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NONPROFIT ORGANIZATIONS COMMITTEE

September 14, 2007

Submitted by E-mail to [Form990Revision@irs.gov](mailto:Form990Revision@irs.gov)

Form 990 Redesign  
Internal Revenue Service, ATTN: SE:T:EO  
1111 Constitution Avenue, N.W.  
Washington, DC 20224

Dear Form 990 Redesign Staff:

I write on behalf of the Nonprofit Organizations Committee of the Association of Corporate Counsel. The Association of Corporate Counsel (ACC) was formed in 1982 as the professional bar association for in-house counsel, and today has almost 22,000 members worldwide. One of the primary missions of ACC is to act as the voice of the in-house bar on matters of concern in corporate legal practice. The Nonprofit Organizations Committee of ACC has over 1100 members who practice as in-house and general counsel to nonprofit organizations, primarily 501(c)(3) organizations, including both charities and private foundations, and 501(c)(6) organizations.

As in-house counsel to the tax-exempt sector, it falls to our membership to put into practice "on the ground" the laws, regulations, and other compliance procedures required by the Service. Given our intimate perspective on nonprofit operations, we believe we bring an important point of view to the debate on the proposed Form 990.

While our membership has many detailed comments on individual line items, we have chosen to comment only on four overarching issues that reflect widely-shared concerns of our membership:

I. Misleading Nature of Summary Section on First Page

The new form requires on the front page a summary of the organization's activities, governance, revenues, expenses and fundraising activities. This is evidently intended to provide a "snapshot" of the organization for the general public. However, by including items in the summary, the Service is placing its official imprimatur on the judgment that these are the most important aspects to consider about a nonprofit. The public, most of whom do not have significant background in assessing tax-exempt organizations, is likely to take the Service's word for it.

We have grave misgivings about this approach. The information in the summary, by necessity given limited space, is presented without context or established metrics to help the user comprehend it. Further, in some cases, terminology that sounds negative is used to describe appropriate behavior. For these reasons, the summary is highly susceptible to being misunderstood or misinterpreted, and thus prejudicial to the reporting organizations.

Specifically, the various percentages to be calculated are provided without context. While it is true that some of these ratios are used by some charity evaluation groups, those groups set standards that explain their views of appropriate ranges for these ratios. Without that context, the public will likely draw the conclusion that lower is always better for management and fundraising costs – why else would the Service be drawing their attention to these figures? But it is well established that nonprofit organizations with inadequately funded management are frequently ineffective, while those with very low fundraising costs are simply underreporting. Moreover, the ratio of key employee compensation to total program expenses is not even used by the major charity evaluation groups and thus is a metric with no context even for those well-versed in the nonprofit sector.

Similarly, the number of board members is not an established metric for high-performing nonprofits. While large boards were once preferred, now the trend is toward smaller boards. Organizations will have widely differing answers to this question depending on their governance structure (membership, chapter-based, self-perpetuating board), and it has not been established that those differences are correlated to their effectiveness. Also, organizations have different approaches to having related parties on their board – medical facilities often have physicians, religious charities have ministers. The Better Business Bureaus Wise Giving Alliance standards recognize this and allow up to 10% compensated board members. Without such context, the public may draw an unwarranted negative inference.

The focus on compensation is also misleading. No context is given for whether salaries over \$100,000 are unreasonable under the Service's own "intermediate sanctions" test or are appropriate given the location of the organization's offices. Further, the highest compensation amount often includes severance pay, a retirement bonus, or deferred compensation and is not reflective of the organization's overall compensation system. A more detailed picture of the organization's compensation is provided on the very next page (although even that page lacks accuracy given the double-counting of deferred compensation)– it is inappropriate to single out a potentially misleading figure on the first page.

Finally, the form's use of standard tax terminology may unintentionally cast aspersions on perfectly legitimate activity. As to unrelated business income, the words "unrelated" and "business" wrongly suggest to readers that the organization is engaging in something inappropriate. A similar example is "gaming" – a word that sounds racy, with vaguely criminal overtones. Yet the picture evoked by a Bingo game at the neighborhood senior center is completely different. Including these activities in the summary may in itself have an inflammatory effect, without adding much to the understanding of the reporting organization, as these activities are often a relatively minor part of an organization's total operations.

Nonprofit organizations cover a huge breadth and range in their variety, and a meaningful summary of the complex information in the Form 990 may not be possible. It is also not necessary. The form itself provides a wealth of information to the interested reader, and other groups provide comparative data on nonprofits in different formats that will serve the needs of different audiences. At the very least, the form should allow for the organization to provide written explanations of the summary items, to help address the misleading impressions that otherwise may occur.

## II. Implied Establishment of "One Size Fits All" Governance Practices

Part III of the proposed revised 990 deals with governance. The IRS is in a uniquely complicated position to pursue governance matters through the 990. On one hand, the 990 is an enforcement vehicle by which the IRS and state charity officials gather information to use in making decisions to pursue more information or initiate an audit. As IRS officials have said, standards of governance can reflect on an organization's standards of compliance. On the other hand, the 990 can be a useful tool for educating – albeit somewhat forcefully – the sector and the public about the importance of certain governance policies, practices, and standards. Unfortunately, even the best of intentions can have the potential of opening the door to unintended consequences, including infringing on matters best left to the states, undermining the ability of private individuals and organizations to exercise business judgment in the fullest light of applicable circumstances, and imposing on the sector a "one size fits all" view of governance practices.

Traditionally, matters of corporate and entity governance have been within the purview of the states and subject to enforcement by state corporate and charity officials. It certainly seems to be appropriate for the IRS to inquire through the 990 about the presence of certain policies and procedures through which tax exempt organizations can more readily ensure compliance with applicable federal laws. For instance, the existence and application of a conflicts of interest policy can simultaneously and with consistency facilitate compliance with the state-based duty of loyalty and federal-based prohibitions against self-dealing and excess benefit. Similarly, inquiring about the presence and application of whistleblower and document retention policies, which are arguably federal law mandates, or about financial controls can serve legitimate enforcement purposes and educational opportunities.

Some contend that only asking about the presence and general application of such policies does not go far enough to evidence compliance and that it will be too easy for organizations and the people who run them to concoct minimalist compliance protocols. Pursuing such depth through the 990, however, risks embarking on a slippery slope of trampling on matters of state authority. Moreover, the downsides of using the 990 to probe more deeply into governance matters outweigh the potential for catching those with a "race to the bottom" mindset.

Using the 990 to inquire more deeply, for instance about the size of the governing body, the number of independent members of that body, or (even more problematically) specific numbers of conflict of interest transactions reviewed, can inadvertently present an aura of the

IRS appearing to pass a judgment— either good or bad but in either event without full information -- that the press and public may unfairly and inaccurately extrapolate from the fact of the questions being asked and answers being given without adequate context. Moreover, inquiring too deeply about conflict of interest transactions could have an unintended and unfortunate “chilling effect” in that organizations might implement narrow policies bounded by rigid legal parameters. Under such legalistic policies, organizations might forgo considering the implications of potential transactions not contemplated by narrow constraints, such as the appearances of conflict when a legal conflict does not exist. Such a result can actually undermine the very transparency and accountability that the 990, and Part III in particular, are pursuing.

The depth of inquiry into governance matters through the 990 can expose implicit “one size fits all” expectations that might be blindly pursued in an effort to comply with what people may interpret to be IRS expectations thereby displacing more thoughtful, appropriate, and effective decision-making at individual board and management level. The diversity of the sector in size, mission, operations, and otherwise – including approaches to governance -- contributes to its effectiveness. Uniform governance expectations from government, whether explicit or implicit, will threaten that effectiveness more than does the relatively low rate of law breaking from within the sector.

### III. Arbitrary Reporting of Compensation of All Employees with Salaries of \$100,000

The form requires disclosure of the individuals with annual compensation above an arbitrary ceiling of \$100,000. The Committee believes that, given the vast diversity in size and revenue of nonprofit organizations, the selection of a single threshold will yield confusing information on large organizations and misleading information on small organizations. A single threshold also does not allow for the large disparity in salary levels between major urban areas and smaller cities and rural areas, nor does it recognize the difference in skills required and the marketplace demand for, say, a traditionally low-paid preschool teacher and a biomedical researcher. The Committee would recommend consideration of a sliding scale pegged to the organization’s total budget, a higher figure that would limit reporting to fewer staff, or similar alternative. Further, whatever number is chosen should be adjusted regularly for inflation, or it will soon be even more over-inclusive.

### IV. Need for Delay of Implementation

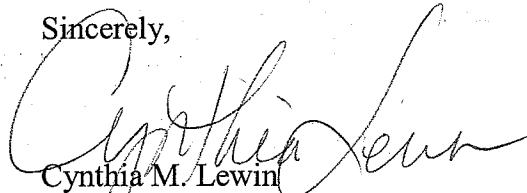
The draft Form 990 requires a massive amount of new information and recordkeeping. For example, significant new reporting is required in Parts II and V (requiring compensation reporting for two different periods), Part IX (matching direct program revenues with program expenses, which is not required for financial statement purposes), Schedule G (fundraising), Schedule I (grants), Schedule K (tax-exempt bonds), and Schedule M (non-cash contributions). Major accounting firms are advising our organizations that the new Form 990 will cost more to prepare than the current form, another indicator that the form involves added complexity.

For compliance, calendar year organizations would need to have procedures in place to begin collecting this information by December 31, 2007 – less than four months away. This would be difficult even if the final form was available today. The volume of comments and the careful attention the Service is devoting to those comments will further impede the release of the new form in time for organizations to have sufficient time to prepare for meaningful compliance.

We urge the Service to delay implementation of the new Form 990 or at least the various schedules until 2009 (assuming that a final form can be completed and released to the public well before January 1, 2009). To do otherwise risks unfairly burdening the nonprofit community, most of whose members are understaffed, underfunded, and least able to handle it.

We applaud the Service for its significant efforts in reshaping the Form 990, a valuable undertaking. We also applaud its openness to public comment on this important process and for its outreach to the public through phone seminars, speaking engagements, and publications. Thank you for your consideration of these comments.

Sincerely,



Cynthia M. Lewin  
Chair, Nonprofit Organizations Committee  
Association of Corporate Counsel