



IMPORTANT IMPLICATIONS OF THE PROPOSED REVISIONS TO FORM 990

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Welcome & Introductions



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Overview of Presentation

- General introduction to the proposed revisions
- Emphasis on implications and themes rather than specific wording
- Particular emphasis on new tax-exempt bond reporting and hospital reporting requirements

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Background of Proposed Form 990 Changes

- Wholly redesigned form released for public comment on June 14, 2007
- Proposed to become effective to 2008
- September 14, 2007 deadline for comments
- First overhaul since 1979

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Deficiencies of Current Form

- Inadequate description of filing organization
- Inadequate basis for “comparing an organization with its peers”
- Congressional criticism of IRS oversight of exempt organizations

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Purposes of the Proposed Revisions

- Enhancing transparency
- Promoting compliance by enabling the IRS to accurately assess compliance
- Minimize filing burden

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Overview of Proposed Changes

- 10-page “core” form
- 15 schedules
- Reporting depends on nature of reporting organization, its activities, finances and other matters
- Disclosure of revenue, expense and balance sheet items is comparable to current form

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Overview of the “Core” Form

- Summary section provides a snapshot of key information (mission, activities, governance, revenue, expenses and assets)
- Summary requires statement of
 - Total number of directors and independent directors
 - Highest compensation amount paid to any one person
 - Percentage that total officer, director and key employee compensation bears to total expenses

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Overview of Schedules

- Public charity status
- Contributions
- Lobbying and political activities
- School activities
- Community benefits of hospital organizations
- Executive compensation
- Tax-exempt bonds
- Others

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Compensation Disclosures

- Only W-2 (or 1099) compensation paid must be reported
- Schedule J requires breakdown of reported compensation similar to current form Schedule A
- Schedule J thresholds
 - \$150,000 reported compensation for any officer, director or key employee
 - \$250,000 total compensation for any person

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Overview – Narrative Questions

- In general, narrative questions are far broader than in current form
- An example: whether the organization has a “written policy that requires an organization to safeguard its exempt status with respect to its transactions and arrangements with related organizations”

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Compliance Rationale for Proposed Tax-Exempt Bond Changes

- “The Service is aware of significant noncompliance with recordkeeping and record retention requirements relating to tax-exempt bonds issued by or for the benefit of section 501(c)(3) organizations. This has made it difficult for the Service to determine whether bonds continue to remain qualified throughout their life. The Service is also concerned about the investment of proceeds that might circumvent existing arbitrage rebate requirements.”

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Tax-Exempt Bond Compliance Context

- Audit initiative targeted at 501(c)(3) bonds
- Compliance check letters on tax-exempt bond compliance – expected this summer
- Revisions to Form 8038
- FAQs on record retention requirements – posted on IRS website

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Review of Existing Form 990 Tax-Exempt Bond Reporting Requirements

- Line 64a: “Tax-Exempt Bond Liabilities”
- Instructions require a schedule showing (a) the purpose of the issue; (b) the amount of the issue outstanding; (c) the unexpended proceeds, if any; (d) whether any portion of the bond-financed facility was “used” by a third party and, if so, the percentage of space used

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Overview of New Tax-Exempt Bond Reporting Requirements

- All information in current Form 990
- Much greater detail on private use
- Compensation of third parties
- Issuance costs from proceeds
- Working capital expenditures
- Defeasance information
- Refunding information
- Temporary period qualification
- Treatment upon cessation of operations

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Detailed Private Use Information

- Separate reporting for “management contracts”, “research agreements”, ownership by a partnership and other use
- Reporting of management contracts and research agreements not within IRS safe harbors
- Reporting “highest percentage of use”

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Detailed Private Use Information – Reporting “Safe Harbor” Compliance

- “Management contracts” probably broadly refer to most service contracts, as defined in Rev. Proc. 97-13
- “Research agreements” have a narrower definition, as defined in Rev. Proc. 97-14
- Safe harbor reporting in addition to private use reporting

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Safe Harbor Compliance Reporting: Problems

- Failure to meet safe harbor does not necessarily result in private use
- Many common arrangements are not within safe harbor
- Burden of separate tracking of private use and safe harbor compliance
- Specific safe harbor opinions may be required

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Comparison: Other IRS Tax-Exempt Bond Safe Harbors

- “3-bid” procedure to establish fair market value of guaranteed investment contracts and defeasance securities
- Safe harbor for brokerage fees and commissions for investments
- Form 8038-T requires information about GICs and brokerage fees and commissions, but not safe harbor compliance

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Compensation of Third Parties

- Compensation “with respect to” any tax-exempt issue
- Not limited to issuance expenses
- Total payments and payments from bond proceeds
- \$10,000 threshold
- Role in the issue (bond counsel, borrower’s counsel, financial advisor, underwriter)
- Other roles
- Formal selection process

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Compensation of Third Parties: Possible IRS Uses

- Identify “two hat” transactions of possible concern to the IRS (e.g., underwriter and credit enhancer)
- More readily identify transactions of a particular “promoter”, or team of professionals, under IRS scrutiny
- IRS could link to Form 8038-T identification of GIC providers and derivative counterparties

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Compensation of Third Parties: “Formal Selection Process”

- Proposed instructions do not define or explain this term
- Presumably, a formal interview or bidding procedure generally would suffice
- May be targeted at identifying “promoter” transactions

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Costs of Issuance Reporting

- Already required on Form 8038
- Would cover costs of issuance paid after the date of issuance

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Working Capital Expenditures

- Working capital financing is generally permitted, but subject to restrictions
- Special importance for the \$150 million limit on nonhospital bonds
- May reflect a general IRS skepticism regarding working capital financings
- May raise difficult interpretive questions

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Defeasance Information

- Would cover advance refunding, change of use, acquisition financing and other defeasance escrow
- Part VII, line 6c would require identification of any defeasance escrow other than an advance refunding escrow
- Purpose of defeasance escrow is not otherwise required to be stated
- Date of redemption of defeased bonds is not required to be stated

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Temporary Period Information

- Probably intended to focus on whether new money project funds qualify for the general 3-year temporary period
- Part VII, line 6b would require statement whether funds were invested beyond a temporary period exception
- Form 8038-T requires the same statement
- IRS could compare to unspent proceeds and placed in service date reporting

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Placed in Service Date Reporting

- Relevant to rules for measuring private use, bond maturity limitations, and time limits for determining how bond proceeds are spent
- IRS reason for information is not clear, but probably reflects an expectation that post-issuance compliance procedures require keeping track of placed in service dates
- Reporting numerous placed in service dates may be burdensome

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Tax-Exempt Bond Information Not Required

- Amount of nonhospital bonds, although working capital reporting is relevant and included on Form 8038
- Private ownership as distinct from other private use, except for partnership ownership
- Derivatives entered into after the date of issuance
- Rebate compliance, although largely covered by Form 8038-T
- Statement whether the organization has a written tax-exempt bond compliance policy

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“Transition Relief” for Tax-Exempt Bond Changes a Possibility

- Comments specifically invited on “transition relief” for tax-exempt bond changes
- Recent regulations have provided transition relief to bonds issued before May 16, 1997
- Invitation for transition relief may indicate that the IRS does not expect to substantially change the approach

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Implications for Compliance Check Letters

- Emphasis on perceived recordkeeping noncompliance
- Emphasis on management contract and research agreement safe harbors

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Additional Notes on the Tax-Exempt Bond Recordkeeping Requirements

- Record retention “FAQs” are posted on the IRS website, but the IRS has not provided a formal legal analysis of recordkeeping requirements
- Part III, line 5 would require a statement regarding whether the organization has a written document retention policy

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Community Benefits and Other Reporting by Hospital Organizations

- New Schedule H applies to organizations that operate and maintain facilities to provide hospital and medical care, including clinics, skilled nursing facilities and others
- Based on Catholic Health Associations community benefit reporting model

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Hospital Reporting: Schedule H Purposes

- IRS states intent “to quantify, in an objective manner, the community benefit standard applicable to tax-exempt hospitals”

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Hospital Reporting: Schedule H Part I

- Costs and revenues relating to
 - Charity care
 - Care provided to beneficiaries of Medicaid and other governmental programs
 - Other “subsidized” health services
 - Community and professional health education programs
 - Research activities

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Hospital Reporting: Possible Schedule H Implications

- Does emphasis on costs in excess of revenues suggest a withdrawal from Rev. Rul. 69-545 (generally that health care is an inherently charitable activity)?
- Future IRS guidance
- Legislation
- State property tax and other exemptions

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Hospital Reporting: Other Schedule H Information

- Collections relative to gross charges as between different payor categories
- Debt collection policies
- Interest owned in management companies and joint ventures in which directors, officers, key employees and physicians are owners
- Processes for assessing health needs in the community
- Information and education provided to patients on financial assistance
- Emergency room policies and procedures
- How health facilities otherwise further exempt purposes
- Name and address of all health care facilities, including a description of activities and programs at each

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Presentation Takeaways

- Burdensome and extensive reporting requirements for large exempt organizations
- Different revisions serve different purposes
- Tax-exempt bond revisions have strong implications for enforcement and other compliance initiatives
- Hospital revisions may have stronger implications for future guidance or legislation

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