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New Disclosure Issues Facing Exempt Organizations

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Background

On June 8, 1999, final regulations regarding how to make an exempt organization's three most recent Form 990s and certain other documents more accessible to the public were effective. These disclosures were called for as part of a 1997 law that is perhaps better known for allowing the IRS to issue "intermediate sanctions" short of complete revocation of an organization's tax exemption against individuals found to be engaging in better-than-fair-market-value transactions connected with 501(c)(3) and 501(c)(4) organizations.

Both "intermediate sanctions" and the new disclosure rules came about as a response to a perceived need for more accountability among exempt organizations. The infamous United Way matter regarding former chief staff officer William Aramony is widely believed to have been the spark that started Congress on the road to enacting legislation. Despite the fact that these new requirements had the potential of placing new burdens on exempt organizations, umbrella groups like the American Society of Association Executives and the Independent Sector supported it as a means of helping to improve the public's perception of the nonprofit community.

Since the new rules became effective, there have been calls for further disclosures – one from the Joint Committee on Taxation, and another from Congress. The JCT call for further disclosure was contained in a lengthy report issued earlier this year, and Congress' action was to increase disclosure requirements for some political organizations exempt under Section 527 of the Internal Revenue Code.

Form 990 Disclosure

Although the "new" rules for Form 990 disclosure have been in effect for some time, below is a refresher on how they apply to exempt organizations.

1. What do the new disclosure requirements mean to exempt organizations?

Since 1987, associations and other tax-exempt organizations have been required to make their three most recent annual information returns (Form 990) and their applications for tax-exempt status available for inspection by any member of the public who requests it at the organizations' principal offices and certain regional offices (those with three or more staff). The 1996 law broadened the disclosure provisions to require that organizations

provide copies of these documents to those who request them by mail or in person.

When this law and these final regulations become effective on June 8, 1999, organizations will be required not only to allow in-person requesters to view the covered documents while on site, but they also must provide copies to requesters. Organizations will be allowed to charge a small fee for their copying expenses and their actual postage costs.

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2. What documents must an organization disclose as part of these regulations?

A tax-exempt organization (all organizations exempt from tax under Section 501(c) and (d) of the Internal Revenue Code) must be prepared to disclose its application for tax exemption (such as Form 1023 or Form 1024) and any supporting documents filed by, or on behalf of, the organization in connection with its application. Also, the organization must be prepared to disclose any letter or document issued by the IRS in connection with the application. Finally, and probably most importantly, tax-exempt organizations must be prepared to disclose each annual information return (such as Forms 990, 990-EZ, 990-BL and Form 1065) that have been filed for the previous three years.

It is important to note that the IRS exempts from these disclosure requirements an organization's Form 990-T and the portions of the Form 990 that identify names and addresses of contributors to the organization.

3. What is the organization obligated to do in the event it gets a request for disclosure?

There are likely to be three distinct types of requests that an organization will get from members of the public: (A) In-person requests to review covered documents while the individual remains at the organization's offices; (B) in-person requests for copies of all or parts of the covered documents; or (C) mail, fax or electronic mail requests for copies of all or parts of the covered documents.

A. In-person requests to review covered documents: The rules have not changed with respect to these requests. Tax-exempt organizations must make these documents available for such requesters free of charge at the organizations' principal places of business and regional offices with three or more staff.

B. In-person requests for copies: The new rules now require that such requests be complied with on the same business day of the request, except in "unusual circumstances." In response to comments from ASAE on this issue, the IRS included in its final regulations a provision that stated that an organization faced with "unusual circumstances" must provide copies on the next business day following the day the unusual circumstances cease to exist. However, in no event may the period of delay exceed five business days. The final regulations clarify that unusual circumstances include times when the organization's managerial staff capable of fulfilling the

request attends an off-site meeting or convention.

Organizations may charge a fee for this provision of copies. The final regulations cap the fee at the rate the IRS charges for copies of exempt organization tax returns – currently $1.00 for the first page and $.15 for each subsequent page. The organization may limit the forms of payment accepted in this instance to cash and money order. The organization must also comply with requests for copies of specifically identified portions of a document.

As is also the case for requests for copies that are made in writing, an organization can avoid being subject to any of these requirements if it makes the relevant documents "widely available." The means of making the documents widely available that is discussed in the final regulations is via posting on the Internet and allowing members of the public to access the documents for free. There are a number of guidelines on to post the documents, including a lengthy discussion on the format that the documents

are required to appear on the Web. The regulations require the documents to be posted "in a format that, when accessed, downloaded, viewed and printed in hard copy, exactly reproduces the image of the [document] as it was originally filed... ." The regulations would allow posting in the popular "portable document format," since the software necessary to view such documents is generally available for free on the Internet. Organizations that make their documents widely available in this manner must tell

in-person requesters the web address where they can find the documents.

(It should be noted that an organization that makes its application for tax exemption and/or annual information return widely available must nevertheless make the document available for public inspection as noted in item (A) above.)

C. In-writing requests for copies: The regulations require organizations to comply with requests for the covered documents that are made in writing, whether by mail, electronic mail, fax, or a private delivery service.

Organizations must mail copies of the requested documents (or requested parts of documents) within 30 days from the date it receives the request. However, if a tax-exempt organization requires payment in advance (for reasonable copying fees as described above and actual postage costs), it is only required to provide the copies within 30 days from the date it receives payment. If an organization requires payment in advance and it receives a written request without payment or with an insufficient payment, the organization must, within seven days from the date it receives the request,

notify the requester of its prepayment policy and the amount due.

If the organization charges a fee for copying and postage, it must accept payment by certified check, money order, and either personal check or credit card for requests made in writing.

If an organization makes its forms "widely available" in the manner described above, it is required to tell the requester within seven days how the requester may access the documents. When the organization does not require prepayment and the requester does not enclose payment with a request

If an organization makes its forms "widely available" in the manner described above, it is required to tell the requester within seven days how the requester may access the documents. When the organization does not require prepayment and the requester does not enclose payment with a request, the organization must receive consent from the requester before providing copies for which the fee charged for copying and postage exceeds $20.

4. What if the organization feels it is the target of a harassment campaign?

An organization that reasonably believes it is subject to a harassment campaign may suspend compliance with requests for documents and then must file an application for a "harassment campaign determination" within 10 days after suspending compliance. Generally, the regulations provide that a harassment campaign exists where the relevant facts and circumstances show that the purpose of a group of requests was to disrupt the operations of the tax-exempt organization rather than to obtain information. The IRS will

generally presume that requests from members of the news media are not part of a harassment campaign, but that presumption can be overcome by showing specific facts regarding harassment. The regulations also state that an organization may, without submitting an application, disregard requests for copies in excess of two per month or four per year made by a single individual or sent from a single address.

Be careful in exercising this exception to the general rules. If the IRS determines that an organization was not reasonable in its belief that it was the subject of a harassment campaign, then all the fines for failure to disclose this information will be deemed to have accrued from the day the organization suspended compliance.

5. What are the penalties for failure to comply?

The costs of not complying with the disclosure law are $5,000 per document for each willful failure to comply with a request to see the documents covered in this law. There are also penalties of $20 for every day of non-compliance up to a maximum of $10,000.

6. What should my organization do now that these new requirements will soon be effective?

Organizations should identify key persons to be familiar with the requirements of this law and these regulations, and have those persons notified as soon as a request comes to the office.

From a strategic standpoint, organizations may wish to view these heightened disclosure rules as an opportunity to better tell their stories. While there is certain to be a focus by some on the Form 990 section on key staff salaries, there also will be increased scrutiny on all other portions of the publicly available document. Part III of the Form 990 asks for a description of program services, management services, and fund-raising

efforts. Rather than fill the lines provided on the form with a few short phrases, your organization might take time to craft an annual attachment that describes in full detail your organization's broad-reaching activities. Use language similar to your membership recruitment brochure. That way, when the media and members of the public inspect your Form 990, they will find a more complete story of your organization instead of just accounting figures.

Joint Committee on Taxation Report

A 215-page (counting the appendices) volume calling for many new disclosure requirements from exempt organizations was released by the Joint Committee on Taxation (JCT) on February 3. Among the items that are currently not available that the JCT suggests should be disclosed are: Form 990-T for unrelated business income tax, information about exempt organization audits and closing agreements, more information about lobbying activity by 501(c)(3) organizations, and annual tax filings for organizations that are related to exempt organizations.

Also, the report states that the Internal Revenue Service (IRS) should be allowed to provide certain tax information to state attorneys general to assist them in their duties.

There are some concerns in the exempt organization community about some of the calls for increased disclosure. Along those lines, it appears that some of the JCT recommendations are more burdensome than beneficial. For example, the study suggests making public information regarding an exempt organization's voluntary compliance efforts to correct past mistakes. The specter of airing these past mistakes to the public could actually serve as a disincentive for such organizations.

At the time of this writing, Congress has not incorporated any of the recommendations called for in the report. A list of all recommendations appears below:

- Accelerated electronic filing and redesign of Form 990
- Disclosure of third-party communications concerning written determinations
- Confidentiality of taxpayer identification numbers
- Disclosure of annual returns by section 527 organizations
- Disclosure of names under which exempt entities conduct their operations
- IRS notification of public availability of Form 990
- Mandatory disclosure and IRS reporting of exempt organizations' web pages
- Increased penalties for preparers of exempt organizations' returns
- More flexibility for IRS information sharing with state attorneys general
- Increased reporting about transfers among different, related exempt organizations
- Permitting private foundations to report summaries of transactions and assets

- Annual notice requirement for small exempt organizations
- Non-redacted disclosure of written determinations and related file documents
- Non-redacted disclosure of closing agreements and audit results
- Non-redacted disclosure of exemption applications at the time of filing
- Non-redacted disclosure of Forms 990-T and 1120
- Narrative description of lobbying by 501(c)(3) organizations under section 501(h)
- Reporting of 501(c)(3) self-defense lobbying expenses
- Reporting of expenses for nonpartisan analysis that include indirect calls to action

Section 527 Disclosure Law

President Clinton signed legislation into law on July 1 requiring that all groups organized under Section 527 of the Internal Revenue Code notify the IRS of their existence within 30 days of the law's enactment. New 527 groups must notify the IRS within 24 hours of their formation. The law's disclosure requirements will likely not apply to all but a few association-related PACs, due to exceptions written into the law, but earlier versions of this legislation would have indeed had an impact on a number of nonprofit organizations, including 501(c)(4), (c)(5) and (c)(6) groups.

The House Ways and Means Committee had originally passed a bill on June 22, (H.R. 4717) that imposed new disclosure requirements for 501 (c)(4) , (c)(5) and (c)(6) organizations, as well as section 527 organizations. The final package removed the broad coverage and focused more narrowly on section 527 organizations. If the House Ways and Means Committee version had passed, exempt organizations would have faced a very cumbersome reporting regime in the instance they were deemed to have been engaged in what the bill called "disclosable activities." Included under the proposal's broad definition of "disclosable activities" were the mention in an organization's communications of any federal officeholder or candidate for federal office that went beyond the organization's membership. Under that wording, if the Journal of the American Medical Association (presuming that the Journal is read not only by AMA members, but also by nonmembers) discussed Vice President Al Gore's wife's bout with depression, the AMA would likely have to track the expenditures involved in producing the publication and report them to the IRS.

Conclusion

It is anticipated that nonprofit organizations will always be faced with new disclosure proposals and requirements, and will be forced to evaluate such proposal by weighing the administrative and privacy burdens with the desire to maintain a strong public image.