AMERICAN COUNCIL ON EDUCATION

DIVISION OF GOVERNMENT & PUBLIC AFFAIRS

501(c)(3) DUE DILIGENCE
Form 990 Checklist

The Internal Revenue Service recently redesigned the Form 990. As a result, non-profit organizations will be required to disclose, under penalty of perjury, whether they have in place various polices and procedures, some of which are mandatory under the Internal Revenue Code or the Sarbanes-Oxley Act of 2002. Other policies and procedures are voluntary but may become mandatory over time or may expose a non-profit to adverse publicity if absent. Below is a checklist of these rules, based primarily on the reporting requirements set forth in the new 11-part core form. The rules become effective for returns filed for the applicable deadline in 2009 for organizations with tax years beginning on or after January 1, 2008.

The adoption of the policies and procedures discussed below will prevent compliance issues before they arise. In the face of intensified scrutiny of non-profit governance, tax-exempt organizations can best defend themselves by being prepared.

Suggested or required written policies:

- ☐ Conflict of interest policy for board members, officers, and senior staff
  - Outlines procedures to determine whether a relationship, financial interest, or business affiliation results in a conflict of interest
  - Details the appropriate response when a conflict is identified
  - Requires annual disclosure of interests, such as a list of family members, substantial business or investment holdings, and other transactions or affiliations with businesses or other organizations
  - Ensures any potential excess-benefit transactions are scrutinized and approved by a disinterested decision-making body[1]
  - Requires periodic review of compensation arrangements, partnerships, joint ventures, and arrangements with management organizations to prevent inurement, impermissible private benefit, or an excess benefit transaction

[1] Pursuant to I.R.C. § 4958, a manager of a tax-exempt organization who approves an excess-benefit transaction may be subject to intermediate sanctions.

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- Whistleblower policy[2]
    - Establishes procedures for the receipt, retention, and treatment of employee complaints regarding suspected financial impropriety or misuse of the organization's resources

- Document retention and destruction policy[3]
    - Provides guidelines for maintaining and documenting the storage and destruction of electronic and hard-copy files
    - Outlines backup procedures, archiving of documents, and regular check-ups of the reliability of the system

- Investment and/or joint venture policy
    - Outlines procedure to evaluate relationship with taxable entity and safeguard the organization's exempt status
    - Outlines procedure to evaluate exempt organization's investment in sophisticated financial products or investments that require financial and investment expertise and, in some cases, the advice of outside investment advisors

- Gift acceptance policy
    - Requires review of any non-standard contributions
    - Provides for substantiation of gifts of more than $250
    - Provides for periodic monitoring or compliance under state charitable solicitation laws
    - Outlines policy with respect to acceptance of gifts
    - Outlines potential IRS reporting obligations

- Easement policy
    - Describes the periodic monitoring, inspection, and enforcement of any conservation easements

- Expense Reimbursement policy (see also Compensation committee below)
    - Outlines the procedure for the payment, reimbursement, or provision of the following expenses:
        - First-class or charter travel
        - Travel for companions
        - Tax indemnification and gross-up payments
        - Discretionary spending account
        - Housing allowance or residence for personal use
        - Payments for business use of personal residence

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[2] The Sarbanes-Oxley legislation imposes criminal liability on tax-exempt organizations for retaliation against whistleblowers. *See* 18 U.S.C. § 1513(e) (2008).
[3] The Sarbanes-Oxley legislation imposes criminal liability on tax-exempt organizations for destruction of records with the intent to obstruct a federal investigation. *See* 18 U.S.C. § 1519 (2008).

        - Health or social club dues or initiation fees
        - Personal services (maid, chauffeur, chef)
    - Requires substantiation prior to reimbursement for the expenses listed above

- Executive Compensation policy (see also Compensation committee below)
    - Outlines the procedure for establishing compensation for the organization's chief executive, officers, and "key employees"
    - Provides that the following procedures will be implemented so that payments under the organization's executive compensation arrangements are be presumed to be reasonable:[4]
        - Compensation will be reviewed and approved by the board of directors or a compensation committee thereof, provided that persons with conflicts of interest are not involved in this review or approval
        - Compensation is reviewed and approved using data as to comparable compensation for similarly qualified persons in functionally comparable positions at similarly situated organizations
        - There is contemporaneous documentation and recordkeeping with respect to the deliberations and decisions regarding the compensation arrangements

- Parent-subordinate consistency policy
    - Ensures activities and operations of local chapters, branches, or affiliates are consistent with those of the parent organization

Suggested procedures:

- Contemporaneous documentation of meeting minutes of board and committees

- Board review of the Form 990 prior to submission to the IRS

- Publicly available organizing documents, conflict of interest policy and Form 990 (including financial statements)

[4] Treas. Reg. section 53.4958-6 set forth this three-part "rebuttable presumption" test that charities are encouraged to rely upon when determining executive compensation. If all three components are met, the IRS can rebut the presumption of reasonableness only if it develops sufficient contrary evidence to rebut the probative value of the comparability data relied upon by the authorized body. If all three components are not met with respect to compensation of the organization's chief executive, officers or key employees, the organization will not be able to rely on the rebuttable presumption of reasonableness if questioned by the IRS.

- Provide donors and the public with information about fundraising costs and practices

- Board composition reflects broad public interest and minimizes potential for misuse of charitable assets
  - Includes independent members with broad public interests
  - Selected with organization's needs in mind
  - Is of appropriate size
  - Is not dominated by individuals with family or business relationships related to the organization
  - Delegates responsibilities to executive committee or advisory committees (organizations with large boards)

- Periodic review with staff of the rules constraining lobbying and political activities

- Uncertain tax positions recorded according to the two-step process outlined by the Financial Accounting Standards Board (FASB) in FIN 48.[5]

- Periodic review of organization's mission and organizational documents

Suggested committees:

- Compensation committee

  - Relies on the rebuttable presumption test of Treasury Regulation section 53.4958-6

  - Identifies five currently highest compensated employees who receive reportable compensation of more than $100,000 from the organization or any related organization

  - Identifies any former officers, key employees, or highly compensated employees who received more than $100,000 of reportable compensation on any of the organization's prior five Forms 990

  - Identifies its former directors or trustees that received, in their capacity as former directors or trustees, more than $10,000 of reportable compensation on any of the organization's prior five Forms 990

[5] FIN 48 (Interpretation 48 of Financial Accounting Standard 109), effective for fiscal years beginning after December 15, 2006 (for nonpublic organizations, effective for fiscal years beginning after December 15, 2007), requires tax-exempt organizations to record a liability for income when there are uncertainties as to whether its income is exempt from income tax. Although the Form 990 does not refer to FIN 48 specifically, the disclosure requirements may alert the IRS to potentially unrelated business income.

- Audit committee
    - Assumes responsibility for oversight of the audit, review, or compilation of financial statements by an independent auditor and selection of an independent auditor
    - Ensures oversight of independent auditor
    - Presents financial statements to full board for review
    - Ensures compliance with any state law audit requirements imposed on charities

The following further best practices are specific to the type of organization (schools, hospitals, organizations providing grants or other assistance, and organizations issuing tax-exempt bonds).

Schools[6]:

Policy:

- Nondiscriminatory policy towards students included in charter, bylaws, other governing instrument, or in a resolution of its governing body
    - Policy included in all brochures, catalogues, and other written communications with the public dealing with student admissions, programs, and scholarships
    - Policy publicized through newspaper or broadcast media during the period of solicitation for students or during the registration period

School must maintain the following:

- Records indicating racial composition of the student body, faculty, and administrative staff
- Records documenting that scholarships and other financial assistance are rewarded on a racially nondiscriminatory basis

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[6] Per Code section 170(b)(1)(A)(ii), the term "school" includes any educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.

- Copies of all catalogues, brochures, announcements, and other written communications to the public dealing with student admissions, programs, and scholarships

- Copies of all materials used by the organization or on its behalf to solicit contributions

Hospitals

Written policies:

- Charity care policy
  - Describes how organization will provide charity care[7]
  - Provides free or discounted care to the "medically indigent"[8]
  - Ensures policy is applied consistently by affiliate organizations

- Debt collection policy
  - Contains provisions on the collection practices to be followed for patients who are known to qualify for charity care or financial assistance

Procedures:

- Prepares annual community benefit report that is available to the public
  - Describes the organization's programs and services that promote the health of the community or communities it serves

- Patient intake process informs and educates patients about their eligibility for assistance under federal, state, or local government programs, or under the hospital's charity care policy

Organizations Providing Grants and Other Assistance

- Maintains records to substantiate the amount of the grants or assistance, the grantees' eligibility for the grants or assistance, and the selection criteria used to award the grants or assistance

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[7] "Charity care" means free or discounted health services provided to persons who meet the organization's criteria for financial assistance and are thereby deemed unable to pay for all or a portion of the services. Charity care does not include bad debt write-offs.
[8] "Medically indigent" means persons whom the organization has determined are unable to pay some or all of their medical bills because the bills exceed a certain percentage of their family or household income or assets, even though they have income or assets that otherwise exceed the generally applicable eligibility requirements for free or discounted care under the organization's charity care policy.

- Maintains procedures for monitoring the use of grant funds

Organizations Issuing Tax-exempt Bonds[9]

- Management policies and procedures ensure the post-issuance compliance of its tax-exempt bond liabilities

- Books and records support the final allocation of proceeds

[9] Providing information about these policies and records will be optional for returns filed in 2009.