Internal Revenue Service
Tax-Exempt & Government Entities Division
Exempt Organizations

Background Paper
Redesigned Draft Form 990

The IRS has released for public comment a discussion draft of a redesigned Form 990, Return of Organizations Exempt from Income Tax, filed by many public charities and other exempt organizations. Links to the draft form, draft instructions, and IRS news release are contained at the end of this document. The discussion draft constitutes a significant redesign of the form, which has been revised only on a piecemeal basis since 1979. The IRS anticipates using the form for the 2008 tax year (returns filed in 2009). The proposed redesign does not affect the other forms in the IRS Form 990 series; however, through this process, we are requesting comments on filing thresholds with respect to some of these forms.

Questions concerning the redesigned form and instructions should be:

- e-mailed to the IRS at Form990Revision@irs.gov or
- mailed to the IRS at:
  Form 990 Redesign, SE:T:EO
  1111 Constitution Avenue, NW
  Washington, DC 20224.

Comments are due no later than September 14, 2007.

Current Users of the Form 990

The Form 990 is used by the IRS as the primary tax compliance tool for tax-exempt organizations. In addition, most states rely on the Form 990 to perform charitable and other regulatory oversight, and to satisfy state income tax filing requirements for organizations claiming exemption from state income tax. The Form 990 is a public document that is made available by filing organizations, the IRS, and others. It is the key transparency tool relied on by the public, state regulators, the media, researchers, and policymakers to obtain information about the tax-exempt sector and individual organizations.

Background and Sector Demographics of the Tax-Exempt Sector

Approximately 1.3 million public charities or other types of non-charitable exempt organizations are included in the IRS master file. This consists of public charities (not including churches), non-charitable tax-exempt organizations, and private foundations. For tax year 2004, the most recent year for which complete data is available, the IRS received 364,601 Forms 990 and 142,269 Forms 990-EZ, for a total of 506,870 returns. (Many small organizations did not have a filing requirement.)

The tax-exempt sector is diverse as to size and types of organizations and sources of revenues. Small organizations make up the largest percentage of the number of tax-exempt organizations, but they account for a relatively small percentage of the total assets and annual revenues of the exempt sector. For example, of all public charities that file annual returns with the IRS, the largest 1% of public charities holds 61% of the assets and derives 66% of the revenues.

This disproportionate allocation of assets and revenues across the various sizes of organizations, the large concentration of assets and revenues in the hospital and education sub-sectors, and the reliance on fee-for-service revenues and investment earnings to fund operations, are important considerations in designing an effective and efficient information reporting system.

Reasons for Redesign and Guiding Principles

Since the Form 990's last redesign in 1979, the tax-exempt sector has undergone tremendous growth and experienced significant change in virtually all aspects of operations.

The current Form 990 has not kept pace with changes in the sector and the law. Because of its history of ad hoc revisions, the current form neither adequately describes the filing organization nor provides a basis for comparing an organization with its peers. Some of the most common complaints regarding the current Form 990 include (1) the questions and instructions often are unclear; (2) some questions are not applicable to all organizations required to file the form; (3) many of the questions and parts are not arranged in a logical sequence; and (4) the form fails to provide a complete picture of the reporting organization.

The redesign of Form 990 is based on three guiding principles: enhancing transparency, promoting tax compliance, and minimizing the burden on the filing organization.

- Enhancing transparency means providing the IRS and its stakeholders with a realistic picture of the organization and its operations, along with the basis for comparing the organization to similar organizations.
- Promoting compliance means the form must accurately reflect the organization's operations and use of assets, so the IRS may efficiently assess the risk of noncompliance.
- Minimizing the burden on filing organizations means asking questions in a manner that makes it relatively easy to fill out the form, and that do not impose unwarranted additional recordkeeping or information gathering burdens to obtain and substantiate the reported information.

Summary of the Revised Core Form

The redesigned Form 990 consists of a 10-page core form, including a summary page at the beginning, to be completed by each Form 990 filer. In addition, an organization may be required, depending upon its type and activities, to complete one or more schedules.

Part I, the Summary page provides the organization's identifying information and a snapshot of the organization's key financial, compensation, governance, and operational information. By looking at the summary page, users will find a breakdown of the organization's revenues, expenses, assets, liabilities, and net assets, to quickly see the size and key financial measures of the organization. In addition, the summary page highlights certain items, such as the percentage of net assets currently expended in operations, and various fundraising measures, such as fundraising expenses as a percentage of the organization's total contributions or total expenses. Items reported in the Part I Summary are derived from information provided elsewhere in the form.

Part II of the core form requires the organization to report information about compensation of officers, directors, trustees, and certain other employees. As is the case with the current Form 990, an organization must list each officer, director, trustee, or key employee of the organization, regardless of compensation amount. The redesigned core departs from the current form, however, by requiring the reporting of compensation based on Form W-2 reporting for employees, and Form 1099 reporting for directors and other independent contractors. As is the case with the current form, compensation paid by related organizations must be reported separately. The core compensation form reduces the reporting burden for most organizations by asking for summary (a single W-2 or 1099 amount), rather than detailed, information about the various components of an individual's compensation. We estimate that less than 5% of filers will be required to complete Schedule J, Supplemental Compensation Information, to break down the reporting of an individual's executive compensation into multiple components, including regular wages and salary, incentive compensation, deferred compensation, fringe benefits and expense allowances or reimbursements.

Part III of the core form requires each organization to provide certain information regarding the composition of its board or governing body, certain of its governance and financial statement practices, and the means by which the organization is accountable to the public by making certain governance information publicly available. Good governance and accountability practices provide safeguards that the organization's assets will be used consistently with its exempt purposes, a critical tax compliance consideration, especially with respect to organizations that are subject to private benefit, excess benefit, and private inurement prohibitions. In our view and experience, a well managed organization is likely to be a tax compliant organization.

Parts IV, V, and VI of the core form generally follow the current form's layout for reporting of revenues, expenses, and balance sheet items. One proposed major change places all the required supplemental financial information from Parts I, VII and VIII of the 2006 Form 990 into a separate schedule (see Schedule D discussion, below) and eliminates exclusion codes. The redesigned financial statement reporting requires additional reporting of actual and contingent federal tax liabilities, and other amounts that are not necessarily reported on an organization's balance sheet (such as museum collections, conservation easements, and escrows held for the benefit of others).

Parts VII and VIII of the core form contain questions about the general activities of the organization and its compliance with various IRS filing requirements. Many of the questions in Part VII serve as "trigger" questions for the various schedules an organization might be required to complete, depending upon its type and activities. Part VIII requests information about the organization's employment tax, excise tax, unrelated business income tax, and other filing obligations.

Part IX of the core form requires information on the program service and exempt function activities of the organization, and asks the organization to describe its most significant accomplishment for the year.

Summary of Potentially Applicable Schedules

The redesigned form's 15 schedules are designed to require reporting of information only from those organizations that conduct particular activities. A list of the schedules is contained in Appendix A. Certain schedules, such as Schedules A and B, generally will be completed only by public charities, as is the case with the current form. Most of the remaining schedules will be completed by only a small percentage of the organizations filing the core form. Nearly every organization will be required to complete at least one portion of Schedule D, Supplemental Financial Statements, similar to what is required presently. Based on our estimates, only 3 of the 15 schedules will be completed by more than 25% of the filing organizations, with 8 of the schedules to be completed by less than 10% of all filing organizations.

Comparison to Current Form 990 (2006) and Guiding Principles

The current Form 990 (2006) consists of a 9-page core and Schedules A and B. It contains 36 possible attachments, most of which request additional financial information by each type of filing organization. The redesigned form contains a core form of 10 pages (including the one page summary), and 15 potential schedules.

The redesigned form enhances transparency by asking additional questions and presenting the information in an improved manner. The summary page provides the user with the snapshot of key information without having to go beyond the first page.

The redesigned form promotes tax compliance by requiring an array of identifying information, allowing the IRS to pinpoint organizations that have particular characteristics of concern without burdening other organizations who do not share these characteristics. Compliance is also promoted by asking focused questions in certain problematic areas the IRS has observed, such as problems in compensation and fundraising.

Minimizing burden on the filing organizations was a critical consideration in redesigning the form. At first glance, it would appear that the redesigned form is much longer than the current form, as a simple comparison of the number of questions, schedules and pages is deceiving. The structure of the redesigned form, and the thresholds that trigger completion of a schedule, operate to minimize the reporting burden for most organizations. As Appendix B indicates, most organizations will be filing, at best, a handful of schedules. In addition, the revision continues the move away from allowing unstructured material (e.g., PDF files) to be filed with the form. In the context of electronic filing, such material presents technological and cost difficulties and in any event results in non-searchable data.

Most organizations will not experience a material change in burden, while those with complicated compensation arrangements, related entity structures, and activities that raise compliance concerns, may see an increase in the effort associated with providing the information required by the redesigned Form 990.

Request for Comments by September 14, 2007

The IRS is providing a 90-day comment period regarding the discussion draft. Comments are due September 14, 2007, and should be e-mailed to the IRS at Form990Revision@irs.gov. The IRS hopes to have the form ready for the 2008 tax year (i.e., forms filed in 2009). In order to reach this deadline, it is critical that comments be received within the comment period.

Notwithstanding the aggressive schedule, the IRS recognizes that some parts of the form will need modification after we receive input. Certain revisions will require changes in regulations or other guidance. The IRS specifically requests comments and suggestions regarding:

- other ways to minimize the reporting for the sector and for individual organizations, including electronic filing concerns;
- raising the Form 990 filing thresholds for certain organizations. For example, raising the current $25,000 annual gross receipts threshold to $50,000, and allowing these organizations to file a Form 990-N (a new annual electronic information notice for small organizations with annual gross receipts under $25,000) in lieu of the Form 990 or 990-EZ;
- whether certain portions of the discussion draft Form 990 can be used as a substitute for the current Form 990-EZ;
- the efficiency indicators contained on the summary page (lines 19b, 24b, 25 and 26);
- additional items regarding governance and management best practices (Part III of the core form);
- the reporting of community benefit by hospitals in Schedule H, and the extent to which the Catholic Health Association's reporting format on which Schedule H is largely based should be modified;
- defining relatedness for compensation and other purposes, including arrangements in joint ventures and with for-profit subsidiaries;
- whether transition periods are necessary in order to ease the burden of implementing the new reporting requirements for certain form components (such as the tax exempt bond schedule);
- whether adequate care has been given to privacy concerns; and
- whether the IRS should preclude group returns.