SIMPSON THACHER

CLIENT MEMORANDUM

Policy and Practice Checklist for the 2008 IRS Form 990

December 8, 2008

The Internal Revenue Service (the "IRS") recently released a redesigned 2008 Form 990 (the "2008 Form 990"), "Return of Organization Exempt from Income Tax."[1] This memorandum summarizes in checklist form the governance policies and practices about which the IRS now inquires.

The Form 990 is used by organizations exempt from income tax under Section 501(c),[2] including Section 501(c)(3) organizations that are classified as public charities. Organizations classified as private foundations do not use the Form 990, but instead use the Form 990-PF for their annual return. Those organizations that are required to file the redesigned 2008 Form 990 will find a substantial number of new disclosure requirements regarding governance policies and practices. Many of the policy questions can be found in Part VI *(Governance, Management and Disclosure)* of the 2008 Form 990, but others are scattered throughout the Form. While most of these questions request information about policies or practices that are not required by federal tax law, these questions appear to represent particular areas of focus for the IRS and behavior modification suggestions that the IRS would like to encourage filing organizations to implement. Organizations, whether or not required to file the 2008 Form 990, will want to consider the information the IRS will now gather regarding policies and practices, and to implement or revise internal practices where desirable. In general, to answer policy and practice questions favorably on the 2008 Form 990, the filing organization must have adopted the applicable policy or practice on or before the last day of its 2008 tax year.

The IRS has instituted a graduated

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1 For further information, please see the Client Memorandum entitled "Changes to 2008 IRS Form 990 and Instructions," available under the Publications link at http://www.simpsonthacher.com/content/publications/pub760.pdf

2 All section references are to the Internal Revenue Code of 1986, as amended. Generally, organizations exempt under Sections 572 or 4974(a) must also complete the Form 990.

transition period for the 2008 Form 990, in order to give filing organizations time to become familiar with the new form. The redesigned form will be phased in over a three-year period, during which an organization's annual filing requirement will be based upon its financial activity. Beginning with the 2008 tax year, certain organizations which formerly had to file Form 990 may be able to instead file the shorter Form 990-EZ. The policy and practice checklist outlined below applies only to the 2008 Form 990, not to the Form 990-EZ, which does not include any questions regarding policies and practices. Generally, organizations with gross receipts greater than or equal to $1,000,000, or total assets greater than or equal to $2,500,000 at the end of the tax year will be required to file the redesigned Form 990 for the 2008 tax year. Organizations with gross receipts or total assets below these minimum amounts may instead file either Form 990-EZ or Form 990-N for 2008, depending upon the level of financial activity.[3]

Although the items on the following checklist are all referenced in the 2008 Form 990, not all may be relevant to every organization, and the list is not all-inclusive. Please contact us with questions about your organization's particular circumstances.

POLICY AND PRACTICE CHECKLIST

Governance Policies

Part VI, Section B of the 2008 Form 990 requests that filing organizations disclose whether or not the following policies and practices have been adopted:

☑ Conflict-of-Interest Policy

Part VI, line 12a of the 2008 Form 990 asks whether the filing organization has a written conflict-of-interest policy. For organizations that do have a written conflict-of-interest policy, line 12b asks whether officers, directors or trustees and key employees are required to annually disclose interests that could give rise to a conflict. Line 12c asks whether the organization consistently monitors and enforces its conflict-of-interest policy, and if so, to describe how it does so.

A conflict-of-interest policy puts into place mechanisms by which relationships, financial interests or business affiliations that could result in conflicts of interest between the organization and an individual are identified and resolved. Under such a policy, Board members, officers and key employees annually disclose potential conflicts. The IRS includes a sample conflict-of-interest policy as an attachment to the instructions for IRS Form 1023.

☑ Whistleblower Protection Policy

Line 13 of Part VI of the 2008 Form 990 asks whether the filing organization has a written whistleblower policy.
It is illegal for any person to retaliate against a whistleblower who provides truthful information to a law enforcement officer regarding the commission of a federal offense. A whistleblower protection policy outlines an organization's approach to situations of whistleblowing, and establishes procedures for the reporting of accounting or financial wrongdoing.

☑ Document Retention and Destruction Policy

Line 14 of Part VI of the 2008 Form 990 asks whether the filing organization has a written document retention and destruction policy.
It is illegal for any person to knowingly alter, destroy, mutilate, conceal, cover up or falsify any record, document or tangible object with the intent to impede, obstruct or influence the investigation or administration of any matter within the jurisdiction of any federal department or agency or any bankruptcy proceeding. A document retention and destruction policy provides guidance regarding the length of time certain electronic and hard-copy files must be stored before they are destroyed.

☑ Compensation Policy

Lines 15a and 15b of Part VI of the 2008 Form 990 request information regarding the filing organization's practices for awarding compensation to its key employees and

[3] Further information on the financial threshold requirements can be found at http://www.irs.gov/charities/article/0,,id=184445,00.html.

officers. Similar information is also requested in Line 3 of Schedule J. The filing organization must disclose whether the process for determining the compensation amount awarded to such individuals includes review and approval by independent persons, a review of comparable data and contemporaneous substantiation of the decision. In addition, the Form asks that the filing organization describe its compensation award process separately in Schedule O. The filing organization is permitted to pay its managers, other employees and consultants "reasonable compensation." As long as the amount of compensation is both (i) the product of arm's-length bargaining and (ii) "reasonable," it will not result in private inurement, private benefit or intermediate sanction penalty taxes. The "reasonableness" of any given compensation arrangement is determined with reference to the market rate for individuals in comparable positions. The filing organization can create a rebuttable presumption that a particular individual's compensation is reasonable if (i) the compensation is approved by an authorized body of the organization (*e.g.*, the Board of Directors or a committee of the Board of Directors) which does not include the individual whose compensation is being considered and is otherwise composed of individuals who do not have a conflict of interest concerning the transaction, (ii) prior to making its determination, the authorized body relied upon appropriate data as to comparability and (iii) the authorized body adequately documents the basis for its determination concurrently with making that determination.

☑ Joint Venture Policy

Lines 16a and 16b of Part VI of the 2008 Form 990 ask the filing organization to report its involvement in joint ventures, and, if it is involved in such relationships, whether it has adopted a written policy or procedure to evaluate such arrangements under Federal tax law and to safeguard the organization's exempt status with respect to such relationships.

The filing organization may enter into a relationship with a for-profit entity, through which the organization and the other entity will jointly engage in activities. A joint venture policy guides the organization through the establishment and maintenance of a relationship with a for-profit entity, and safeguards the organization's exempt status.

Management Practices

Section A of Part VI of the 2008 Form 990 asks filing organizations about certain management practices. Included in this section are the questions about the following practices:

☑ Contemporaneously Recorded Minutes

Lines 8a and 8b of Part VI of the 2008 Form 990 ask whether the filing organization contemporaneously documents the meetings held and written actions taken by the Board and by any Board Committee. In order to answer "yes," the organization must have recorded contemporaneous minutes for every meeting of the Board and every Board Committee throughout the tax year. For purposes of the 2008 Form 990, "contemporaneous" means by the later of (i) the next meeting of the governing body or committee (*e.g.*, approving the minutes of the prior meeting) or (ii) 60 days after the date of the meeting or written action.

☑ Chapter, Branch, and Affiliate Policies

Lines 9a and 9b of Part VI of the 2008 Form 990 ask whether the filing organization has local chapters, branches or affiliates, and if so, whether the organization has written policies and procedures governing the activities of the related organizations to ensure consistency with the activities of the filing organization.

☑ Form 990 Review

Line 10 of Part VI of the 2008 Form 990 asks about the filing organization's review of the Form 990 prior to its submission. All filing organizations are required to describe in Schedule O the process, if any, used to review the Form 990. That process may be set forth in an audit or Form 990 written policy, which designates either the Board or a Committee of the Board as the reviewer of the Form 990 prior to submission.

Other questions regarding general management practices are scattered throughout the 2008 Form 990. These include questions about the following practices, among others:

☑ Financial Statement Review

Lines 2a through 2c of Part XI of the 2008 Form 990 ask filing organizations whether financial statements were compiled, reviewed or audited by an independent accountant, and if so, whether the organization has a committee that oversees the audits or reviews and that selects the independent accountant.

☑ Grantmaking Practices

Schedule I of the 2008 Form 990 asks filing organizations about grantmaking practices for grants to organizations, governments and individuals in the United States. Schedule F of the 2008 Form 990 asks filing organizations about activities outside of the United States.

Structured grantmaking practices guide staff regarding the maintenance of grant records, the due diligence required prior to the awarding of a grant and the selection criteria to be used by that particular filing organization.

☑ Gift-Acceptance Policy

Line 31 of Schedule M of the 2008 Form 990 asks filing organizations whether they have a gift-acceptance policy that requires the review of any non-standard contributions. A gift-acceptance policy guides organizations through the review of non-standard contributions, and outlines the substantiation and solicitation requirements. A non-standard contribution includes a contribution of an item that is not reasonably expected to be used to satisfy or further the organization's exempt purpose (aside from the need of such organization for income or funds) and for which (i) there is no ready market to which the organization may go to liquidate the contribution and convert it to cash and (ii) the value of the item is highly speculative or difficult to ascertain.

In addition, upon the receipt of a donation, a public charity must follow certain substantiation rules in its acknowledgement of the gift. Every solicitation must comply with applicable state solicitation laws.

☑ Expense Reimbursement Practices

Lines 1a, 1b, and 2 of Schedule J of the 2008 Form 990 ask filing organizations about expense reimbursement practices, including the procedure for payment, reimbursement, provision and substantiation of the following, where applicable: first-class or charter travel; companion travel; tax indemnification; discretionary spending; housing allowance or residence; payments for the business use of a residence; health or social club dues; and payment of personal services. If reimbursement for any of these items was provided to a director, officer or key employee, the filing organization is required to disclose whether it has a written policy in place for such reimbursement, and, if not, to explain why not.

General Disclosure Practices

Part VI, Section C of the 2008 Form 990 requests that filing organizations indicate whether, and if so, how certain documents are made available for public inspection.

☑ State Solicitation Registration

Line 17 of the 2008 Form 990 asks the filing organization to disclose all of the States with which a copy of the Form 990 is required to be filed.

☑ Public Disclosure Practices

Line 18 of the 2008 Form 990 asks the filing organization about the manner in which it makes its Form 1023, Form 990 and Form 990-T (where applicable) available for public inspection.

Line 19 of the Form asks the filing organization to describe in Schedule O whether and how the organization makes its governing documents, conflict-of-interest policy and financial statements available to the public.

New Disclosure Requirements of Which Certain Organizations Should Be Aware

Schedule D of the 2008 Form 990 requires, among other items, supplemental disclosure of certain financial information. These new disclosure requirements include, but are not limited to, the following:

☑ Donor Advised Funds

Organizations which maintain donor advised funds may be required to disclose additional financial information and information about certain written policies.

☑ Organizations Maintaining Collections

Organizations which maintain collections of works of art, historical treasures or other similar assets held for public exhibition, education or research in furtherance of public service may be required to include a description of the collections and explain how the collections further the organization's exempt purposes.

☑ Organizations Maintaining Restricted Endowment Funds

Organizations which maintain restricted endowment funds may be required to disclose additional financial information about activities over a five-year period. Public charities which maintain endowment funds may wish to establish an endowment spending and accumulation policy to guide the expenditure and accumulation of such funds.

For more information, please contact one of the following members, or any member of Simpson Thacher & Bartlett LLP's Exempt Organizations Group:

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