

IRS Form 990 Updates: How Much More Will Your Organization Need to Disclose about Compensation in 2009?

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November 12, 2008

■ Agenda

- **Overview and Timeline of Changes**
- **History and Backdrop**
- **Structural Changes**
- **New Governance Provisions (Part VI)**
- **New Compensation Disclosures (Part VII)**
- **Schedule J**
- **Implementation and Effective Dates**
- **What should you do now?**

■ Overview and Timeline of Changes

- Form 990
 - Informational return for tax exempts
 - Reports income, expenses, assets, liabilities and other information
 - Most states rely on the forms for oversight
 - Only “publicly” available information for media, research, potential donors
- 2008 overhaul is first major revision to Form 990 since 1979
 - Enhances transparency
 - » Realistic picture of exempt organization
 - » Basis for comparing the organization to similar organizations
 - Promotes tax compliance
 - » Staying within exempt purpose
 - » Appropriate use of assets
 - Minimizes burden on filing organizations (?)
- Proposed Rules Issued in June, 2007
 - Parallels SEC’s transparency goals for public company compensation disclosure
- Final Rules Communicated December, 2007
- Effective for 2008 Tax Year
 - Decisions and payments made now subject to new reporting rules

History and Backdrop

- **Congress enacts IRC 4958 in 1996 (Final Regs in 2002): Intermediate sanction on excess benefit transactions**
 - “Disqualified person” receives an improper personal gain from the exempt organization
 - Three-part compensation test:
 - » Independent governing body
 - » Reliance on comparable data
 - » Adequate documentation
 - Results in excise tax against individual (25-200%) and organization manager (10%)
 - Service cannot revoke tax exempt status

History and Backdrop (con'd)

- **Executive Compensation Compliance Initiative implemented by IRS in 2004, with results published in 2007**
 - Many organizations confused and did not understand instructions
 - Significant errors and omissions in compensation reporting
 - \$21 million in excise taxes assessed for excess benefit transactions
 - » Excessive salary and incentive compensation
 - » Unreported payments for vacation homes, personal legal fees, or personal auto
 - » Unreported payments for personal meals and gifts to others on behalf of the disqualified person
 - » Payments to an officer's for-profit corporation in excess of the value of services provided to the corporation
 - » Loans with favorable rates or total forgiveness

■ History and Backdrop (con'd)

- **Government Accountability Office and Senate Finance Committee**
- **Scandals and news in tax-exempt community**
 - CareFirst BCBS
 - United Way of Central Carolinas
 - Smithsonian Institution
 - University of California
- **SEC revamped executive compensation disclosure of public companies in 2006**
- **Sarbanes-Oxley**
- **Bailout legislation**

■ Structural Changes

■ Old Form

- 9 pages, 2 schedules, 36 potential attachments
- Compensation: Compensation paid, benefits, expense accounts

■ New Form

- **“Core Form”** – for all organizations
 - » Part I: Summary
 - Allows the organization to tell its story up front, with a snapshot of financial, governance and operations information, including a 2-year comparison of key financial data
 - » Part II: Signature Block
 - » Part III: Statement of Program Service Accomplishments
 - » Part IV: Checklist of Required Schedules
 - » Part V: Statements Regarding Other IRS Filings and Tax Compliance
 - » **Part VI: Governance, Management and Disclosure**
 - » **Part VII: Compensation to Officers, Directors, Trustees, Key Employees, HCEs and ICs**
 - » Part VIII Statement of Revenue
 - » Part IX: Statement of Functional Expenses
 - » Part X: Balance Sheet
 - » Part XI: Financial Statements and Reporting

▪ Structural Changes (con'd)

- **16 Schedules** – As appropriate
 - » Schedule A: Public Charity Status and Public Support
 - » Schedule B: Schedule of Contributors (no change)
 - » Schedule C: Political Campaign and Lobbying Activities
 - » Schedule D: Supplemental Financial Statements
 - » Schedule F: State of Activities outside of U.S.
 - » Schedule E: Schools
 - » Schedule G: Supplemental Information Regarding Fundraising or Gaming Activities
 - » Schedule H: Hospitals
 - » Schedule I: Grants and Other Assistance to Organizations, Governments and Individuals in the U.S.
 - » **Schedule J: Compensation Information**
 - » Schedule K: Supplemental Information on Tax Exempt Bonds
 - » Schedule L: Transactions with Interested Persons
 - » Schedule M: Non-Cash Contributions
 - » Schedule N: Liquidation, Termination, Dissolution or Significant Disposition of Assets
 - » Schedule O: Supplemental Information to Form 990
 - » Schedule R: Related Organizations and Unrelated Partnerships

■ New Governance Provisions (Part VI)

- **IRC cannot require governance, management or disclosure policies**
 - But absence of policies could lead to opportunities for excess benefit transactions
- **Three Sections**
 - Governing body and management
 - Disclosure
 - Policies
 - » Compensation-setting process: Disclose if the company has a process for determining compensation that includes:
 - Review and approval of a governing body or compensation committee (that excludes interested parties)
 - Use of data as to comparable compensation for similarly qualified persons in functionally comparable positions at similarly situated organizations, and
 - Contemporaneous documentation and recordkeeping for decisions
 - » Process question applies to CEO, Executive Director, top management, or other officers or key employees
 - » If yes, provide description of the process and dates of process in Schedule O

■ New Compensation Disclosures (Part VII)

- **Must populate chart that includes:**
 - Name and title
 - Average hours per week
 - Positions
 - Reportable compensation from the organization
 - Reportable compensation from related organizations
 - “Other” compensation
- **The following positions must be included:**
 - Current “**officers**”, directors, trustees and “**key employees**”
 - Current top five “**HCEs**” (other than above) > \$100,000 in compensation
 - Former officers, key employees and HCEs who received current compensation of > \$100,000
 - Former directors or trustees who receive current compensation of > \$10,000

New Compensation Disclosures (Part VII) (con'd)

▪ **Officer**

- Manager of daily operations, such as president, VP, secretary, treasurer, top financial officer and top management officer.

▪ **Key Employee – must meet 3-part test:**

- \$150,000 Test: Reportable compensation > \$150,000
- Responsibility Test:
 - » Has responsibility over organization as a whole
 - » Manages a discrete segment that represents 10% of organization, or
 - » Has authority to control or determine 10% of budget
- Top 20 Test: Is one of the 20 employees with highest reportable compensation for the organization and related organizations

New Compensation Disclosures (Part VII) (con'd)

- **What compensation is being reported?**
 - W-2 and 1099
 - Other compensation
 - » Employer contributions to qualified DC plan
 - » Annual increase in actuarial value of qualified pension plan (whether or not funded or vested)
 - » Value of health benefits
 - » Tax-deferred contributions by the employer and employee to non-qualified defined contribution plan (whether or not funded or vested or subject to SRF)
 - » Annual increase in actuarial value of a non-qualified pension plan (whether or not funded or vested or subject to SRF)
 - » \$10,000 exception

New Compensation Disclosures (Part VII) (con't)

- **Independent Contractors have a separate table**
 - Must provide name and business address, description of services, compensation for the five most highly paid independent contractors that received > \$100,000 of compensation from the organization
 - Must also provide total number of ICs who receive more than \$100,000 in compensation from the organization

■ What Triggers Schedule J?

- Former officers, key employees, or HCEs who received current compensation > \$100,000
- Former directors who received current compensation > \$10,000
- Anyone listed whose reportable compensation + other compensation > \$150,000
 - **All key employees**
 - **Current directors, officers if total compensation > \$150,000**
 - **Current HCEs if total compensation > \$150,000**

Schedule J Disclosure – All reported individuals in Core Form (except ICs)

- **Perquisite disclosure**
 - First class or charter travel
 - Companion travel
 - Tax indemnification and gross ups
 - Discretionary spending accounts
 - Housing allowances
 - Payments for business use of personal residence
 - Health or social club dues
 - Personal services (maid, chauffeur, chef)
- **Written policies and substantiation**
- **Compensation process and arrangements**
 - Compensation committee
 - Independent Compensation Consultant
 - Form 990s
 - Written employment agreements
 - Surveys
 - Approval of Board or compensation committee
- **Termination payment disclosure**
 - Severance or CIC
 - SERP payouts
 - Equity benefits
- **Compensation contingent on the organization's revenue or net earnings**

Schedule J Disclosure – “Triggering Individuals” only

Detailed Quantification in Tabular Format on Schedule J

Name	Base	Bonus & Incentive Compensation	Other Compensation	Deferred Compensation	Nontaxable Benefits	Total	Prior Form 990 Compensation
Executive A							
Executive B							
Executive C							
Executive D							

■ Implementation and Effective Dates

- **Revised Form 990 for 2008 tax year**
- **3-Year Transition Rule for smaller exempt organizations that use Form 990-EZ**
 - 2008 tax year:
 - » Gross receipts between \$25,000 and \$1M, and
 - » Total assets at year end less than \$2.5M
 - 2009 tax year:
 - » Gross receipts between \$25,000 and \$500,000, and
 - » Total assets less than \$1.5M
 - 2010 and later:
 - » Gross receipts between \$50,000 and \$200,000 and
 - » Total assets less than \$500,000
- **Form 990-N**
 - Companies with gross receipts less than \$25,000
 - Postcard identifies organization and indicates justification for not filing a return

▪ Checklist for Initial Filing

- **Create a mock-up of Core Form and Schedule J**
- **Identify other potential Schedules**
- **Strengthen the Board's processes**
- **Identify officers, directors, trustees and potential key employees and top 5 highest compensated employees**
- **Educate them as to the breadth of disclosure**
- **Review perquisites and perquisite policies**
- **Review CIC and severance arrangements**
- **Review the governance questions**
- **Answer "why"**