ltr re Form 990 Instr.DOC
Date: Friday, May 30, 2008 6:31:27 PM
Attachments: Malamut IRS Ltr re Form 990 Instr.DOC

Attached please find my comments on the draft Form 990 Instructions. Hard copy to follow by first class mail.

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May 30, 2008

BY ELECTRONIC AND
FIRST CLASS MAIL

Michael E. Malamut
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IRS
Draft 2008 Form 990 Instructions, SE:T:EO
1111 Constitution Ave., NW.
Washington, DC 20224

Re: Draft Form 990 Instructions

Dear Sir or Madam:

I am writing as a practitioner who works mainly in the area of nonprofit governance, forming new entities and drafting or advising on governing documents and governance policies. I am one of the few lawyers nationwide who has also obtained the highest level of accreditation from the American Institute of Parliamentarians and the National Association of Parliamentarians. I commend the Service on its commitment to strong governance and its efforts to integrate best practices into the draft instructions and for its diligence in considering and incorporating comments on the draft Form 990 before it was adopted.

In addition to my practice as a lawyer and professional parliamentarian, I serve as Co-Chair of the American Bar Association Business Law Section's Subcommittee on Nonprofit Governance, a joint committee of the Corporate Governance and Nonprofit Corporations Committees; Chair of the Joint Committee of the National Association of Parliamentarians, the American Institute of Parliamentarians, and the Robert's Rules Association for Comments on the Revised Model Nonprofit Corporation Act; Treasurer of the American College of Parliamentary Lawyers; member of the Opinions Committee of the American Institute of Parliamentarians; member of the Editorial Board of *Massachusetts Lawyers Weekly;* member of the Board of the Murray Inn of Court; Adjunct Professor at Suffolk University Law School; and elected Commissioner of Trust Funds in the Town of Dedham, Massachusetts. These comments are not made on behalf of any of these organizations or my law firm, Kopelman & Paige, P.C., but solely in my personal capacity based on my expenence.

General Instructions. The general instructions indicate that they provide guidance on which entities are required to file the Form 990-N. The Form 990-N is now required for almost all small tax-exempt organizations, including small, small tax-exempts (under $5000 in annual revenues), with limited exceptions. 501 (c) (3) entities with under $5000 in annual revenues are exempt from filing Form 1023 determination requests, but still have to file Form 990-N unless they fall within one of the limited exceptions. I have also worked with many other small nonprofits that qualify for treatment under 501 (c) (4), (5), (6), (7), and (10), but that never filed Form 1024 determination

requests because their extremely small size (under $5000 in annual revenues) made the filing fees prohibitive. Many of these organizations are entirely run and led by volunteers. I may work with them on a one time basis because they wish to incorporate, adopt articles of association (if a voluntary association), or adopt or revise bylaws, but they cannot afford regular, ongoing representation. If such an organization attempts to file its Form 990-N electronically on its own, even ifit has obtained an EIN to open a bank account, it will be rejected because the Service does not have a record of the entity associated with that EIN qualifying as a tax-exempt organization. I understand that such an organization may orally request the IRS to enter its EIN into the tax-exempt database by calling the tax-exempt information telephone line and speaking with a representative. The instructions should refer to this procedure, or provide some information about how small, small tax -exempt organizations, not required to request determination letters, can still file their required Form 990-Ns.

Glossary. *Audit Committee.* The definition proposed in the instructions fits the audit committee practices of most larger organizations. It does not recognize, however, the variations on standard practice in many small- to mid-size nonprofits. For example, in many very small, volunteerrun organizations, the audit committee consists of volunteers who actually perform the audit themselves by reviewing the treasurer's books. *See* Remy M. Robert, *Robert's Rules of Order Newly Revised* (10th ed. 2000) ("RONR") pp. 461-62; Alice Sturgis, *The Standard Code of Parliamentary Practice* (4th ed. 2001) pp. 213-14. In such organizations, it is important that the Treasurer not serve on the audit committee. *Id.* Somewhat larger organizations, with some paid staff, may have outside financial review by an accounting firm, but not a full audit, which is beyond their financial means, and members of the audit committee may facilitate the financial review process and serve as liaisons between the organization and the outside accountants. Often, in these smaller organizations, there are few board members with sufficient financial expertise to serve on the audit committee and the finance committee, so the full board or the membership retain the primary power over hiring the outside accountants and the audit committee plays only an advisory role. *Id.* The instruction may want to acknowledge these variations in practice in the role of the audit committee in smaller organizations.

Glossary. *Officer.* In many membership organizations, the title of president is reserved for the volunteer presiding officer at meetings of the membership, who mayor may not have such additional duties as the bylaws may prescribe. RONR p. 440. Often, but not always, the bylaws require the president to perform significant additional administrative duties. *Id.* Few state nonprofit statutes prescribe any management duties for the president. The principal legal role of the president at common law and under most state statutes is to serve as the titular head of organization, in particular when dealing with outside organizations. Vice-presidents have no more common law duty than to succeed the president upon resignation, death, or disability. The Service should consider expanding the definition of "officer" to include all those who hold offices of trust in the

organization, which would include a president or vice president without specific management duties, but who are recognized by statute and common law as officers of the corporation.

***Part VI-Governance**, Line* 4, *changes to organizational documents.* I know that the Service would prefer not to have to retain paper documentation of every bylaw amendment and therefore is encouraging organizations only to describe significant changes to their governing documents. My concern is, however, that many smaller organizations may find it difficult to describe significant changes in appropriate detail without attaching the relevant bylaw amendment.

Many volunteer-run organizations do not have good record-keeping practices and have no idea what changes have been incorporated into their bylaws since their determination letters were issued. They know what their bylaws are now and may be able to retrieve their original bylaws only from the Service through a document request. I have worked with many small organizations that adopted bylaw revisions for no better reason than that no one in the organization was sure which copy "floating around" was the correct set. For such groups, it might be much easier simply to attach their current bylaws than to retrieve the historic bylaws and compare the two documents laboriously.

Now, in the era of scanning and electronic storage, it is much easier for the Service to store the actual bylaws in electronic form. The instruction might be more helpful to small nonprofits if it allowed attachment of copies of bylaws amendments or bylaw revisions to be filed, but restricted such attachments to electronic copies in commonly available formats such as pdf, rtf, and doc, which could be posted or e-mailed to an appropriate address at the Service for hard-copy filers.

While some filers welcome the privacy afforded by keeping their current bylaws unavailable to outsiders, certainly they agreed to waive the "privacy" oftheir bylaws when initially filing for an exemption through the Form 1023 or Form 1024. If organizations choose to keep the actual content of their current bylaws in-house, that can be their choice. Small organizations in particular, however, should be able to opt for greater transparency and disclosure by filing electronic versions oftheir current bylaws or individual bylaw amendments, at great savings for the organization in time and money over describing the detail of each significant change, a particularly onerous process when an organization adopts a bylaw revision.

***Part VI-Governance**, Line* 6, *members or stockholders.* In regard to criterion (2), in many membership associations, the members may elect the officers, but not the directors, or the members may only elect delegates, who in turn elect the officers and/or directors. In other organizations, the members may have a direct role only in approving fundamental transactions like amendments to the articles of incorporation or bylaws, mergers, and voluntary dissolutions. *See* January, 2008, Exposure Draft of Revised Model Nonprofit Corporation Act § 1.40 (25), (37), available at *http://meetings* . abanet. org/webupload/ comrnupload/CL5 *800001* sitesofinterest files/MN CAPart I.doc, promulgated by

the American Bar Association. Using "significant changes" instead of "fundamental transactions" in keeping with the definitions in Line 4, it might be more inclusive to re-phrase criterion (2) to state, "the members approve significant changes or elect the officers or members of the governing body, or elect delegates with any of these powers."

Part VI-Governance, *Line 9b, policies and procedures governing chapters.* As I read this line, it applies both to multi-tiered organizations with a group determination letter and to such organizations without a group determination letter. Some such organizations may, however, think that this is a compliance-related question directed only at organizations with a group determination letter. It may make things clearer if the instruction specifically indicates that the question is directed towards good governance practices and applies whether or not the organization has a group determination letter.

Part VI-Governance, *Line 12a, Conflict of Interest Policy.* While it is helpful to include a negative example of when dual board membership does not cause a financial conflict of interest, it may be helpful to have an example of when dual board membership may cause a financial conflict of interest, such as when two organizations compete for funding from a limited funding source or when two organizations with similar missions negotiate over ajoint awareness campaign or membership drive.

Thank you for your consideration of these com

Michael E. Malamut

Michael E. Malamut

MEM/man

347128/80000/0150

From: Jody Blazek
To: *TE/GE-EO-F990-Revision;
Subject: FW: Comments on Draft of 2008 990 instrucitons
Date: Friday, May 30, 2008 6:33:28 PM

Email Transmission to Lois G. Lerner, Ronald J. Schultz, and Catherine E. Livingston
Internal Revenue Service Exempt Organizations Division

==========

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Form 990 Instructions Draft issues April 7, 2008

Comments/suggestions of Jody Blazek CPA, Blazek & Vetterling

Highlight Pages

Information on highlight pages duplicate information in instructions and could be eliminated in some cases.

Glossary Reference

It would be helpful if words defined in the glossary were bolded in the instructions.

Core Form
Headings, Part I and Part II

Item B. Checkbox []Application Pending

This instruction should address the situation in which a new organization plans to submit, but has not yet submitted, Form 1023 or 1024. Since such organizations are not in the Exempt Organization Master File, the IRS Utah Service Center currently sends a notice suggesting the application be filed rather than asking that a Form 1120 or 1041 be filed.
For a properly organized 501(c)(3) organization, the exemption is retroactive to date of formation. Non-501(c)(3) organizations qualify for exemption without regard to the date of the Form 1024 filing. Often the revenue of new organizations is comprised of voluntary contributions excluded from taxable income by section 103 so that income tax returns are not technically due to be filed. It is, therefore, reasonable for the IRS to accept Forms 990 filed by those organizations. If subsequently exempt status is denied, normal income tax returns can be requested when denial is issued.

Item G: Gross Receipts

Instruction should be clarified by adding the following sentence at the beginning.

> "To arrive at gross receipts for this purpose, expenses that reduce revenue on Part VIII must be added back to Total Revenue reflected on line 12."

A description of the lines to be added back would provide clarity as follows:

> "Add back both columns of line 6b [rental expenses] and line 7b [cost of non-inventory assets sold, line 8b [direct expenses of fundraising events, line 9b [direct expense of gaming activities, and line 10b [cost of inventory sold]."

Part III Statement of Program Service Accomplishments

In last sentence of first paragraph, the parenthetical paragraph "(other than by raising funds)" should be removed. The sentence is very clear without it and the phrase is contradictory for the typical United Way/community fund-type organizations that raise and disburse funds to others.

Line 1: Mission

Eliminate the last sentence that says "leave this blank." Change the first sentence to say "Describe the organization's exempt purpose as articulated in the organizational documents and mission statement, budgets, or other operating plans and policies approved by the governing body." Consider whether to explain the IRS view that good governance is key to operating for exempt purposes and what the consequence of a "blank" might be (maybe to use omission as an audit tool).

Lines 2 and 3: New Significant Activity.

Text is necessary, either here or in the glossary, to express what the Service considers a "significant" new program service (Line 2) or "significant" change in how a program service is conducted (Line 3).

Line 41-4c. Program Service Accomplishments

The Donated Services paragraph should be moved forward and combined with the Expenses and grants paragraph with the following sentence. "Do not include the expense or revenue from donated services and use of facilities, materials or equipment reported under generally accepted accounting principles, but not reported for tax purposes.

The Description of program services paragraph should add examples for section 501(c)(6), (7), and other non(c)(3) filers.

Part IV Checklist of Required Schedules

Line 30. Contributions of Art, Historic Treasures etc.

Remove last sentence regarding contributions to capital from the instructions for this question that prompts

submission of Schedule M. The term does not appear in the instructions for Schedule M. The term normally applies to non(c)(3) membership organizations such as social clubs, and does not involve a contribution of the sort described in this question.

Part V Statements Regarding Other IRS Filings and Tax Compliance

Line 3. Unrelated Business Income – Form 990-T

We want to make you aware that in our experience a significant number of K-1s are incorrect as it pertains to unrelated business income. The mistakes go both ways. Often an activity that is indeed a related business (for example, a historic film project for a museum or a healthcare joint venture) is reported as unrelated. On the other side, the K-1 does not designate the tax-exempt partner as such and reports no unrelated business income.

It is our custom to report partnership income/loss items correctly even though the K-1 reports otherwise. We inform the K-1 preparer, when possible, of the mistakes to prevent future issues.

Part VI Governance, Management and Disclosures

Question 10

Board approval at a formal meeting prior to filing will be difficult in most instances in our experience. The human response to filing deadlines and reluctance of many to gather the detailed information required for Forms 990 results in the majority of returns being completed near the filing deadline. In our practice, we provide a draft for approval prior to finalizing the return to the chief executive or financial officer. Our meetings to review the return with the full board or financial committee often occur after the return is filed. We agree, then, with Jack Siegel's suggestion that approval of the form, at least once a year, be recommended without necessity for approval prior to filing.

Part VII Compensation of Officers, Directors, Trustees, Key Employees, Highly Compensated Employees and Independent Contractors

We recommend IRS consider the May 5th comments of the American Research Company quoted below and consider a tiered threshold tied to the gross revenue of the organization in the future. For example set the threshold at $50,000 for an up to $1million organization, $100,000 for a more than $10million organization, and $150,000 for a more than $100million organization.

> First, the new Form asks for a list of key employees, regardless of compensation (Part VII, Section A, 1a), while the instructions ask for this information only if compensation exceeds $150,000.
>
> Secondly, although the current Form 990 asks for compensation of the five highest paid employees who receive more than $50,000 (Schedule A, Part I, required for 501(c)(3) organizations), the new Form 990 asks for the five highest compensated employees with reportable compensation of more than $100,000. With this higher threshold in the new Form, we believe the following problems will be created: 1) less information will be provided, i.e., the highest paid employees in the $50,000 to $100,000 range will be eliminated entirely; and 2) average compensation figures obtained for the major staff positions (e.g., Deputy, V.P., Marketing, Finance, etc.) will increase substantially, and unnecessarily as the new Forms come on line.
>
> From a statistical perspective, to obtain truly accurate comparable compensation averages for staff positions, the $50,000 threshold should be removed altogether. As a practical matter, however, this figure has been used for quite some time, and there are probably few senior staff who fall below the $50,000 threshold. This is not true, however, of the new threshold of $100,000. For example, consider the current Form 990 of a 501(c)(3) organization with revenues of almost $5,000,000. The organization's 2005 Form reports that the CEO was paid $96,000, the Chief Librarian $77,000, and the Finance Manager $62,000. In the new Form 990 this information would not be reported. And yet the leaders of an organization like this one need to determine if their senior executives' pay is comparable to the compensation of others "in functionally comparable positions in similarly situated organizations" (IRS instructions for line 15, part VI). This organization, as well as all other non-profits, regardless of compensation levels, will be asked in the new Form 990 to indicate if comparability data were used in the process of determining compensation for the CEO and other key employees of the organization (Part VI, Section B, item 15). If the information is eliminated from the Forms, how are organizations expected to obtain the required comparable data?
>
> In order for organizations to continue to obtain accurate and relevant comparable data, either on their own or by using publications such as ours, it is essential to continue to capture all key employee compensation, as well as staff data for the highest paid employees, without imposing higher compensation thresholds.

Part VIII Statement of Revenue

We wonder why business codes are not provided for types of income that may include unrelated business income under the fragmentation concepts and debt-financed property. Line 6 (rents), line 7 (sale of non-inventory assets), and line 10 (sale of inventory) are lines that can contain UBI. You might consider adding codes for those lines on future versions of the Core Form.

X Balance Sheet

Line 3

Instructions should provide pledges for voluntary contributions to the organization from directors, trustees, and other related parties be listed on line 5 are reported on this line, not line 5.

Schedule A: Public Charity Status and Public Support

Part II, Line 1. Gifts, Grants, Contributions, and Membership Fees

Membership fees: Page 17 instructions for Line 1 and paragraph in Highlights should address the issue of membership fees for which disregarded benefits are provided in the form of free admission and discounts pursuant to Reg. 1.170-13(f)(8).

Unusual grants: On page 12 of the instructions, we find it surprising only the three primary criteria required for this classification are listed and the six factors found in Regs. 1.170A-9(e)(6)(ii) and 1.509(a)-3(c) listed below are omitted.

1. The grant or contribution is not made by a person (or related person) who created the organization or was a substantial contributor to the organization before the grant or contribution.

2. The grant or contribution is not made by a person (or related person) who is in a position of authority, such as a foundation manager, or who otherwise has the ability to exercise control over the organization. Similarly, the grant or contribution is not made by a person (or related person) who, because of the grant or contribution, obtains a position of authority or the ability to otherwise exercise control over the organization.

3. The grant or contribution is in the form of cash, readily marketable securities, or assets that directly further the organization's exempt purposes, such as a gift of a painting to a museum.

4. The donee-organization has received either an advance or final ruling or determination letter classifying it as a publicly-supported organization and, except for an organization operating under an advance ruling or determination letter, the organization is actively engaged in a program of activities in furtherance of its exempt purpose.

5. No material restrictions or conditions have been imposed by the grantor or contributor upon the organization in connection with the grant or contribution.

6. If the grant or contribution is intended for operating expenses, rather than capital items, the terms and amount of the grant or contribution are expressly limited to one year's operating expenses.

Part II, Line 5. Amounts exceeding 2%:

The list of organizations to which the 2% limitation does not apply will appear to some to only apply to four types listed because two major types are embodied in the explanatory paragraph. The six types should be listed in code section order as follows:

170(b)(1)(A)(i) churches
170(b)(1)(A)ii) schools
170(b)(1)(A)(iii) hospitals
170(b)(1)(A)(iv) public college support organizations
170(b)(1)(A)(v) governmental units
170(b)(1)(A)(vi) publicly support organizations

Part II, Line 9. Net Receipts from Unrelated Activities

Proceeds of special events not classified as contribution revenue should be listed as an example.

Part II, line 12. Other Income

Unless we are totally confused by what is intended to be reported on this line, we suggest the instruction can be clarified as follows:

"This line will primarily include revenues from performance of exempt function activities and other , and will include all revenues not reported on lines 7-9."

Part II, line 12, and Part IIII, line 12

A contribution from a for-profit business that constitutes a quid-pro-quo transaction in which the donor is publicly recognized are properly reported on these lines as provided in the last item in the examples for this line. A comment is needed, however, to acknowledge circumstances in which such contributions are not sponsorship payments and, thereby, are reported on line 1.

Part III, line 10 c.

In the future, this line could be entitled "Investment Income."

Part II, line 18 and Part III, line 20

Technically, the result reached on these lines is correct as we understand Reg. 1.170A-9(e)(4)(iv) and 1.509(a)-3)(c)(1)(i). In drawing up new regulations to implement the five-year support test period, we recommend the provisions of the regulations quoted above be changed to cause the organization to be reclassified as a private foundation (PF) in the year following the year in which it fails the test for two years. Since the test now includes the current year, it will be impossible to be certain that an entity has converted to private foundation status until the last day of the year. The likelihood of imposition of the penalties is high, particularly the requirement that estimated taxes be deposited for the §4940 tax.

If this change is not implemented, the instructions should be expanded to explain the requirements that were in effect because the organization has been essentially retroactively reclassified as a private foundation because the conversion occurs at the beginning of the filing year. The sanctions that apply should be clearly described, including the excise tax on investment income (§4940), prohibition against self-dealing (§4941), satisfaction of private operating foundation test (§4942), disposition of excess business holdings acquired during the year (§4943), jeopardizing investment (§4944), and taxable expenditures (§4945) due because Expenditure Responsibility is not exercised.

Schedule F: Statement of Activities Outside the United States

Highlights

We recommend you reconsider the concept that this schedule is designed only to capture activities outside the U. S. WHEN the funds to pay for the programs are disbursed from foreign accounts. The Part IV question 14, prompting completion of Schedule F, makes no mention of this distinction, It simply asks if the reporting organization "maintains an office, employees, or agents outside the U.S." [question 14a], or has "revenue or expenses …from grantmaking, fundraising, business, and program services activities outside the U.S. [question 14b].

The words and tone of the Part IV questions and the first three pages of the instructions indicate the organization will report expenditures that benefit activities and grantees outside of the United States without regard to the situs of the bank or other financial account from which the funds to pay for the activities. The instruction for column (f) in Part I, however, says "Do not report expenditures paid in the United States or outside of the listed region, even if they are allocable to the listed activity." Following this instruction literally, an organization that contracts with vendors outside the U.S. to purchase food, supplies, housing materials and other items to provide aid BUT disburses the funds from its U.S. bank account by wire to the foreign vendor will not include the expense on this Schedule.

Based on interviews with our clients who think they "conduct" activities outside the U.S. and a review of the nature of their financial transactions, we expect the information gathered with this schedule will be flawed. We have the same questions and recommend you seriously consider the points raised by Ron Larson, in his May 6th email in regard to an entity with "all of our organization's programs [are] located outside the United States."

Schedule M. Non-Cash Contributions

We thank you for the blanks in column (b) for lines 4 and 5 and hope they remain.

We also thank you for the incredible effort made to explain the extensive new requirements.

Submitted May 30, 2008 by Jody Blazek CPA

From:	Kay Guinane
To:	*TE/GE-EO-F990-Revision;
cc:	larry clpi
Subject:	Comments on Form 990 Instructions
Date:	Friday, May 30, 2008 6:41:15 PM
Attachments:	990 instruction comments.doc

Attached are the comments of the Center for Lobbying in the Public Interest and OMB Watch regarding the draft instructions for Form 990. Please let me know if you have any difficulty with the file, or any questions

Kay Guinane

Combined Federal Campaign #10201

Internal Revenue Service
Draft Form 990 Instructions, SE:T:EO
1111 Constitution Ave. NW
Washington, DC 20224

May 30, 2008

Comments on Draft Instructions for the 2008 IRS From 990

OMB Watch is a nonprofit, charitable organization that promotes government accountability and citizen participation at the national level. In our work, we encourage nonprofit organizations to participate in governmental decision-making, through advocacy, lobbying activities, and nonpartisan voter engagement. We filed comments on the draft 2008 Form 990 because we promote a transparent and accountable nonprofit sector and governmental policies that avoid unnecessary reporting burdens for nonprofits.

The Center for Lobbying in the Public Interest (CLPI) is a national, nonpartisan organization that promotes, supports, and protects nonprofit advocacy and lobbying in order to advance the mission of charitable organizations and to strengthen our democracy. CLPI filed comments on the draft 2008 Form 990, because we believe that advocacy is a core function of nonprofits in our democracy and civil society. The IRS must simplify and facilitate the ability of nonprofits to lobby and engage in nonpartisan voting and other activities within clearly defined legal parameters.

OMB Watch and CLPI appreciate the opportunity to comment on the draft instructions, which are crucial to accurate reporting and appropriate IRS enforcement.

Our comments mostly focus on the instructions for Schedule C, since that relates to civic participation through lobbying and political activities. This does not mean our comments on Schedule C comprise all of our views. In addition, the fact that we do not comment on other issues does not imply support or opposition to them.

Summary of Comments

1. *To improve organization and navigation, we recommend a Table of Contents to make finding sections easier*

2. *The lack of any definition for "substantial lobbying" makes it difficult for 501(c)(3) organizations that do not use the expenditure test to measure their lobbying activities and to answer the question in Part II-B2(a).*

3. *The question regarding volunteer hours for political activities should be limited to a "yes" or "no" or an estimate of the number of volunteers.*

4. *Specific suggestions for Schedule C Part I-A and Part II A and B to clarify the instructions and result in more accurate reporting.*

5. *In the core form the term "legislative liaison" in Part IX 11(d) should be defined or dropped.*

Comments in Detail

1. *Organization and Navigation*

We recommend a Table of Contents for Schedule C instructions to make it easier to find individual sections. There are 21 pages of instructions for Schedule C, which is only one of 16 potential schedules Form 990 filers must complete. With no table of contents, substantial time is needed to wade through the instructions to find individual sections. The line-by-line instructions do not begin until page 8. A short Table of Contents at the beginning would make using the instructions much easier.

2. *The "substantial part" definition problem*

Part II-B Line 2a-d asks charities to identify whether their lobbying activities "cause the organization to be not described in section 501(c)(3)?" In OMB Watch's comments on the draft form we said, "This is an unfair question, since these organizations have no clear definitions or thresholds to make this judgment." The draft instructions do nothing to clarify how this question should be answered. However, lines b-d asks for information about penalties for excessive lobbying, implying that the IRS has made a determination that an organization's lobbying has been "substantial."

The instructions should make it clear that the only organizations that should answer "Yes" are those that the IRS already has determined to have engaged in substantial lobbying. Otherwise, the question has great potential to create confusion and result in unnecessary IRS investigations because:

- The instructions do not provide any definition of "substantial" lobbying, either on the Line instructions at page 13, or in the definitions section. The IRS should harmonize its definitions of lobbying under the substantial part test and the expenditure test.
- The majority of 501(c)(3) organizations that file Form 990 do not elect to use Form 5768 and the expenditure test, making this question a widespread problem.

3. *The question regarding volunteer hours for political activities should be limited to a "yes" or "no" or an estimate of the number of volunteers.*

Part I-A(3) asks all organizations that engage in political campaign activities to list their volunteer hours. The instructions say "any reasonable method may be used to estimate this amount." While this may help avoid onerous reporting that would discourage volunteers from participating in civic, union, association or political organizations, the information that results is not likely to be useful for IRS enforcement purposes.

For example, a large organization with a national membership base may report 5,000 volunteer hours, which may be insubstantial in the context of its overall operations. At the same time, a smaller organization may have a dedicated corps of volunteers that also put in 5,000 hours of time. How does the IRS interpret this information for regulatory purposes? Assuming the goal is to determine whether 501(c)(4) organizations have made electoral activity their primary purpose, it appears the IRS is placing undue weight on the number of hours volunteered.

4. Specific suggestions for Schedule C Part I-A and Part II A and B to clarify the instructions and to facilitate more accurate reporting.

The following revisions to the instructions are intended to provide greater clarity and avoid reporting errors:

- Definition of terms on p. 3: Lobbying Activities. The definition should note the exceptions to the definition of lobbying so that activities such as nonpartisan analysis and research or testifying at the request of a committee chair are not reported as lobbying.
- Part II-A Definitions p. 6 Affiliated Groups. At the end of the first paragraph there is an incomplete reference to an annual revenue procedure.
- Part I-A p. 8 Note. At the end of the Note paragraph the following sentence should be inserted: "Nonpartisan activities that encourage participation in the electoral process should not be reported here."
- Part I-B introductory paragraph. Add "If no excise tax has been imposed put down "0" and answer "No."
- Part II-A Line 1(4) p. 14. There is an incomplete reference to an annual revenue procedure.

5. In the core form the term "legislative liaison" in Part IX 11(d) should be defined or dropped.

We appreciate removal of executive branch lobbying from the instructions for Part IX 11(d). This will provide more consistent data and prevent 501(c)(3) organizations from having to track two different sets of lobbying-related expenses. However, the phrase "legislative liaison services" remains in the definition of what is to be reported. As OMB Watch said in our earlier comments, "IRS rules do not define "legislative liaison services." The instructions should either remove the reference to legislative liaison services or define it in a manner consistent with 501(c)(3) regulations.

We appreciate the instructions and example in the introduction to this section. They adequately clarify how expenditures for non-employee lobbying are to be broken down into functional expenses.

Conclusion

The new Form 990 and instructions should improve accountability and transparency of nonprofit operations. They should ease the burden of compliance and reporting by nonprofits. By doing so, the IRS will improve both and help the public to understand nonprofit activities. We urge you to adopt our recommendations to help produce the best possible form and instructions, as they are likely to be in use for years to come.

Yours truly,

Kay Guinane
Director, Nonprofit Speech Rights, OMB Watch
1742 Connecticut Ave NW
Washington, DC 20009

Lawrence S. Ottinger
President, Center for Lobbying in the Public Interest
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Washington, DC 20006

From: Gregory L. Colvin
To: *TE/GE-EO-F990-Revision;
Subject: Comments from Adler & Colvin re: Schedule C instructions on behalf of four clients
Date: Friday, May 30, 2008 7:48:51 PM
Attachments: May 08 comments on 990 C instructions (00115804).DOC

Internal Revenue Service: Second attempt to send. Please disregard prior versions.

Attached please find our comments re: 2008 Form 990 Schedule C instructions. Thank you for the opportunity to be heard on this important matter.

Greg Colvin

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May 30, 2008

VIA E-MAIL

Internal Revenue Service
Draft 2008 Form 990 Instructions, SE:T:EO
1111 Constitution Avenue, NW
Washington, D.C. 20224

Re: **Comments on Instructions for Form 990, Schedule C**

Dear Internal Revenue Service:

We appreciate the opportunity to submit further comments on the draft instructions for Form 990, Schedule C, on behalf of the following clients: Humane Farming Association, a section 501(c)(3) organization with a 501(c0(4) affiliate; Olson, Hagel & Fishburn, LLP, a law firm whose practice focuses on California and federal election laws; Planned Parenthood Affiliates of California, a section 501(c)(4) organization with affiliates exempt under both section 501(c)(4) and 501(c)(3); and Washington Education Association, a section 501(c)(5) organization.

These comments focus on the instructions for reporting of political activities by non-section 501(c)(3) organizations. Consequently, these comments are directed primarily to Schedule C, Part I-C. To a large extent, we are repeating, emphasizing, and elaborating upon certain comments we made on September 14, 2007, regarding items that we believe the Service has still not addressed adequately.

Schedule C, Part I-C, Re: "Own Internal Funds" and Calculation of Section 527(f) Exempt Function Expenditures

a. Analysis

A section 501(c) organization other than a section 501(c)(3) organization must calculate its "exempt function expenditures" under section 527(f). The section 501(c) organization is liable for tax on the lesser of those expenditures or its net investment income for the year, which is reported and paid with Form 1120-POL. Lines 1, 2, and 3 of Part I-C purport to lead the filer

through this calculation of exempt function expenditures, but the draft language in Part I-C is unclear in some significant respects, potentially leading to calculation errors and, therefore, inaccurate tax assessments.

Part I-C, line 2, asks filers to "enter the amount of the filing organization's own internal funds contributed to other organizations…." In the instructions for lines 1 and 2 of Part I-C, the phrase "the amount of its own funds" is used to describe these same expenditures. In the 2006 Form 990, the term "its own funds" appears in the instructions for 501(c) organizations reporting political expenditures on line 81a.

There is no Code section or Regulation defining the term "own internal funds" or "its own funds" in relation to political or lobbying activities.

These phrases are probably the result of Reg. section 1.527-6(e), promulgated under section 527(f)(3), which refers to political contributions or dues collected (typically from members) by a section 501(c) organization and then promptly and directly transferred to an SSF. Earmarked check-off union dues are a familiar example. Prompt and direct transfers of such monies are not exempt function expenditures for the section 501(c) parent under section 527(f). All other payments made by a section 501(c) organization to an SSF for political use are treated as exempt function expenditures and are thus potentially taxable. These other payments became informally known as made from "treasury funds" or "internal funds."

This informal nomenclature is unnecessary in a tax reporting form and is potentially confusing and misleading. Filing organizations, without a definition of "internal" or "own" funds, may mistakenly believe that any assets supplied by others, including grants, loans, donations, rents, and sales—even investment income—are not internal funds. The result could be inaccurate reporting and significant under-reporting of taxable amounts. The form and instructions should require filers to clearly identify the non-taxable prompt and direct transfers to SSFs, and all other expenditures should be reported without any extra verbiage regarding the source of funds.

As drafted, lines 1, 2, and 3 use inconsistent, confusing, and inaccurate terminology, such as "directly expended," "own internal funds," and "direct and indirect." Line 3 incorrectly suggests that "indirect" expenses count as exempt function expenditures. On the contrary, Regulations section 1.527-6(b) establishes that indirect expenses are not considered exempt function expenses for a section 501(c) organization, and are not subject to tax. Furthermore, the draft overlooks Regulations section 1.527-6(b)(3), which excludes from the computation of taxable exempt function expenditures those expenses that section 501(c) organizations may make under the Federal Election Campaign Act or comparable state election laws, such as to communicate political endorsements to their members. We do not believe the Service has the authority to alter these regulations through a forms change.

While the text of the 2008 Form 990, Schedule C, cannot be revised further at this point, the instructions could be improved to lessen confusion and bring requested information into line with legal requirements.

b. Recommendations

Revise the draft instruction for Part I-C, line 1, as follows:

> "Enter the amount ~~of its own funds~~ that the organization expended for section 527 exempt function activities. Refer to Regulations section 1.527-6(b) to determine the amounts properly reported as exempt function expenditures."

Revise the draft instruction for Part I-C, line 2, as follows:

> "Enter the amount ~~of its own funds~~ that the organization transferred to other organizations including a separate segregated section 527(f)(3) fund created by the organization, for section 527 exempt function activity, except for amounts meeting the requirements of Regulations section 1.527-6(e)."

Delete as follows from the draft instructions for Part I-C, line 3:

> ~~Total of direct and indirect exempt function expenditures.~~ Add lines 1 and 2 and enter on line 3 and on Form 1120-POL, line 17b.

Schedule C, Part I-C, line 5, Reporting Payments to 527 Organizations

a. Analysis

The instructions for Part I-C, line 5, ask non-charitable section 501(c) organizations to:

> State the name, address and Employer Identification Number (EIN) of each section 527 political organization to which payments were made. Enter the amount paid and indicate if the amount was paid from the filing organization's own internal funds or were political contributions received and promptly and directly delivered to a separate political organization, such as a separate segregated fund or a political action committee (PAC).

No IRS tax form has ever required section 501(c) organizations to report such payments to section 527 organizations. As drafted, there is no minimum threshold for reporting these payments. By contrast, the Form 8872 filed by section 527 organizations only reports

contributions received of $200 or more and expenditures of $500 or more. The requirement to list **all** payments to section 527 organizations, regardless of size, could be extremely burdensome in some cases, without apparently furthering any of the Service's other goals in the redesign process. Furthermore, the draft is not clear whether the section 501(c) organization should include payments to a section 527 organization made in return for goods or services in a *quid pro quo* exchange. This must be clarified to ensure consistent reporting; we favor excluding such *quid pro quo* payments to focus on the filer's material support of section 527 organizations, not on all transactions that the filer may have with section 527 groups.

Some organizations exempt under sections 501(c)(4), (c)(5), and (c)(6), particularly in states that do not have election laws requiring the creation of separate segregated PAC funds in all cases, may not have substantial investment income to protect from the section 527(f) tax, and therefore may be accustomed to making a variety of large and small political contributions from their general funds. In addition, many section 501(c) organizations engage in frequent transactions with section 527 entities for the purchase of goods, services, admissions to events, etc. For example, unions may pay for advertising as part of a labor council political (COPE) fundraising dinner, or they may pay membership or convention fees to political parties or clubs.

The proposed revision limits the information reported to large amounts only, and would include only donative payments, not payments made in exchange for goods or services. This information should be sufficient to apprise the IRS and the public of the major financial relationships that a 501(c) filing organization may have with 527 organizations, without requiring every $200 or even $10 donation to a candidate's committee to be listed.

b. Recommendation

Revise the instructions for Part I-C, line 5, to read as follows:

> State the name, address and Employer Identification Number (EIN) of each section 527 organization to which ~~payments were made~~ the filing organization transferred $500 or more without consideration. Include only the recipients of the ten largest amounts. In column (e), ~~E~~enter the amount transferred, if any, that constituted ~~paid and indicate if the amount was paid from the filing organization's own internal funds or were~~ political contributions or dues received and promptly and directly transferred to ~~a separate~~ the section 527 ~~political~~ organization ~~such as a separate segregated fund or a political action committee (PAC)~~. In column (d), enter the total of all other amounts transferred without consideration, if any, to the section 527 organization.

We respectfully submit these further comments to the Service regarding the Form 990 Schedule C instructions. They are offered in the spirit of correcting those few potentially misleading and unduly burdensome filing requirements that remain at the end of your otherwise very commendable effort.

Very truly yours,

<signed>

Gregory L. Colvin

GLC:krb

cc: Humane Farming Association
Olson, Hagel & Fishburn LLP
Planned Parenthood Affiliates of California
Washington Education Association

From:	Euwema.Ken
To:	*TE/GE-EO-F990-Revision;
cc:	John Fallock; Euwema.Ken;
Subject:	United Way Comments on the Draft Instructions for the New Form 990
Date:	Friday, May 30, 2008 11:47:38 PM
Attachments:	Draft Comments to IRS on instructions for the new Form 990.doc

To whom it may concern,

We would like to thank the Internal Revenue Service (IRS) for the opportunity to offer opinions on the Draft instructions for the new Form 990 and associated new Schedules. We greatly appreciate the work that has been done in researching, discussing, and crafting the current Draft instructions and overall we see this as a great stride forward in making the Form 990 serve the broad purposes required of it today.

We have undertaken a detailed review of instructions in order to provide you with a response that we believe reflect the best interest of United Way organizations (UWs), Federated Fundraising organizations (FFO), and Non-profits in general. We have also sought to address what in our experience are the concerns of donors who often look to Form 990 as a means of evaluating non-profit performance as they weigh where to invest their donations for maximum impact.

Our hope is that the new Form 990 will allow for greater transparency and accountability by placing an emphasis on an organization's quantitative and qualitative outcomes. We therefore are very enthusiastic about the change IRS made to the new Form 990 allowing for an organization to report early in the form it's progress against specific, articulated objectives (now part III of the core form). It is also important that such reporting not be based solely upon those activities into which the organization makes its largest financial investment. A better basis for what three programs are identified in Part III would be those that, in the opinion of the organization, are most important to the execution of its mission, regardless of the financial resources invested. As you will see later in our comments, we have very specific reasons for suggesting this but suffice to say here that this change in the instructions is one of our highest priorities.

Attached is a document that contains our observations and recommendations. As always, if the IRS would like to discuss any of our responses in greater detail, please contact Kenneth C. Euwema, Vice

Comments to the Internal Revenue Service on the Draft Instructions for the new Form 990

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May 30, 2008

To: Internal Revenue Service
Draft 2008 Form 990 Instructions, SE:T:EO
1111 Constitution Ave., NW.
Washington, DC 20224

RE: Draft Instructions for the new Form 990

To whom it may concern,

We would like to thank the Internal Revenue Service (IRS) for the opportunity to offer opinions on the Draft instructions for the new Form 990 and associated new Schedules. We greatly appreciate the work that has been done in researching, discussing, and crafting the current Draft instructions and overall we see this as a great stride forward in making the Form 990 serve the broad purposes required of it today.

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resources invested. As you will see later in our comments, we have very specific reasons for suggesting this but suffice to say here that this change in the instructions is one of our highest priorities.

GENERAL IMPRESSION

In general, United Way of America (UWA) believes the new Form 990 will be a more useful tool to the average user, regardless of their level of expertise in reading financial reports. The approach of providing key summary information that then points the reader to supplementary information for greater detail is an improvement over having organizations prepare their own schedules with varying formats and levels of detail. The increased consistency that will be derived from the use of standardized schedules will improve transparency considerably.

UWA is also pleased to see that the IRS has incorporated into the draft instructions for Form 990 many of the points we have raised in our response to the draft revised forms as well as those made through our participation with other distinguished groups such as:

- The Independent Sector
- The Greater Washington Society of CPAs Quality Reporting Task Force.
- The Panel on Non-Profit Accountability.

We applaud the IRS for heeding the recommendations of the non-profit community in creating these draft instructions for the new Form 990 and offering us the opportunity to contribute additional comments/recommendations. At this critical stage of development, we have observed a number of areas where we believe the draft instructions could be enhanced. The remainder of this letter will enumerate in greater detail the specific points and we respectfully request that the IRS give due consideration to making further changes.

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CORE FORM – Highlights and General Instructions

Part III – Statement of Program Service Accomplishments (page 1 of 16)

In the draft instructions, the IRS requests "comments on specific examples of accomplishments to be reported by organizations in a particular sub-sector" and that IRS "intends to include these in the final instructions". Because no examples can currently be found in the draft instructions, we take this to mean that the IRS would like us to provide you with examples that can be considered for inclusion. To that end, ***we offer the following examples:***

Example #1
Funding to local impact partners as part of the organization's multi-year Community Plan focused on achieving outcomes in the four specific areas determined to be essential in improving people's lives and strengthening our community: 1) helping kids and families lead successful lives; 2) improving health and independence; 3) responding to emergency and basic needs; and 4) encouraging civic and neighborhood involvement.
$15,824,937

Example #2
Expenses incurred by the organization to assess community needs; provide outcome measurement training to various entities in the community; provide program assessment, review and selection; administer grants; provide financial and stewardship oversight of grant recipients; and participate in community partnerships to advance common goals in the four focused areas.
$2,109,656

Example #3
Community Goal: Older adults age successfully, remain in their homes and communities, and stay connected with family, friends, and neighbors.

Specific Goal #1: To improve the overall health of our senior population by 10% over a five year period as measured by annual community health index. The organization has funded a number of programs such as Meals on Wheels, the Community Senior Center's daily water aerobics program, etc. (see detailed list in

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Schedule O) which have contributed to an increase of 7.8% in the health index over the past three years. $1,069,321
Specific Goal #2: The organization…

Example #4

The organization's Center for Excellence in Early Education is an innovative learning, teaching, research, and training facility dedicated to elevating the quality of early care and education in our local community and nationally. Expenses provide comprehensive high quality early care and education to 130 children from a variety of backgrounds as well as training in early childhood development proven best practices for adult learners--educators, academics and parents. The organization's vision is that all children will have access to high quality early care and education, so they can get the best possible start in school and in life. $563,270

Example #5

All the children in our community should be born healthy and enter school ready to learn. Currently in our community, 1 in 12 children are born at low birth weight, 1 in 6 have a mother without a HS diploma, & 28% of 3rd graders are not reading on grade level. Therefore, we fund programs that we believe will have the most impact in improving these community conditions and consider those investments successful if after three years at least 19 of 20 infants weigh 5.5 lbs or more at birth, 75% or more of 3rd graders are reading at grade level, and 9 of 10 parents have at least a HS education. $1,071,643

Part VI – Governance, Management, and Disclosure (page 2 of 16)

The first sub-bullet under the second bullet point indicates that "for purposes of determining independence, a material financial benefit is defined" but as we will note later in more detail, the definition is inconsistent with the AICPA definitions and ***we recommend that IRS adopt the AICPA definition of a "direct and indirect financial interest" to avoid confusion.***

Part VII – Compensation (page 3 of 16)

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In our original comments to IRS on the Draft forms, we recommended that there be no threshold for reporting compensation but we note that IRS is establishing in the draft instructions that compensation below $150,000 need not be reported. ***As a matter of integrity and full transparency, we believe that all compensation of Officers, Directors, Trustees, and Key Employees should be made public, regardless of level.***

We contend that the public needs to hold non-profits accountable for paying reasonable compensation based on community norms. With out full disclosure about compensation paid to those who have fiduciary responsibilities for the organization's assets, the community lacks an important tool for accountability.

Part VIII – Statement of Revenue (page 3 of 16)

The third bullet point says that the instructions "Provide for classifying membership payments as contributions or as program service revenue". Clarification is needed for the other side of that… can membership payments made to an affiliated organization (like United Way of America) be reported as program expense by the payor (like a local United Way organization)? Previously these payments were recorded by the payor on line 16 (Payments to affiliates) and not included in any category of functional expense but it would seem from this instruction that these could or should now be included in functional expenses. ***We do not necessarily disagree with this position; rather we simply wish to gain clarification, if at all possible, within the instructions.***

General Instructions, Point C. – Sequencing List (page 10 of 16)

We find this section to be very helpful and applaud the IRS for endeavoring to create such a user friendly process.

General Instructions, Point D. – Accounting Methods (page 11 of 16)

We find the instruction here unclear when it says "should generally use the same accounting method on the return to report revenue and expense that it uses to keep its books and

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records". Is the IRS indicating that the reporting on all of Form 990 should be done on either cash or accrual basis?

CORE FORM 990

Item F – Name and address of principal officer

We would like to note that we are happy to see that you have allowed organizations the option of listing the organization's address as the principal officer's address. It is an important option for purposes of privacy and identity protection.

Part I – Summary, Line 1 – Mission of significant activity, **and** Part III – Statement of Program Service Accomplishments, Line 1

The instructions indicate here that one should look to the instruction for Part II, Line 1 for an explanation of "mission". In that section, it indicates that one should *"Describe the organization's mission as articulated in its mission statement or as otherwise adopted by the organization's governing body"*. ***We would recommend that in one of these two places, either here or in Part II, line 1, the organization should be instructed to state their mission statement exactly as it has been approved by their governing board.*** Doing so will assure that somewhere on this document the public and regulators will see specifically what the board approved which aids in determining if the current activities of the organization continue to be in alignment with its properly approved exempt purpose.

Part III – Statement of Program Service Accomplishments

We would like to note first our gratitude that IRS has moved the Statement of Program Service accomplishment to the front of the Core form. As we have noted from the beginning, we believe that positioning this section allows exempt organizations, like their for-profit counterparts, with the opportunity to present a written summary of what the organization has been able to accomplish relative to their mission which assists the reader in understanding the financial information that follows.

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Because the public garners its information about non-profits primarily from the Form 990, it is important to have the Form 990 present information in a format that creates the proper context for the reader. By putting the "Statement of Program Service Accomplishments" early in Form 990, the organization has the opportunity to set the context for the financial information that follows. Without that context, it is more likely that inexperienced readers will react negatively to amounts that they perceive to be "high" but in the right context, the reader understands that the specific cost may well be appropriate.

The narrative naturally should include any number of "key" metrics that assist the reader in understanding what the financial reports that follow say about the organization's efficiency and success at delivering on its mission promise. Readers of Form 990 can then factor this information into their thinking when attempting to determine whether or not the organization is worthy of their support. Without the narrative and metrics, inexperienced readers of Form 990 may be misled by any number of external factors and end up making unfounded assumptions regarding the value and contribution of the organization to the community good.

Part III, Line 2 – New Program Services

The draft instructions say to "*Answer 'Yes' if the organization undertook any new significant program service activities…*" As we indicated in our comments on the draft forms, it is unclear to us what the importance of this question would be, but since it remains as a part of the form, ***we recommend that IRS include a definition or examples of what the term "significant" means in this context.*** Significance after all can very much be in the eye of the beholder (e.g. it is a very subjective term) so providing some form of benchmark with which to gauge significance is imperative.

We would further recommend that significance be defined both quantitatively and qualitatively.

For example, many United Ways have begun to institute programs to assist people in filing for the Earn Income Tax Credit. Such a program generally is not high cost in terms

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of the money invested but engages many volunteers whose services are not reported on Form 990. These programs can be of great significance to the community because they generate millions of dollars for individuals which are then spent locally. If the measure of significance is based solely on quantitative measures like organizational expenditures, such programs may never be made public through Form 990 but if qualitative measures are also used, it may prove to be the most significant program the organization engages in.

Part III, Lines 4a-4c – Program service accomplishments

We note that the draft instructions state that organizations *"must describe their achievements for each of their three largest program services, as measured by total expenses incurred."* Similar to our recommendation for line 2, ***we recommend that significance be defined both quantitatively and qualitatively.***

Because this is a public document, we believe that the organization should be free to report what it believes are its most important accomplishments as measured by outcomes rather than just expenses.

Part IV – Checklist of Required Schedules, Line 2

With the increased focus that the Pension protection act brought to an organization's status under Section 509(a) of the tax code, it has become apparent that many organizations, while they know that they fall under 501(c)(3), do not know exactly where they are classified under Section 509(a). This is evident given the tremendous increase IRS has seen in organizations filing for changes in their classification of late.

Publication 557 contains a section (Chapter 3, Pages 30-31) that gives a very clear description of what a Publicly-Supported organization is without using the more obscure references to specific code sections and even offers examples of some of the more typical organizations that would fall into this category.

For this reason, ***we recommend that the instructions be more explicit about what an organization's classification should***

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be. The descriptions found in Publication 557 would be very helpful to reproduce or at least reference here.

Part IV, Line 6 – Donor advised funds and similar accounts

The draft instructions refer users to see the Glossary for a definition of Donor Advised Funds and similar accounts and the Glossary does a fair job of defining what a Donor Advised Fund is however it does not define what "similar" accounts are and the definition may be too generalized as it could be interpreted to apply to a number of common giving methods employed by Federated Fundraising Organizations and others.

For example, would a donation made by a donor to a specific organization through a Combined Federal Campaign be considered a similar account? Those contributions are:

- Separately identified by reference to contributions of donors (CFC requires a separate/specific accounting for CFC campaigns)
- Are controlled by the sponsoring organization (OPM dictates that contributions must be distributed to the organization of the donor's choice and what happens to contributions that were not specifically "designated" by donors)
- The donor has a reasonable expectation of advisory privileges in the distribution of the funds because OPM dictates that the PCFO must follow the donor's choice when making distributions
- Donors often choose more than one organization to be the beneficiary of their contribution
- Donors do not give advice about which individuals will receive grants
- To our knowledge, the Secretary has not exempted these contributions from being treated as Donor Advised Funds

We recommend that IRS define in the Glossary the following term:

- ***Donor Designated Contribution – Generally, a contribution:***
  - ***That is separately identified by reference to contributions of a donor or donors;***
  - ***That is controlled by a sponsoring organization;***

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- ***For which the donor or donor advisor has or reasonably expects to have agency designation privileges for no more than a period of 18 months from the date of contribution; and***
- ***For which any undesignated portion remaining at the end of the 18 month period subsequent to contribution will revert to the sponsoring organization in the form of an unrestricted contribution.***

We further recommend that IRS specifically identify that Donor Designated Contributions are not classified as "similar" to Donor Advised Funds and therefore not subject to reporting on this line.

Part IV, Line 29 – Non-cash contributions

The draft instructions for this line indicate that if non-cash contributions exceed $25,000 then check "Yes" and provide details on Schedule M. We note that this threshold has been raised from the $5,000 level originally proposed but we still believe that this threshold may be too low for organizations that run an active in-kind program as part of a multi-million dollar organization.

For example, it is not uncommon for a United Way to operate an in-kind program that handles less than a $100,000 worth of merchandise annually but at the same time has total revenue in excess of $10 million. In such a case, the organization would incur a significant administrative cost to track contribution quantities and values while the activity represents less than 1% of the organization's total contributions.

We therefore reiterate our original recommend that the IRS consider setting a threshold of 5% of total revenue or $25,000, whichever is greater. Doing so would assure that items reported here will represent material activities of the organization.

Part V – Statement regarding other IRS filings and tax compliances

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Some of the questions in this section have direct enforcement implications while others are intended to allow IRS to accomplish other goals such as cross referencing with other tax filings. ***We recommend, as a matter of providing organizations with full disclosure, that the instructions note that some items do not have specific enforcement implications.***

Part V, Line 9 – 501(C)(3)s maintaining donor advised funds

Here, as with Part IV, Line 6, ***we recommend that the glossary definition of Donor Advised Funds be made more explicit such that it is clear that some of the more common types of giving, like donor designated contributions in CFCs and other Federated Campaigns, are not to be treated as Donor Advised Funds.*** Thus, organizations that handle only donor designated contributions will not be required to complete Line 9.

Part VI – Governance, In General

We would like to commend the IRS for including in the opening paragraph wording that indicates that not all of the questions have enforcement implications. We believe that this will go far to set organizations at ease when filling out this part of the Core Form.

Part VI, Lines 1a & 1b – Governing body

We note that the terms & definitions used in this section (e.g. voting & Independent voting members of the governing body) are not consistent with the terms & definitions used by the AICPA in its pronouncements. Such inconsistency may cause confusion and lead to unnecessary errors in reporting. ***We therefore recommend that the IRS use the terms and definitions promulgated by the AICPA to define the governing body rather than creating a unique set of terms.***

Part VI, Line 5 – Material diversion of assets

The draft instructions require and answer of 'Yes' *"if the organization became aware during the year of a material diversion of assets, whether or not the diversion occurred during the year".* We believe that the intent of IRS with this instruction it to include only those diversions that are

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verifiable and proven (e.g. if the organization is only aware of allegations that have been verified) at the time of filing Form 990. Requiring organizations to report when they are only aware of a possible diversion, would put the organization in a potentially harmful situation should the allegations later prove unfounded (e.g. could be sued for libel/slander).

Therefore, ***we recommend that wording be added to clarify that only after an organization has "become aware of a verifiable/proven" diversion, should it be reported on Form 990.***

Part VI, Line 11 – Addresses of officers, directors, etc.

We would like to note that we are happy to see that you have allowed organizations the option of listing the organization's address as the address of Officers, directors, etc. It is an important option for purposes of privacy and identity protection.

Part VII – Compensation, Overview

Current five highest compensated employees: As we indicated in our response to the draft forms, we believe that moving the threshold for five highest paid employees from $50,000 to $100,000 is too arbitrary of a change. While we agree that the $50,000 threshold is too low in today's economy, doubling it sets it too high given the large number of new, smaller organizations that have entered the non-profit sector in recent years. A threshold that is too high limits the value of Form 990 as a tool for monitoring the fiscal responsibility of a smaller or younger organization.

It is important that there be significant disclosure of salary information in the non-profit sector overall, and a threshold that is too high diminishes the value of Form 990 as a monitoring tool. ***Therefore, we recommend the IRS consider establishing a threshold of "10% of total revenue or $100,000, whichever is less".***

Key employees: We note that while until now, all compensation of key employees was to be reported on form 990, regardless of compensation level (e.g. no threshold) the

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draft instructions now indicate that there is to be a threshold of $150,000 or more for reporting in Part VII and a range of $100,000 to $150,000 for inclusion on Schedule R. We believe that it is very important to accountability within not-for-profit organizations that compensation of key employees, particularly the CEO and CFO, be reported regardless of level. These two positions in particular generally have significant influence over the disposition of the organization's assets and creating mechanisms that will remind them that accountability is vital to maintaining trust.

By reporting CEO & CFO compensation regardless of level, it serves as both

- a reminder to that person that their compensation is of interest to the community, and
- a check/balance against that person potentially mis-appropriating organizational assets (e.g. people will be better able to recognize and challenge them when they appear to be living above their means).

An example of why this is important was provided by one of our local United Way members as follows:

> *If UWRI incorporated the suggested language of the draft instructions (e.g. "threshold of 10% of total revenue or $100,000, whichever is less"), none of our Five Highest Paid Employees, whom we classify as Key employees, would make the list. Our concern is that we have been posting our Form 990 on our website in an effort to be transparent with our donors and community. Now if these changes occur in the thresholds, the community will receive less information, making our reporting less transparent.*

Another valid example comes from the very real situation that occurred several years ago in Michigan. In that case the CFO of a charity was found to have been misappropriating organizational assets but because her compensation was not properly reported on form 990, (and in the case of the proposed thresholds would properly not be reported in the

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future) the community (and the CFO's neighbors) were not given the information necessary to have raised the question of whether or not the person was living above her means. Hopefully, if such information is readily available to the public, they can serve as a link in the chain of internal control by calling their suspicions to the attention of the organization's board.

Therefore, ***we recommend that IRS restore the old standard, namely no minimum level, for reporting compensation of Key Employees in both Part VII and schedule R.***

Additionally, we would like to express our appreciation for IRS removing the rather vague statement *"materially effect the organization's operations"* with a more quantitative measure of *"5% or more"*. We believe that this measure makes identifying which employees are key employees much simpler.

Part VIII – Statement of Revenue, Line 1a – Federated Campaigns

In our response to the draft forms, we noted that the draft instructions provided at that time indicated that organizations who are the indirect recipients of funds through a Federated Fundraising Organization (like a United Way) should report such revenue on line 1a. However it remains unclear from the current draft instructions if this is also where the Federated Fundraising Organization is to report the proceeds from its campaigns, whether designated to another organization or as an unrestricted contribution to the FFO itself. The definitions of types of contributions provided in the current draft instructions do not appear to address where to record contributions that are "direct" contributions to the FFO because they only talk about "indirect" contributions received from a FFO. Therefore, ***we recommend that at a minimum the IRS add clear language to the instructions indicating that FFOs should report all contributions on line 1a.***

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Better still would be to have two lines, one indicating contributions to a FFO that the FFO raised themselves and one indicating the contributions to a FFO or other organization that were raised by someone else. It is important to note that in today's global economy, companies often operate in multiple municipalities served by multiple FFOs but prefer to run a single, company-wide fundraising effort. Thus, it is not uncommon for one FFO to raise money that is designated to another FFO. Having two separate lines to report the different kinds of contributions will maintain a level of clarity that has long been part of form 990.

Part VIII, Line 1c – Fundraising events (example)

The example given appears to be in inconsistent with the draft instructions for line 8a. In the example the value of the item received in exchange for the contribution is $16 which to most would seem to be an item of "nominal value" while the instructions for line 8a indicate that an item of nominal value given in exchange for a contribution would not qualify as a fundraising event and should not be reported here.

Perhaps the IRS is making an implication that items with a value less than $16 would be considered "nominal value" but once the value reaches the $16 threshold, it has risen above "nominal value" an would then be considered a fundraising event. If this is the case, we would suggest that IRS be more explicit in both areas of the instructions.

Regardless, ***we recommend that IRS clarify the instructions in both areas so that there is no confusion on the issue of what constitutes "nominal value" and therefore triggers classification as a fundraising event.***

Part VIII, Line 1g – Non-cash contributions

As we indicated in our comments on the draft forms we believe that a set dollar value threshold is inappropriate. We note that IRS has raised that threshold from the $5,000 originally suggested to $25,000 but we still contend that for large organizations, non-cash contributions of even $25,000 may be immaterial. A more

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balanced approach would be as we recommended in our response to the draft forms. ***We therefore reiterate our recommendation that the IRS consider setting a threshold of 5% of total revenue or $25,000 whichever is greater.*** Doing so would assure that items reported here will represent material activities of the organization.

We would also like to take this opportunity to commend IRS for responding to our recommendation of including clear guidance in the instructions on the handling of marketable security gifts, specifically when they are immediately converted to cash.

Part VIII, Line 2 – Program Service Revenue

We believe that the instructions for the current form 990 do a better job of defining what program service revenue is than do the draft instructions. Therefore, ***we recommend that IRS use the old wording here to assure clarity and consistency.***

Additionally, it is unclear from the current instructions and draft instructions if this is the line where a Federated Fundraising Organization would report any fees they deduct to recover their costs for fundraising and processing fees on behalf of other organizations. Therefore, ***we recommend that the IRS provide this guidance in the instructions on where such revenue should be reported.***

Part IX, Line 11c – Accounting Fees

Many organizations outsource their payroll function. It is unclear however if the fees associated with this type of service would be considered an accounting fee and reported on this line or some other line, say line 11g (other fees for services) or perhaps line 13 (office expenses). Therefore, because this type of service is so prevalent, ***we recommend IRS consider including a reference to this type of service specifically in the instructions for whatever line it should be recorded.***

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Part X – Balance Sheet

Generally Accepted Accounting Principles use the term "Statement of Financial Position" instead of "Balance Sheet". We believe that for the sake of consistency in reporting it would be advisable for the IRS to adopt the GAAP term for this report and therefore ***we recommend titling Part X as Statement of Financial Position.***

Schedule A – Public Charity Status and Public Support

Highlights

This opening session does a fairly good job of explaining how to determine which category an organization falls into and then which form to file, even if the organization finds that their status has changed. However, it is unclear what the regulatory implications are for an organization finds its status has changed and has followed these instructions to fill out the schedule properly. ***We therefore recommend that IRS include guidance in this section on what the organization should do subsequent to filing Form 990 if their status has changed (e.g. what additional forms should be filed to assure that their new status is properly recorded in the IRS Master file, direction to other publications that will help them understand the implications of now being classified differently, etc.)***

Accounting Method

We are happy to see that the instruction now allow organizations to report for the Public Support tests using the same accounting method it uses for its Financial Statements. For organizations like United Way who are in the Health and Human Service sector, GAAP rules require accrual based accounting so having to convert our reporting to Cash basis for the support schedule (as has been the requirement up to now) has been a significantly time consuming and tedious burden on organizations. We have also long questioned the value of reporting on Form 990 using different accounting methods compared to the potential confusion it may cause readers. This is a welcome change for us and we believe it will be beneficial to all who use the new form 990.

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Part I, Lines 1 through 11 – Reason for Public Charity Status

As we stated above, does a fairly good job of explaining how to determine which category an organization falls into however, the examples given reference very specific code sections that are not very well know to the average preparer of the Form 990 (as evidenced by the rush of changes in status filed since the passing of the Pension Protection Act). Among the approximately 1,300 local United Way organizations in the United States, we found that nearly 10% were improperly classified on the IRS master file, despite the fact that Publication557 references United Ways as an example of a specific type of organization under the code.

We believe that it is incumbent on IRS, and their fervent desire to create a set of instructions for the new Form 990 that is as informative and "user friendly" as possible so including examples that provoke images of existing organizations or referencing where to go for additional guidance that contains such examples would be most beneficial. Therefore, ***we recommend that IRS refer to specific code sections parenthetically only and add wording that will help users relate to an existing example of the type of organization that is being referenced (as Publication 557 does).***

Part II, Line 1 – Gifts, Grants, Contributions, and Membership Fees Received

The definition provided in the draft instructions for "Unusual Grants" seems a bit vague due to the use of terms like *"unusual and unexpected"* and *"substantial"* which can be very subjective.

For example, suppose one year an organization receives a one time grant for hurricane relief of $500,000 but each of the next two years they receive additional similar grants because each year they are hit with hurricanes. One could argue that while they are unusual because they never received a grant before the first year of the three, but can you still argue that they are unexpected after the first time it happens? After all, the organization operates in an area that is prone to hurricanes and they have received such a grant before so isn't it reasonable to expect that when another hurricane

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strikes, there would be the potential for additional relief grants?

Another example: Suppose an organization is the beneficiary of a $50,000 bequest from a prominent member of its community that had rarely contributed to or participated with the organization prior to dying. It seems that this gift would fit the unusual and unexpected definition but what if over the next three years they receive four similar bequests from people who were all close friends of the first donor? Surely each bequest would be considered unexpected because the donors did not notify the organization prior to death that they were named in the will but at what point does the bequest cease to be unusual?

Also, by inference it seems that the definition of "substantial" here is defined as *"large enough to endanger the organization's status as normally meeting either the 33-1/3% public support test or the 10% facts and circumstances test."* However the instructions do seem to make it clear that this is the threshold to be used.

We recommend that the instructions replace the term "substantial" with the term "extraordinary item" as defined by the AICPA.

Part II, Line 15 – Public Support Percentage from 2007

The "TIP" in this part of the draft instructions indicates that organizations that reported in prior years on a cash basis should report those numbers again and report on the accrual basis for only the current year. We are concerned that this will cause inaccurate interpretation of this section because they will be presented with numbers for comparison that are not displayed using the same basis (e.g. it creates an apples to oranges comparison with will be confusing). While it is true that the organization has the opportunity to explain the difference in the basis and its implications on Schedule O, we believe that most readers will not get that far and thus be left confused.

We are obviously concerned about the public perception of inconsistency by the organization but also question what purpose is served for IRS by displaying the information this way. ***We therefore request that IRS reconsider the necessity***

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of reporting prior year information in this section and only require prior year information be provided if the organization fails the test in the current year.

Schedule B – Schedule of Contributors

Part 1, Column D

We realize that these instructions have not changed substantially from the current Form 990 but we feel compelled to point out, as we did in our response to the draft revised forms, that this column has the potential to create confusion on the part of preparers and readers of the form.

We note that the draft instructions do now define a "contributor" (person) as including individuals, fiduciaries, partnerships, corporations, associations, trusts, and exempt organizations. Additionally we note that the instructions do now clearly state that any gift that is not a payroll deduction or non-cash contribution should be checked off in the "Person" category. However, it seems that the term "Person" does not properly describe what type of contribution it is, basically anything other than payroll deduction or non-cash.

Since the forms themselves are no longer subject to edits, ***We recommend that the IRS make a note to change the term used on the form to "Other" in the next version of the schedule so as to be clear for preparers and readers exactly what is being reported there.***

An additional observation is that there are often multiple contributions received from a single donor that come in different forms and would therefore fit into multiple categories. We note to our delight that the instructions now indicate that in such cases we should *"Check all that apply for the contributor listed".*

Schedule C – Political Campaign and Lobbying Activities

Definitions

When an organization employs someone to participate and advocate in the area of public policy on behalf of the organization and its affiliates, it is unclear from the

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definitions if this cost (salary & benefits) should be included as Direct Lobbying and/or Grassroots lobbying. The only reference to salaries in this section of the draft instructions indicate that salaries are "in-house" expenditures but there doesn't seem to be a direct relationship to what category the in-house expenditures would fall.

We recommend that wording be added to indicate clearly that the expenditures could fall into either category depending on what type of lobbying the person is engaged in (e.g. splitting the cost out and/or spreading it over all the various categories using some reasonable and objective cost allocation method is acceptable).

Part II, Line 1d

The instructions here indicate that one should report all other expenditures (excluding lobbying) related to its exempt purpose. Does this mean that it should not include expenditures associated with the production of Unrelated Business Income and perhaps several other activities that while not specifically related to the organization's exempt purpose, they may be appropriate and acceptable activities for such an organization (like rental of office space it owns to other organizations)?

It is unclear from the instructions if this line is to be used for reporting all other expenses or if there is a select group of expenses that go here.

We recommend that the IRS clarify precisely what it means by "exempt purpose expenditures" and clearly state what exceptions exist.

Part II, Line 2, Point 3

We suspect that instructing organizations to complete line 2a, columns (a) and (e) if 2008 is the first year of a 501(h) election is a typographical error. ***We suspect that organizations should be instructed to complete line 2a,***

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columns (d) and (e) if 2008 is the first year of a 501(h) election.

Schedule D – Supplemental Financial Statements

General observation:

The name of this schedule is somewhat deceptive for users as the common term used in GAAP financial statements for this type of information would be Supplemental Financial "Information" rather then "Statements". Consistency in terms would be beneficial here for transparency purposes. So, while we understand that the forms themselves are no longer a subject to revision, ***we recommend that IRS consider renaming this form at some time in the future when changes are being contemplated.***

Part I

As we noted relative to the Glossary and the Core Forum (Part IV, line 6), we are concerned about the definition of exactly what differentiates a "donor advised fund" from other types of contributions that, while similar to a donor advised fund are not exactly the same thing. Assuming the IRS revises the term in the glossary and the reference to "other similar funds" in the draft instructions for the Core Form (Part IV, line 6), ***we recommend that IRS be careful to make reference to those sections and edit the instructions here similarly to assure consistency throughout.***

Part V – Endowment Funds

We would like to thank the IRS for not requiring organizations to report summary activity for the prior four years in addition to the current year. As we indicated in our response to the draft revised forms, this change prevents an undue reporting burden for organizations during the transition to the new form with minimal negative impact.

Additionally, we thank the IRS for adding line 4 to the form where the organization is directed to explain the intended uses of endowed funds. As we noted in our response to the draft forms, since endowments are established for a variety of reasons, we believe that transparency can be enhanced if readers of Form 990 understand the purpose of the endowment.

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Part VII – Investments-Other Securities

The draft instructions appear to refer to two different "5%" tests (e.g. 5% of the organization's total assets vs. 5% ownership interest in the outstanding shares of another entity) which may confuse readers. ***We recommend that IRS review the general instruction for this part and edit the wording to make clear that readers don't confuse the two different tests and thereby report too little or too much information in this section.***

Schedule I – Grants and Other Assistance

Part II – General comment

GAAP refers to contributions received that are restricted by the donor to be transferred to another organization as "agent transactions" and therefore are considered neither revenue nor expense on audited financial statements. However, as we noted in our response to the draft revised Forms, we believe that Federated Fundraising Organizations should continue to record such activity as revenue and expense on Form 990.

It is important to note that Federated Fundraising Organizations generally have many such transfers every year and the requirement in the draft instructions to report on "each" organization that receives in excess of $5,000 annually could prove particularly burdensome for FFOs.

For example, because Combined Federal Campaigns are considered to be 100% agency transactions (classified as donor designated contributions under our recommended definitions above), there would be literally hundreds, if not thousands of organizations subject to specific reporting on this schedule.

Therefore, ***we recommend that the IRS consider allowing organizations to report based on a threshold of $10,000 or 5% of total program expenditures (core form, part IX, line 25, column B), which ever is less***.

Part II, Column B

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As we noted in our comment on the draft forms, while Federated Fundraising Agencies go to great lengths to gather information on the agencies they fund, it is not always possible to garner an Employer Identification Number for every agency receiving funding (especially when it comes to donor designated contributions). Thus requiring this information will add a tremendous administrative burden to such organizations for what seems to be little substantial benefit to users or the IRS.

We therefore recommend that the instruction simply ask for that information, when available, and assure organizations that there is no penalty to the organization for failing to provide it.

Part II, Column H

The instructions for this column indicate that organizations are to describe the purpose of the grant but not to use broad terms. In the example given preparers are instructed to give not only the purpose but also what was given. Unfortunately, the space allowed on the form is insufficient for such descriptive information.

In addition, Federated Fundraising Organizations typically give multiple grants to the same organization, each having a specific and different purpose. There is certainly not sufficient space on the form in column h to provide that much information and the draft instructions specifically state that one should include everything on a single line (see instruction for column d).

Given that the form is no longer the subject of revision, ***we recommend that IRS make completion of this column optional until such time as the form can be revised.***

Schedule J – Compensation Information

Part I, Line 3

We would like to commend the IRS for including this question in the form it exists currently. We believe it is a very good indication of what good governance looks like in any organization and it is worded in positive rather than negative way.

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Part II

We would like to reiterate our recommendations from the Core Form, Part II in that we believe that compensation for all Key Employees should be reported, regardless of compensation level and that the threshold for the five highest paid employees being set at $150,000 is too high.

Schedule K – Supplemental Information on Tax Exempt Bonds

We would like to commend the IRS for making all but Part I optional for 2008. In future years when the other parts will be mandatory, it will be a significant amount or work beyond what was previously required so allowing organizations to include what information they currently have available will be good for transparency and help them identify what information they will need the following year without having to invest the time right now to gather it all.

However, we believe that this may still be too aggressive given the level of detail that will be required and therefore ***recommend that the other parts be optional for a longer period of time.***

Schedule L – Transactions with Interested Persons

We would like to commend the IRS on the design of this form and its related instructions. We believe it will help further accountability among exempt organizations.

However, the definition of “interested persons” needs to be clearly defined and because the term is also used in several other parts of Form 990 and the Schedules, we recommend that it be the same through out in order to promote consistence of application.

We recommend the definition of Interested Persons should be added to the Glossary and propose it be defined as follows:

1) ***any current officer, director, trustee, key employee, whether or not compensated (as listed in Part VII, Sec A)***
2) ***the top 5 current highest compensated employees (as listed in Part VII, Sec A)***

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3) ***any <u>former</u> officer, key employee, or highest compensated employee who received more than $100k (or whatever this threshold is) of reportable compensation from the organization or any related organization (as listed in Part VII, Sec A)***
4) ***any <u>former</u> director or trustee who received more than $10k of reportable compensation from the organization or any related organization (as listed in Part VII, Sec A)***
5) ***any close relative or immediate family member of 1-4 above:***
    - ***spouse***
    - ***children***
    - ***siblings***
    - ***parents***
    - ***grandparents***

5) any entity (tax exempt or non tax exempt) that is owned by or controlled by individually or a combination of 1-5 above

Also, see comments for Schedule R which recommends defining a direct and an indirect financial interest in accordance with the AICPA's definition.

<u>Schedule M – Non-Cash Contributions</u>

<u>General</u>

We would like to reiterate our recommendation relative to the Core Form, Part VIII, Line 1g. A simple threshold of $25,000 in the aggregate of non-cash contributions is not a level that serves the needs of accountability and transparency effectively. For all the reasons stated earlier, ***we continue to recommend a threshold of $25,000 in aggregate value or 5% of total revenue, whichever is greater.***

<u>Line 5</u>

One type of common non-cash contribution received by exempt organizations is office supply items (e.g. pens, pencils, paper, toner, etc.). It is unclear from the instructions if these items would be classified in the same category as "household goods" or if the IRS intends these items to be listed on lines 25 – 28, namely "other".

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If these items were to be listed in the "Other" category, the organization would be strapped with a significant reporting burden relative to the sheer number of items contributed. Therefore, ***we recommend that they be included on line 5 and that IRS add to the description of "household goods" the term "general office supplies", thereby relieving the organization of the added burden of listing the number of contributions.***

Lines 9 – 12

The instructions for Schedule B, Part II indicate that contributions of stock are considered non-cash contributions even if they are immediately sold. However, the draft instructions for lines 9 – 12 of this schedule do not make reference to this definition. ***We recommend that the IRS include a similar instruction here or make reference to the instructions for Schedule B, Part II.***

Schedule N – Liquidation, Termination, Dissolution or Significant Disposition of Assets

The "Purpose of Schedule" section references a disposition of more than 25% of its net assets through a contraction, sale, exchange, or other disposition. It seems fairly obvious what constitutes a sale, exchange or other disposition and reporting such activities seem like a good addition to aid in transparency. However, the term "contraction" is rather vague and needs better definition, particularly what role the Board's conscious decision to contract and the reason for doing so plays in whether or not it meets this 25% test.

For example, we would agree that if the Board decides to downsize the organization and seeks fewer donations, reduces staff and/or services, etc. then indeed it should be reported here. However, it is possible for an organization to suffer a "down year" where by no conscious choice of the board, revenues fall by 25% or more and as a result, the board orders a proportional decrease in expenditures. In such a case, it seems that the contraction should not rise to the level of reporting it on this schedule.

Another common example of a situation where a contraction of 25% or more should perhaps not be reported would be when an organization experiences a large increase in revenue one year (perhaps from a large grant) and then a contraction of

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similar proportion as the organization "spends down" the grant proceeds. Again it seems that such a contraction would not need to be reported.

Therefore, ***we recommend that IRS either remove the term "contraction" from the instructions or provide a definition for the term that includes a qualitative measure for what constitutes a contraction that should be reported.***

Schedule R – Related Organizations and Unrelated Partnerships

We note that the definition of "related" requires the element of "control" which is further classified as direct or indirect. Indirect control is not defined anywhere but an example is provided in this section of the instructions. Indirect transactions/relationships are also referenced in Schedule L (Transactions with Interested Parties) and the definition of independent member of governing body per the Glossary. Adopting the AICPA definition would further clarify the distinction between direct and indirect financial interests and provide some consistency for reporting.

Also, there are inconsistencies in the classification and reporting of individuals (e.g. Board Member, Manager, Relative) throughout the Instructions and Glossary. A definition of interested persons might be helpful.

Therefore, we recommend the IRS adopt the AICPA's definition of a direct and a material indirect financial interest, define interested persons and include these definitions in the glossary. In addition, definitions of business relationship, independent member of governing body, conflict of interest policy and control should be revised as applicable.
Also, ***there is a reference to "indirect control" which we believe ought to be replaced with the term "indirect financial interest" as defined by the AICPA.***

Finally, see our comments for Schedule L which provides a sample definition for interested parties.

Below is an excerpt from Rule 101 of the AICPA's Code of Professional Conduct and a sample definition for interested persons for reference by the IRS in crafting these definitions.

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17 101-15—Financial relationships.

Interpretation 101-1 [ET section 101.02A.1] states that independence shall be considered to be impaired if, during the period of the professional engagement, a covered member had or was committed to acquire **any direct or material indirect financial interest** in the client

Definitions

A **financial interest** is an ownership interest in an equity or a debt security issued by an entity, including rights and obligations to acquire such an interest and derivatives directly related to such interest.

A **direct financial interest** is a financial interest:

1. Owned directly by an individual or entity (including those managed on a discretionary basis by others); or

2. Under the control [fn 39] of an individual or entity (including those managed on a discretionary basis by others); or

3. Beneficially owned through an investment vehicle, estate, trust, or other intermediary when the beneficiary:

   a. Controls the intermediary; or

   b. Has the authority to supervise or participate in the intermediary's investment decisions.

An **indirect financial interest** is a financial interest beneficially owned through an investment vehicle, estate, trust, or other intermediary when the beneficiary neither controls the intermediary nor has the authority to supervise or participate in the intermediary's investment decisions.

A financial interest is **beneficially owned** when an individual or entity is not the record owner of the interest but has a right to some or all of the underlying benefits of ownership. These benefits include the authority to direct the voting or the disposition of the interest or to receive the economic benefits of the ownership of the interest.

FN39 - When used herein, the term *control* includes situations where the covered member, individually or acting together with his or her firm or with other partners or professional employees of his or her firm, has the ability to exercise such control. [Footnote renumbered by the revision of interpretation 101-1, April 2006. Footnote subsequently renumbered by the Professional Ethics Executive Committee, July 2007.]

Implementation Periods

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A massive re-design effort presents many challenges for both the IRS and the filing community. United Way of America, like Independent Sector and many other organizations, has joined the IRS in working to inform exempt organizations about the proposed changes. Despite these efforts, many organizations are still unaware of the proposed changes. Even once organizations and their professional advisors are aware of the revised Draft, they may lack the where-with-all to invest the many hours necessary to analyze and understand the changes.

Like the IRS, United Way is eager to move forward with an improved Form 990 but we realize that organizations must have sufficient time to understand and implement the significant changes that will be required. The full value of Form 990 can only be achieved if we prepare Form 990 on a consistent basis. Thus, organizations like us will need time to create new guidance & training for members and affiliates to assure that they make the necessary changes in their record keeping systems.

We believe that it will serve the non-profit sector best if, after the Service has had a reasonable amount of time to review comments from the field, they take the time necessary to make further improvements to the draft instructions. While in some areas this may even require additional comment periods, we believe the investment will be worth the effort.

Thus, while the IRS did not accept our recommendation during the comment period on the forms to delay implementation of the Revised Form 990 until reports are due for Fiscal Year 2009 activities, ***we now recommend that the IRS put forward an aggressive plan for significantly increasing exempt organization training on the preparation of the new Form 990.*** All of us have too much invested in the revision of Form 990 to rush to implementation without adequate preparation at this defining moment.

Conclusion

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This letter represents the view of United Way of America and its approximately 1,300 member organizations nationwide. It reflects those issues that we believe are of most direct importance to Federated Fundraising Organizations like us.

United Way of America again thanks the Internal Revenue Service for affording us this opportunity to provide comments and recommendations aimed at making the revised Form 990 most useful to all constituencies. We would welcome the opportunity to participate in any future discussions about these instructions as IRS continues to review and modify them.

If the IRS would like to discuss any of our responses in greater detail, please contact Kenneth C. Euwema, Vice President of Membership Accountability, United Way of America.

Sincerely,

Kenneth C. Euwema, for
The United Way of America Financial Issues Committee

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