

IRS Form 990

Preparing For The New Reporting Requirements

Douglas J. McGregor |

Stephen J. Doneski |



Agenda

1. Schedule G
2. Schedule K
3. Schedule L

Visit us: www.fdcpa.com Call us: 888.875.9770



Focus on: Schedule G – Supplemental Information Regarding Fundraisers or Gaming Activities

- **Part I – Fundraising Activities**
 - Relationships with professional fundraisers
 - Identify states where registered or licensed
- **Part II – Events**
 - Report events with gross receipts greater than \$5,000
 - Revenues, donations and expenses
 - Individual contribution amounts (*notify donor of amounts over \$250*)
 - Reporting of dollar value of goods and services (*dollar value of goods received*)
- **Part III – Gaming**
 - Revenues and expenses by game
 - Gaming activities information

Focus on: Schedule K – Tax-Exempt Bonds

- New Schedule K requires significantly more detail than current Form 990
- Phase in: 2008 form requires only identifying information about bond issues (Part I). All other parts (Parts II – IV) are optional for 2008 and required for 2009.
- Reporting required only for bonds issued after 2002
- Reporting on bonds outstanding at the last day of the year <\$100,000

Focus on: Schedule K – Tax-Exempt Bonds

- **Reporting required in four areas:**
 - General information (issuer name, date, purpose, etc.)
 - Specific uses of proceeds of each issue (proceeds used for capital expenditures, reserve fund, costs of issuance, etc.)
 - Private use:
 - Was property financed by the issue subject to certain types of private use (leases, management or service contracts, research agreements, etc.)?
 - Percentage of bond-financed property subject to private use, broken down between unrelated business taxable income (UBTI) and other types of private use
 - Arbitrage-related matters (guaranteed investment contracts, swaps, rebate compliance)
- **Private use questions will require looking beyond bond transaction or other basic records:**
 - Review uses of property financed or refinanced by post-2002 bond issues and calculate percentage of each issue subject to private use

Focus on: Schedule K – Tax-Exempt Bonds

- Did the organization have a tax-exempt bond issue with an outstanding principal amount of more than \$100,000 as of the last day of the year, and that was issued after December 31, 2002? If “Yes,” answer 24b-24d and complete Schedule K. If “No,” go to question 25.
- Did the organization invest any proceeds of tax-exempt bonds beyond a temporary period exception?
- Did the organization maintain an escrow account other than a refunding escrow at any time during the year to defease any tax-exempt bonds?
- Did the organization act as an “on behalf of” issuer for bonds outstanding at any time during the year?

Visit us: www.fdcpa.com Call us: 888.875.9770



Focus on: Schedule K – Tax-Exempt Bonds

- Tax definition of “issue.” As bond attorneys know, a single “issue” can be composed of bonds covered in multiple Form 8038s and issued over a long period of time.⁴ A single issue for tax purposes can also be only a portion of a large concurrent issuance.⁵ As a result of this legal complexity, the reporting nonprofit should make sure it reviews its files and consistently identifies the separate tax issues.
- Issue Date. A filing entity must know if any bonds have been “reissued.” Did, for example, the conversion of an issue from auction rate securities trigger a reissuance? If so, and the reissuance date was after December 31, 2002, an issue nominally dating from before 2003 must be reported on.
- “On behalf of” — 24d. This question requires an affirmative answer by Rev. Rul. 63-20 corporations and other “on behalf of” issuers filing Form 990. Issues may be reported

Schedule K – Identifying Information

- Effective for 2008
- Most information can be found on Form 8038
- Must report a bond issue if issued after 12/31/2002 and more than \$100,000 remains outstanding

Schedule K – Part I

Part I Bond Issues Planned for 2009							
Bond issue date	Bond issue type	Bond issue #	Bond issue amount	Bond issue price	Description of purpose	On behalf of issuer	On behalf of borrower
A							
B							
C							
D							
E							

- “Description of Purpose”: If there are multiple purposes, each should be set forth, unless separate purposes relate to a single project, in which case they should be aggregated. It is recommended that bond counsel be contacted on this point. Clearly if the contemporaneous tax documents at the time of issue identified separate purposes, that categorization should be followed on Schedule K. Even if not, it may be desirable to have a more specific breakdown here in view of the calculations and other requirements imposed later in Schedule K — some of which are levied purpose by purpose.
- “On behalf of” issuer: According to the instructions for Schedule K, if the filing entity was such an issuer, then this question should be noted as “yes.” If the filing entity was only the borrower of proceeds, then the answer should be noted as “no.”

Schedule K – Part II

	A	B	C	D	E					
1 Total proceeds of issue										
2 Gross proceeds in various forms										
3 Proceeds in refunding or defeasance escrows										
4 Other unearned proceeds										
5 Revenue credit from proceeds										
6 Working capital expenditures from proceeds										
7 Federal expenditures from proceeds										
8 Total of individual categories										
9 Were the bonds issued as part of a current refunding issue?	Yes	No	Yes	No	Yes	No	Yes	No	Yes	No
10 Were the bonds issued as part of an advance refunding issue?										
11 Has the final allocation of proceeds been made?										
12 Does the organization maintain adequate books and records to support the final allocation of proceeds?										

- For each issue there must be breakdown of the use of proceeds. Since the general instructions to Form 990 define “proceeds” to include investment proceeds, logically the sum of the answers 2 through 7 for each issue should equal the amount listed for the answer to question 1. However, the Instructions for question 3, regarding refunding of defeasance escrows, speak about the amount “deposited” into such an escrow.⁷ Under normal usage this ignores investment earnings. Since the defined term “proceeds” used in question 1 of Part II does not so exclude that subcategory, in many instances the total of lines 2 through 7 will not balance back to line one. It is suggested that in such a situation the discrepancy be noted and the difference explained. In addition, note that this breakdown of proceeds in Part II will usually *not match the numbers* in the issue’s Form 8038 since that form does not include *any investment earnings*.
- Final allocations should be made within five years and adequate books and records should be maintained supporting such allocation. Filing entities should be aware that answering these questions inappropriately may trigger an audit.

Schedule K – Part III

The image shows a portion of the Schedule K-1, Part III, Private Business Use (Continued) table. The table has 7 rows of questions and 10 columns for Yes/No answers. The questions are:

	A		B		C		D		E	
	Yes	No	Yes	No	Yes	No	Yes	No	Yes	No
2e. Are there any management or service contracts with respect to the financed property which may result in private business use?										
2f. Are there any research agreements with respect to the financed property which may result in private business use?										
3. Does the organization routinely engage board counsel or other outside counsel to review any management or service contracts or research agreements relating to the financed property?										
4. Enter the percentage of financed property used in a private business use by another party than a section 501(c)(3) organization or a state or local government.		%		%		%		%		%
5. Enter the percentage of financed property used in a private business use as a result of unrelated trade or business activity carried on by your organization, another section 501(c)(3) organization, or a state or local government.		%		%		%		%		%
6. Total of lines 4 and 5.		%		%		%		%		%
7. Has the organization adopted management practices and procedures to ensure the proper maintenance and use of its tax-exempt bond facilities?										

- This section includes the most detailed questions on new Schedule K. First, all such questions relate to the “property financed by the issue.” It is vitally important for the filing entity to remember this concept. The questions do *not* relate to the entire assets of the organization, or even all the assets financed by all its bonds. The questions relate only to the assets financed by the particular issue. Second, absent any clear determination otherwise with advice of counsel, the answers to these questions should be consistent with the position taken by an organization’s bond or tax counsel upon issuance.
- The questions on leases and other private uses of the bond-financed property arise from the limitations on such uses to the extent they do not fall into a permitted exclusion. The filing entity is asked to state if there are any such items extant that “may” result in private business use. If such a contract exists at all, a “yes” answer is to be given even if the corporation has determined that the contract fits an exception, meets a safe harbor or is otherwise not a problem for the issue.⁸

Visit us: www.fdcpa.com Call us: 888.875.9770

- Question 4 seeks the average percentage during the year for aggregate private business use for each issue. In determining this percentage, leases, management or service contracts or research agreements that do fit the public use exemption or the relevant safe harbors are disregarded. If this number on any issue is above 5%, the filing entity should expect to be contacted by the Service. Then question 5 seeks a percentage of unrelated trade or business use by 501(c)(3) corporations (including the filer) or governmental units.

Schedule K – Part IV

	A	B	C	D	E	F	G	H	I	J	K	L
1. Has a Form 8038-T, Arbitrage Rebate, Yield Reduction and Results in Case of Arbitrage Prohibits, been filed with respect to the bond issue?												
2. Is the bond issue a variable rate issue?												
3a. Has the organization or governmental issuer identified a hedge with respect to the bond issue on its books and records?												
3b. Name of provider												
3c. Term of hedge												
3d. Were gross proceeds invested in a GIC?												
3e. Name of provider												
3f. Term of GIC												
4. Were the regulatory safe harbor for establishing the fair market value of the GIC satisfied?												
5. Were any gross proceeds invested beyond an available temporary period?												
6. Did the bond issue qualify for an exception to rebate?												

- This section focuses on arbitrage — whether the issue is a variable issue, whether the rebate form has been filed (8038-T), whether there is a hedge (and if so, the term and the provider thereof) and whether there was or is a guaranteed investment contract (and if so, the name and term of the provider and term thereof). The answers to these questions may change from year to year as investments are made. Note that an affirmative answer to question 5 will need to be discussed with counsel to make sure no other actions (such as yield reduction payments) are required.

Schedule K – Part IV

- Refunding issues need to be segregated into issues that refund bonds issued before 2003 or after December 31, 2002. If bonds being refunded were issued before 2003, then Part III of Schedule K does not need to be completed with respect to the refunding bonds or the bonds being refunded. However, if the bonds being refunded were issued in 2003 or later, then the answers to Part III must be provided. Logically these rules also apply for issues that refund a series of prior refunding issues, with the key question being whether the original issue was on or before December 31, 2002.
- If you are tasked with answering the questions to Part III with respect to a refunding issue, the analysis concerning the appropriate business use and other percentage questions will have to come from the project (or projects) that were financed by the prior issues. This can be an incredibly detailed analysis. Once again the necessity for identification of the “issuance date” of an issue is notably important and therefore, as mentioned above, the concept of “reissuance” and its relevance to the legal analysis is heightened.

Schedule K – Final Thoughts

- It seems certain the IRS has put questions on Schedule K in part to identify potential audit targets and the filing entity should, absent a definite reason for other action, desire to treat its answers on Schedule K in the same manner as originally determined by its bond or tax counsel. Consistency with the determinations made upon issuance should be a strongly pursued goal. Great care should also be taken in identifying separate issues to report on. The purpose of each issue and the particular bond-financed property associated with each issue should be isolated for recordkeeping purposes. The “issue date” of each issue will become very important and each organization needs to make sure that any revisions to outstanding issues or other actions did not cause a “reissuance,” triggering a new issue date for that issue.

- Use of Financed Property
 - Measure private uses
 - Need to associate the bond-financed cost with the asset
 - If the asset is used for both exempt and private uses, need to determine the amount of private use of the asset
 - Time-based
 - Revenue- based
 - Determine the aggregate amount of bond proceeds from the specific issue allocable to private use

- Arbitrage and rebate
 - Optional for 2008
 - Form 8038-T (rebate)
 - Information regarding hedges/swaps
 - Information regarding guaranteed investment contracts
 - Investment beyond temporary period
 - Exceptions to rebate
 - Uses information developed in Step Two –
 - Investments and Step Two – Expenditures

- Common types of private use
 - Leases
 - Includes time share arrangements
 - Includes short term uses, such as day use of a conference facility
 - Contracts where a third party provides services to the borrower
 - Management contracts for a specific function or area, such as food service
 - Medical director contracts

- Common types of private use
 - Contracts where a third party uses the borrower's bond-financed property to provide services to others
 - Physician arrangements where the physicians directly bill the patient
 - Outsourcing of a function, such as pharmacy
 - Unrelated trade or business use
 - Lab testing
 - Support services to taxable affiliates or unrelated third parties

- Safe Harbors Overview – Rev. Proc. 97-13
 - Remember, these safe harbors do not apply to leases, only to management and services contracts
 - In general, the more the compensation is fixed, the longer the contract can be
 - Some safe harbors require early termination rights
 - Must be without penalty
 - Can be an issue if the service provider is supplying upfront capital or equipment

- **Schedule L consolidates reporting of transactions with “interested persons” (officers, trustees, key and highly compensated employees, substantial contributors):**
 - Loans to and from interested persons
 - Grants or assistance benefiting interested persons
 - Business transaction involving interested persons
 - “Excess benefit transactions”: paying more than fair market value or reasonable compensation
- **Not required to disclose substantial contributor’s name**
- **Reporting thresholds**
 - All excess benefit transactions must be reported
 - Business transactions >\$10,000 or 1% of revenues
 - Aggregated business transactions >\$100,000

Focus on: Schedule L – Transactions with Interested Persons

- Part I – Excess Benefit Transactions
- Part II – Loans To and From Interested Persons
- Part III – Grants or Other Assistance Benefiting Interested Persons
- Part IV – Business Transactions Involving Interested Persons

- **Form 990 Resources**

- www.fdcpa.com/tax/0808taxnews-form-990.htm
- www.irs.gov/charities
- www.990forhospitals.org
- www.charities.ago.state.ma.us/
- www.guidestar.org

- Questions
- Comments
- Discussion