

WAATP – CPE

CHAPTER MEETING

JUNE 18, 2024

*Preparing Forms 990 & 990-T
For Tax Exempt Organizations*

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Preparing Form 990 for Tax Exempt Organizations

Public Inspection

Every exempt organization must make available for public inspection

- A. Application for recognition of exemption (along with all supporting documents and communications with the IRS)
- B. Each annual information return available for a period of three years beginning on the date the return is required to be filed with all information the organization reports on or with its Form 990, including schedules and attachments, except for information regarding the identity of donors on Schedule B
- C. Provide a copy without charge, other than a reasonable fee for reproduction and actual postage costs, of all or any part of any application or return required to be made available for public inspection to any individual who makes a request for such copy in person or in writing.
 - Currently reasonable copy fee is \$0.20/page

Tax-Exempt vs Nonprofit

Nonprofit (State Law) DOES NOT EQUAL Tax-Exempt (Federal Law)

Tax Exempt Status

- A. “Section 501 (c) organizations other than those described in Sections 501(c)(3), 501(c) (9), and 509(c)(17) are not required to obtain recognition from the Service of their tax-exempt status, ***these organizations qualify for exemption, if they meet the requirements of the Internal Revenue Code***”
[SCA 200046038]
- B. An organization formed as nonprofit will qualify to be tax-exempt by **conforming its activities** to one or more sections within Internal Revenue Code section 501(a) or 501(c)
- C. There are **34** different sections of code that describe activity qualifying for tax exemption – and the organization needs to meet **at least one** of these
 1. Most are between 501(c)(1) and 501(c)(28)
 2. Plus 501(d), 501(e), 501(f), 501(k), 501(n), 521 and 527



- D. There are also prohibited or restricted activities that could result in the loss of tax- exempt status if engaged in, for example:
1. Private inurement
 2. Political activity (depending)
 3. Illegal activities
- E. For example, most tax-exempt organizations qualify under IRC 501(c)(3) - which are organized and operated exclusively for purposes that are:
1. Religious
 2. Charitable
 3. Scientific
 4. Testing for public safety
 5. Literary, or educational purposes, or
 6. To foster national or international amateur sports competition, or
 7. For the prevention of cruelty to children or animals
- F. This lists the things that the organization must do and further the things that the organization must NOT do
1. No part of the net earnings of which inures to the benefit of any private shareholder or individual
 2. No substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and
 3. Which does not participate in or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office

Who Must File

- A. All tax-exempt organizations need to file one of:
1. Form 990
 2. Form 990-EZ
 3. Form 990-N based on 3-year average annual gross receipts
- B. **Unless they are exempt from filing or are required to file a different form**
- E.g: Form 990-PF, Form 990-BL, Form 1065 or Form 5500

Form 990, 990-EZ and 990-N

Gross Receipts determine of which form must be filed and whether any other forms could be filed instead.

- An organization with:



1. **Gross receipts \leq \$50,000 and assets \leq \$250,000** may file Form 990-N
 - a) Unless prohibited, OR
 - b) Choses to file a complete Form 990-EZ or Form 990, or is required to file a different form (990-PF, 990-BL, 1065 or 5500), OR
 - c) Has no filing required (e.g., a church)
2. **Gross receipts $>$ \$50,000 but less than \$200,00 AND assets \leq \$500,000** file Form 990-EZ or choose to file a complete Form 990
3. **Gross receipts \geq \$200,000 and/or assets $>$ \$500,000** must file Form 990

Due Date

- A. Fiscal year organization returns are due on the 15th day of the 5th month following the end of the fiscal year
- B. For organizations with a calendar year, Form 990, Form 990-EZ or Form 990-N is due on May 15th of the following year
- C. An **automatic** six-month extension may be requested, generally on Form 8868
- D. All Forms 990 must be filed electronically

The Form 990

Statement of Revenue

- A. Three sections
 1. Contributions, grants, etc.
 2. Program services income
 3. Other income
- B. Four categories – in columns:
 1. Total
 2. Exempt function
 3. UBI
 4. UBI but exempt

Contributions

- A. The value of non-cash contributions and gifts should be included in Lines 1a through 1f as appropriate using the valuation as of the date of receipt



- B. Schedule M is required when the total value of non-cash contributions exceeds \$25,000 or includes art, historical treasures or qualified conservation contributions of any amount
- C. The value of donated *services* is NOT reported on any of Lines 1a through 1f nor is it considered a non-cash contribution for Line 1g

Program Service Revenue

- A. Activities that form the basic reason for the organization's existence; these revenues are sometimes referred to as "exempt function income"
- B. Some examples of program services revenues are:
 - 1. Tuition for a school
 - 2. Admission fees for a museum, art gallery or performing arts company
 - 3. Interest income on loans made by a credit union to its members
 - 4. Convention registration fees
- C. Some program services revenues may also be unrelated business taxable income (UBTI), Column 3

Fundraising

- A. Fundraising should be the gross receipts from fundraising events not including donations and gifts received at these events, such as dinners, auctions, gaming events conducted for the **sole or primary purpose** of raising funds for the organization's exempt purpose
- B. Donations and gifts are listed on Part VIII Line 8a referencing their inclusion on line 1
- C. Fundraising events do not include events or activities that substantially further the organization's exempt purpose even if they also raise funds. Revenue from such program service activities is reported on Line 2.



Program Service Revenue

- A. Might come from activities that could be unrelated business activity as well
 - For example, a social club that charges rental fees to both members and non-members for the use of club facilities
- B. Membership dues are program service revenues when they are **comparable to membership benefits** received

Expenses

- A. Four columns:
 - 1. Total
 - 1. Program services
 - 2. Management and general
 - 3. Fundraising
- B. Expenses listed should not duplicate any expenses reported on Lines 6b, 7b, 8b, 9b or 10b of Part VIII
- C. Only organizations exempt under 501 (c)(3), 501(c)(4), and non-exempt charitable trusts must divide their expenses in Columns B, C and D

Program Services Expenses

- A. Activities that are directly related to the purposes for which the organization was granted tax exemption
- B. Includes expenses that are also deductible in determining UBTI when the activity involved is properly categorized as a program service activity
- C. Itemized expense categories may be appropriate to only one column or split between multiple columns

Management & General

- Indirect costs of operating the organization not directly involved in providing the exempt function product or services and not identified as a fundraising activity, for example:
 - 1. Cost of the executive director attending a conference



2. Premiums for liability insurance covering the board of directors
3. General legal services
4. Investment management fees
5. Fees to prepare Form 990

Key Employee

- Three tests
 1. Reportable compensation from organization and all related organization is > \$150,000 **AND**
 2. Has responsibilities, powers or influence similar to that of officers, directors, etc., **OR**
 3. Manages a discrete segment representing 10% or more of the activities, assets, income, or expenses of the organization, **OR**
 4. Has or shares authority to control or determine 10% or more of the organization's capital, budget or compensation, **AND**
 5. Is one of the 20 highest compensated employees
 6. An employee that is paid less than \$150,000 per year is not a key employee, *regardless of their responsibility.*

Disqualified Person

- A disqualified person includes:
 1. A disqualified person's family member
 2. A 35% controlled entity of a disqualified person
 3. A donor or donor advisor to a donor advised fund
 4. An investment advisor of a sponsoring organization
 5. Any person who was in a position to exercise substantial influence over the affairs of the organization at any time during a five-year period ending on the date of the transaction
 6. Persons who hold certain powers, responsibilities, or interest are among those who are in a position to exercise substantial influence over the affairs of the organization. Notice the similarity to "insiders."

Balance Sheet

- A. All organizations must complete Part X. No substitute balance sheet will be accepted



- B. The balance sheet amounts should be the **same as shown in the organization's books, unadjusted for tax differences**. This is the same as for taxable entities.
- C. Lines 27 through 34 of the Form 990 balance sheet reflects accounting items specifically related to nonprofit organizations, principally in the concept of fund balances.

Fundraising

- Fundraising:
 1. Activities that are conducted **primarily** to solicit contributions
 2. Proration may be required
 3. Special attention when outside fundraising companies are used

Accounting

- Form 990 instructions say:
 1. "In order to be permissible, an accounting method must **clearly reflect the taxpayer's income**. Unless instructed otherwise, the organization should generally use the same accounting method on the return (including the Form 990 and all schedules) to report revenue and expenses that it regularly uses to keep its books and record."
 2. Small organizations may use accrual accounting. Cash accounting is also used by many very small organizations, but it is not recommended in favor of greater accuracy and control of accrual accounting.

Detailed Operating Information

- Detailed information on operations is reported in the following:
 1. Part III, *Statement of Program Services Accomplishments*
 2. Part V, *Statements Regarding Other IRS Filings and Tax Compliance*
 3. Part VI, *Governance, Management and Disclosure*
 4. Part VII, *Compensation of Officers, Directors, Trustees, Key Employees, Highest Compensated Employees and Independent Contractors*.

Governance

- Three parts
 1. Governing body
 2. Operating policies
 3. Compliance with public inspection



Independent Voting Board Member

- A. May receive compensation and expense reimbursements as a board Member
- B. Board member must not be compensated as an officer or employee
- C. No family member can receive either compensation or any material financial benefits
- D. Must not receive more than \$10,000 in compensation, plus direct expense reimbursements as an independent contractor.
- E. Must not receive direct or indirect financial benefits from the organization that are material

Operating Information

- A. Small organizations may find the questions in Section B intimidating and intrusive
- B. An organization *is not required to explain WHY* it does not have a written conflict of interest, whistleblower or records retention policy or why key people are not required to disclose interests that could result in conflicts when such is the situation
 - 1. There are no requirements in the IRC that an organization have these policies and procedures. These policies are “best practices” for the organization to follow.
 - 2. State law and governing documents may be more demanding than IRS in this area
 - 3. Failure to have such policies could bode poorly if the organization is the victim or perpetrator of an offence that such policy might have prevented.

Compensation of Officers, Directors, etc.

- A. Enter in Section A up to 25 officers, directors, trustees, key employees and highest paid employees.
 - 1. Key employees must have received compensation > \$150,000
 - 2. Highest paid employees must have received compensation >\$100,000
 - 3. Former officers, key employees, etc. must have been paid >\$100,000
 - 4. Former directors/trustees are listed, paid more than \$10,000



- B. A person is considered a “former” officer, director...etc. only if they did not serve in that capacity at all during the current tax year but did serve in such capacity in *any* of the organization’s prior five tax years.
- C. The form does not ask for the address of persons listed in this section. The assumption is that anyone listed may be contacted at the main address of the organization.
- D. Never include anyone’s Social Security number **in Part VII or on Schedule O, or in any other part of Form 990 or attachments.**

Checklist of Required Schedules

- Schedule O is always required

Support Schedules

- A. Most common schedules for small, local organizations:
 - 1. Schedule A – All 501 (c)(3)s
 - 2. Schedule B – Major Contributors
 - 3. Schedule D – Supplemental Financials
 - 4. Schedule G – Gaming and Fundraising
 - 5. Schedule M – Non-cash Contributions
 - 6. Schedule O – All Organizations Explanations
- B. Only 501(c)(3) organizations need Schedule A
Schedule B requirements vary by exemption type (see instructions)
- C. The IRS does not consider the return complete when [any of] these schedules are required and not attached
- D. An incomplete return is not considered “filed” and therefore is subject to a late filing penalty
 - Failure to attach these schedules is one of the most common errors made with Form 990
- E. Penalty of \$20/day. The maximum late filing penalty is limited to the lesser of 5% of gross receipts or \$12,000 when gross receipts are <\$1,208,500



- If the organization has \$1,208,500 or more in gross receipts, the penalty becomes \$120/day for a maximum of the lesser of 5% of gross receipts or \$60,000

Schedule A

- A. Required for all organizations exempt under IRC 501(c)(3) if required to file form 990 or 990-EZ
- B. Designed to determine whether the organization has met the requirements necessary to avoid private foundation status
 - The failure to include Schedule A or other required schedules is a common error and can ultimately subject the organization to penalty.

Schedule A – Public Support

- A. The organization's determination letter will specify the code section that the IRS **anticipates** that public charity status will be earned by the organization
- B. During the **first five years of existence**, both organizations will complete only the Public Support and Total Support lines of Part II or Part III respectively and check the box on Line 13 or Part II or Line 14 of Part III
- C. What is important is that the organization is able to meet at least one of the allowable public support tests

Public Support

- Among the differences in the support information between Parts II and III is the ability in Part II to claim a special 10% facts and circumstances test, it must describe in Schedule A, Part VI how it meets the test

Schedule B Contributors

- A. IRS issued final regs in TD 9898 (5/28/2020)
 1. IRS exercised its discretion, as allowed in Reg §1.033-2(g)(6), so that exempt orgs., other than Code Sec. 501 (c)(3): orgs., will no longer be required to report **contributors' names and addresses** on Schedule B of Form 990 or Form 990-EZ.
 2. Substantial contributions by amount must still be reported anonymously by organizations exempt under other sections.



- B.** To be listed on Schedule B, the general rule is that a donor must contribute \$5,000 or more to the organization during the tax year being reported.
- 1. In counting to \$5,000, only individual contributions of \$1,000 or more each are considered.**
 2. Check the “general rule” box on page 1 of Schedule B.
 3. By election, an organization may list only donors whose contributions exceed the greater of \$5,000 or 2% of total revenues from contributions, gifts, etc. (Form 990, Part VIII, Line 1h).
 4. Check the first “special rule” on page 1 of Schedule B

Schedule B

- A.** The Supreme Court in 2021 held that a state cannot require up-front disclosure of a charitable organization’s Form 990, Schedule B, which contains the names, addresses and contribution amounts of substantial donors.
- B.** The state must narrowly tailor its disclosure requirements to avoid a widespread burden on donors’ First Amendment rights to free speech and association. The burden can’t be justified by the state’s interest in preventing and detecting fraud and achieving administrative efficiency.



Unrelated Business Income – Form 990-T

Overview

- A. Certain activities carried out by churches & non-profit organizations may be subject to federal income tax.
- B. Misconception is that it is “bad” to do these activities.
- C. Many exceptions apply, so look carefully at all sources of revenue to determine if tax is due.
- D. Basic idea here is to eliminate unfair business advantage that tax-exempt organizations have as they compete with taxable organizations.
- E. Applies to almost all tax-exempt organizations.
- F. Although churches are exempt from filing Form 990, must file Form 990-T if have \$1,000 or more of gross UBI in a year.

Who is subject to unrelated business income tax [UBIT]?

- 1. All Section 501(c) organizations [except (c)(1)]
- 2. Church and religious organizations
- 3. Pension and profit sharing plans
- 4. State colleges and universities

Three Criteria For Taxation

- A. Income derived from a trade or business
 - 1. Activity conducted for the production of income from the performance of services or the sale of goods.
 - 2. Existence of a profit motive.
 - a. Does not mean actual profits must be made.
 - b. Losses from one activity cannot offset income earned by other activities.



3. Each program and many fundraising activities are businesses.
 4. Activity done in a commercial manner, i.e., like a for-profit entity would do it.
- B. Trade or business must be regularly carried on**
1. There is no precise measurement for regularity
 2. Examples used by IRS
 - a. Sandwich stand for two weeks at a state fair – not regularly carried on.
 - b. Commercial parking lot for one day each week – is regularly carried on
 3. Must be measured against the length of a particular season if applicable, e.g., selling Christmas trees.
 4. The “how long” factor must include preparatory time for the activity.
- C. Trade or business must not be substantially related.**
1. Substantially related is recognizably large or material – no formula – fundamental question: Is the organization primarily engaged in exempt activities?
 2. Size and extent of the activity in relation to size and extent of the exempt function – how much UBI is too much?
 - a. Activity conducted on a scale larger than necessary to complete the functions – you have UBI
 - b. Activity is partially related to exempt function
 - c. Some percentages to consider
 1. Rev Rul 57-313: 75% UBI is okay
 2. Orange County Case: 33% UBI is not okay
 3. Safe perhaps 15%-20% before considering a for-profit entity.
 3. “Same state” test says if product of activity is sold in basically same state as it was produced – you do not have UBI]
 4. “Dual use test” deals with use assets and facilities for exempt purpose and unrelated purpose – allocation of expense is key.
 5. “Exploitation test” holds that income generated in connection with the good will of a non-profit could be UBI.



Exceptions to UBIT Rules

A. Activities

1. Performed substantially [more than 85%] by volunteers
2. Related to selling merchandise, substantially [more than 85%] of which was donated.
3. Distribution of low-cost [\$12.50 for 2023] goods in return for donations.
4. Conventions or trade shows of certain organizations in educating members or attracting new members.
5. For the convenience of members, students, patients, officers, or employees.
6. Bingo

B. Passive Income

1. Interest and dividends
2. Royalty income
3. Rental income from real property not financed by debt
4. Gain on the sale of assets
5. Research income

Income From Debt Financed Asset is Unrelated

A. Debt financed income

1. Includes income producing assets that were acquired with borrowed funds.
2. Includes rental income.
3. Includes interest, dividends, and capital gains on investment assets.

B. Prior to 1969, tax exempt organizations could borrow funds and use those funds to purchase business and investment property.

1. Taxable entities were adversely affected.
2. New law passed in 1969 to even the playing field.



C. Exceptions

1. When substantially all [85% of more] of the property's use is directly related.
2. If related use falls below 85% only a portion is exempt.
3. Property used in an activity not unrelated because it is:
 - a. Carried out by volunteers
 - b. Performed for the convenience of members, etc...
 - c. Involved in selling merchandise, substantially of which has been donated [e.g. a thrift shop]

D. Debt-financed refers to the unpaid balance of debt incurred:

1. In acquiring or improving property
2. Prior to acquiring or improving property if the only reason for the loan was to acquire or improve the property.
3. After acquiring or improving property if the only reason for the loan was to acquire or improve the property and it was reasonable to foresee the need for a loan.

Note: Rental income is subject to tax:

- When debt incurred because of the property and is outstanding
- Involves personal property
- Rent is calculated as a percentage of net income
- Rent includes payment for services rendered by the non-profit to the lessee

Compliance and Calculation of Tax

1. Form 990-T filed

- a. When unrelated gross income is \$1,000 or more
- b. Due on 15th of fifth month following year end [typically December 31 making May 15th the deadline]
- c. Extensions are allowed
- d. Penalties apply: 5% for late filing and .5% (1/2%) for late payment of tax
- e. Estimated tax payments are required: Due the 15th of April, June, Sept, & December if tax will be least \$500



2. Use tax rates applicable to for-profit corporations for most non-profits corporations: flat 21%
3. May deduct expenses that are “directly connected with” the conduct of the unrelated trade or business – more narrow than “ordinary and necessary.”
4. Is subject to the public disclosure rules

NON-CASH CONTRIBUTIONS

A. Form 8282

1. Completed by the organization [church or non-profit]
2. For the contributions in excess of \$5,000 [other than certain publicly traded stock.]
3. Organization signed donor’s Form 8283, Part B
4. If organization sold, exchanged, consumed, or otherwise disposed of the property within three years of the contribution unless exception applies.
 - a. Property consumed or for charitable purpose
 - b. Property was one of several items donated and had a value of less than \$500 as noted on donor’s Form 8283, Part B
5. Filed with IRS Center in Ogden, UT within 125 days from the date the organization disposed of the property.

Note: If the organization had no reason to know that Form 8282 was required, must file within 60 days of learning of that Form 8282 is, indeed, required. Also, must provide copy to donor.

B. Form 8283

1. Completed by individual donor
2. For non-cash contributions in excess of \$500
3. Part B deals with property in excess of \$5,000 and requires that a qualified appraisal be attached to the tax return [Form 1040]



4. Filed with the Form 1040 for the year of claiming the contribution deduction.
5. Organization should have these on hand to give to people who give non-cash in excess of \$500.

OTHER ELEMENTS

A. IRS Disclosure Rules – Public Inspection

1. Must make Form 1023 [exemption application] available
2. Must make three most recent Form 990's available
3. Can post on the internet
4. Request can be made in person
 - a. Make copies immediately
 - b. If unusual circumstances, next business day if back to normal, but no later than five days.
5. Request can be made in writing
 - a. Includes mail, e-mail, facsimile, or private delivery
 - b. Provide within 30 days unless have policy calling for prepayment of copying and postage fees. If policy in place, must provide within 30 days of receiving fees.
6. Fees cannot exceed IRS amounts – 20 cents for each page plus actual cost of postage.
7. If no prepayment policy, must inform the requester if fees will exceed \$250 and get OK before providing copies.
8. If site is a regional or district office with fewer than three full-time employees or with no management staff on site, then not required to provide copies at this site.

B. Form 8868 simplifies extension requests for 990 & 990-T

1. Simply check the box for automatic six month extension
2. No additional extension available

