SUNSHINE AND SHADOWS ON CHARITY GOVERNANCE:
PUBLIC DISCLOSURE OF FORMS 990 AND IRS DETERMINATIONS

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Abstract:

As legislatures turn to disclosure as the primary tool of nonprofit regulation, we should ask some basic questions: Why isn’t it enough that charities report information to the authorities, rather than disclose to the public? Is information collected by regulators who worry primarily about financial self-dealing useful to a public worried about charity effectiveness? Ideally, the prospect of disclosure should improve not just the accuracy of filings, but also board monitoring and governance: Boards will become sensitive not only to how operations look, but how well the charity is really doing. If mandated disclosures focus on the wrong questions or paint an incomplete picture, engaged boards can ensure that charities tell their stories through additional, voluntary forms of disclosure. At the same time, increased public disclosure of the IRS’s exemption determinations and revocations argue for formal (rigorous and systematic) guidance from the regulator.

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INTRODUCTION

In the last twenty years, the annual information return filed by federally tax-exempt organizations – the Form 990 – has become not only the public face of individual charities, but also the most readily available data source for potential donors, state regulators, the media, and the charity’s governing board, staff, and volunteers. Indeed, the Internal Revenue Service kept in mind the interests of these various stakeholders when it produced its 2008 radical redesign of the Form 990; this filing now makes available, among other information, a detailed picture of the organization’s governing structure, policies, and related-party transactions. Simply by asking questions about the existence of perceived “best practices,” the Service sends a strong signal of

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their desirability. Meanwhile, the emergence of the third-party online database of Forms 990 maintained by GuideStar – itself a private, nonprofit organization – completes the goal of transparency: Aside from any oversight actions of regulators, any member of the public can scrutinize filings without any awareness by charities of who is taking a look at the Forms 990, when, or for what purpose.

Sunlight, of course, creates both clarity and shadows. Knowing that detailed information about charity structure and practices will be available to the public can – as no doubt intended – influence charity behavior. Importantly, requiring charities to disclosure information to the IRS is a separate question from requiring charities to make their IRS disclosures to the public. Since 1987 exempt organizations have operated under a statutory obligation to provide their Forms 990 upon demand.¹ This significant development made me wonder about the effect on the nonprofit sector from mandated public disclosure of tax filings, as abstruse and arcane as the Form 990 read then. As I wrote in 1996:

The IRS information return required of tax-exempt organizations covers many pages and requests a great deal of information. Charities must report, among other things, their primary activities, their sources of funding, the salaries earned by managers, and any relationships they have with other nonprofit and proprietary organizations. The wealth of data demanded by the IRS inspired the following exchange between a member of the American Bar Association and the IRS’s special assistant for exempt organization matters:

Mr. Gallagher: Howard, what does the IRS do with all this stuff?

Mr. Schoenfeld: It’s not so much what the IRS does with all this stuff. It’s also what the public does with all this stuff. That’s an equal part, I think, of what the question should be.

But what, then, is the public to do with all this stuff?²

Compare this view of public disclosure as a regulatory tool with its expression in a March 2010 letter by former Senate Finance Committee chair (and now ranking member) Charles

¹ See Pub. L. 100-203, Sec. 10702(a), adding subsection (e) to Internal Revenue Code § 6104. In 1998 Congress replaced subsections (d) and (e) with the current subsection (d). See Pub. L. 105-277, Div J, Title I, Subtitle A, Sec. 1004(b)(1).

Grassley, who declared: “The best way I know to increase voluntary compliance is to inject transparency.” He continued:

If a tax-exempt organization has to disclose its top salaries or its payout rates for public scrutiny, odds are it will curb any potential abuses. The vast majority of charities operate above board, without abuse, and should have nothing to fear from more transparency; filling out a form is a lot less burdensome than being subject to a random audit. Congress made the tax-exempt filings with the IRS open for public inspection specifically so that the public would take on an increased role in oversight of charities.

As a result, probably the most significant step the IRS has taken in recent years to increase compliance is revising the Form 990 for tax-exempt organizations. . . .

The new form also provides significant opportunities for the IRS to educate tax-exempt organizations. For example, questions regarding governance and management practices ideally will spur discussions on internal controls and best practices. Such discussions can often be more effective than legislation such as the so-called Sarbanes-Oxley law that tightens financial controls on corporations.

The public’s role in oversight is important. . . . According to The New York Times, it was a professor’s review of the Stevens Institute of Technology’s tax returns and other public documents, and his determination that there were big problems, that resulted in the New Jersey attorney general’s lawsuit against the school’s president and a subsequent IRS investigation.

Such a reliance on public disclosure, however, puts pressure on the IRS to ensure that the form asks the “right” questions, and allows the filer to present a complete and accurate picture. Even if the form is well-constructed, does the public understand it, and react appropriately to the information presented there? Of course, “the public” embraces a variety of constituencies – with different motives – who might be interested in requesting a particular charity’s Form 990.

Meanwhile, pursuant of its obligation to administer and enforce the requirements for federal tax exemption, the IRS has long kept its hand in issues of sound charity governance. The public was treated to peeks at the IRS’s view of appropriate governance through the release of a few otherwise confidential “closing agreements” that the IRS entered into on the condition that the organization agree to publish them.³ More systematically, in 1996, Congress involved the

³ The closing agreements with Jerry Falwell’s Old Time Gospel Hour, Jimmy Swaggart Ministries, and Pat Robertson’s Christian Broadcasting Network not only required the payment of taxes, but also required the organizations to make changes in corporate governance and to publicize the general terms of the closing agreements. See Public Statement, Jimmy Swaggart Ministries, Baton Rouge, Louisiana (Dec. 17, 1991), 5 Exempt Org. Tax Rev. 205 (Feb. 1992). In this agreement, the
IRS in charity governance by adopting the “intermediate sanctions” statute designed to deter charity insiders from engaging in “excess benefit transactions” with charities.\(^4\) The legislative history to Internal Revenue Code section 4958 suggested that administrative guidance could protect financial transactions entered into between charities and their insiders if the approval process assured independent decision-making, obtaining comparable data, and documentation. Treasury Regulations issued under section 4958 detail the process for qualifying for such a “rebuttable presumption of reasonableness.”\(^5\)

organization agreed to desist from political activities – Jimmy Swaggart Ministries had endorsed Pat Robertson’s presidential bid-and to pay about $170,000 in back taxes and interest. According to the public statement: “Under the terms of a closing agreement between itself and the IRS, JSM has made certain changes in its organizational structure, including the creation of an ‘Audit and Compliance Committee’ composed of members of an expanded board of trustees, to ensure that no further political campaign intervention activities will occur.” Id. at 207; see also *Statement of Jerry Falwell Regarding Closing Agreement* (Feb. 17, 1993), 7 EXEMPT ORG. TAX REV. 876 (May 1993).

Another much-discussed closing agreement is the settlement between the Service and the Church of Scientology, including all of its constituent entities. Compare *Founding Church of Scientology v. United States*, 412 F.2d 1197, 1199, 1201 (Ct. Cl. 1969), cert. denied, 397 U.S. 1009 (1970) (payments to founder L. Ron Hubbard of 10% of gross income of affiliated Scientology organizations “were disguised and unjustified distributions of plaintiff’s earnings”); and *Church of Scientology v. Commissioner*, 823 F.2d 1310, 1317 (9th Cir. 1987) (“[T]he payments in this case cross the line between reasonable and excessive.”), id. at 1317, aff’d 83 T.C. 381 (1984), with Closing Agreement on Final Determination Covering Specific Matters (Oct. 1, 1993), available in LEXIS, Fedtax Library, Tax Notes Today File, as 97 TNT 251-24 (Dec. 1, 1997) (note that this document was leaked, and never acknowledged by either party). The introduction to Part VI.A of this putative closing agreement states: “it is intended that the consensual sanctions set forth in this section are to provide the Service with intermediate sanctions for activities or conduct not in accordance with the provisions of Code section 501(c)(3) for which revocation of recognition of exemption may be too harsh or otherwise inappropriate as a sanction . . .”. Id. at VI.A.

\(^4\) Evelyn Brody, *A Taxing Time for the Bishop Estate: What Is the I.R.S. Role in Charity Governance?*, 21 U. HAW. L. REV. 537 (1999) (Bishop Estate Symposium Issue). For the August 18, 1999 closing agreement between the Internal Revenue Service and the Kamehameha Schools / Bishop Estate (KSBE), go to www ksbe edu/newsroom/filings/final_v021029.pdf. This Closing Agreement required – in addition to a payment from KSBE to the IRS of $9 million plus interest (for a total of about $14 million) – the permanent removal of the Incumbent Trustees; the reorganization of KSBE around a chief executive officer to carry out the policy decisions of the Board of Trustees; the adoption of an investment policy and a spending policy focused on education; adoption of a conflicts-of-interest policy and adherence to the Probate Court’s directive for setting trustee compensation; a ban on hiring any governmental employee or official until three years after termination of governmental service (or earlier Probate Court approval); the Internet posting of the final Closing Agreement and of KSBE financial statements for the next five years; and a $9 million payment (plus interest). The Closing Agreement did not cover any personal tax liability of the trustees.

More recently, charity governance writ broadly has emerged as a fundamental focus in the regulation of federally tax-exempt organizations. In 2004, the staff of the Senate Finance Committee produced a white paper proposing a broader role for the IRS in charity governance; the nonprofit sector responded with studies and proposals to improve nonprofit governance, including recommendations for self-regulation. Both when chair and now as ranking member of the Senate Finance Committee, Grassley has demanded and posted online massive amounts of information (including emails and correspondence, some labeled “privileged and confidential”) from specific organizations whose governance practices he questioned. An IRS employee seconded to Senator Grassley’s staff later returned to the IRS, where she was a key participant in the multi-year overhaul of the Form 990. (She is now back on Grassley’s staff.)

The IRS itself followed a transparent process in its Form 990 redesign: It posted online drafts of the form (and schedules) and the thousands of comments it received, all still available on the IRS website. That exposure process allowed the IRS not just to rework misleading questions but also recast the questions both to produce a better picture of the organization and to steer the sector to good governance structures and practices. Notably, the IRS acceded to a storm of pleas to remove the most “prejudicial” (and uninformative) lines from the all-important new summary page (Part I). (Compare the 2007 draft, on the first page of the Appendix, below, with the final version, on the third page.) Line 6 of draft Part I had asked: “Enter the number of individuals receiving compensation in excess of $100,000 (Part II, line 2)”; while this line, like all the others in the summary page, draws from a question elsewhere on the form, what valid information does it convey by including it on the front of the form? Similarly, the IRS removed the three “efficiency ratio” questions, which, while used by some charity watchdog groups and rating agencies, have long been criticized as oversimplified and unhelpful metrics.

To give another example, consider the 2007 draft Form 990's question in Part III (Statements Regarding Governance, Management, and Financial Reporting) on conflict of interest transactions (see the second page of the Appendix, below):

3a Does the organization have a written conflict of interest policy?

b If “Yes,” how many transactions did the organization review under this policy and related procedures during the year?

What is the preferred answer to question 3b? If the organization answers “zero,” is this good (because there were no conflict of interest transactions to review) or bad (because the

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7 The 2007 draft Form 990 and related schedules, the draft instructions, and the comments on these drafts, along with educational material, are available at www.irs.gov/charities/charitable/article/0,,id=185892,00.html.
organization was blind to the interested transactions that occurred)? Commentators pointed out the problems with this and other governance questions of the draft. Substantially revised (and renumbered) Part VI not only addresses the suggestions (see the last page of the Appendix), but also states at the outset: “Governance, Management and Disclosure (Sections A, B, and C request information about policies not required by the Internal Revenue Code.)”. Moreover, the draft did not provide an ability for the organization to provide attachments to the form. In response to complaints – including the argument that it is unconstitutional to deny a filer subject to mandatory disclosure the opportunity to explain yes/no and other short answers – the final form includes a Schedule O for extensions of responses and supplemental narration. The final conflict of interest questions read:

12a Does the organization have a written conflict of interest policy? If “No,” go to line 13.

b Are officers, directors or trustees, and key employees required to disclose annually interests that could give rise to conflicts?

c Does the organization regularly and consistently monitor and enforce compliance with the policy? If “Yes,” describe in Schedule O how this is done.

Separately, since 2003, the Internal Revenue Service has become subject to public disclosure obligations of its own. As a result of Freedom of Information Act suits brought against the IRS, the agency’s views on a range of issues can, at least informally, be gleaned through the release of rulings denying or revoking exemption. (By law, these rulings are redacted to hide the names of and other identifying information about the affected charities and individuals.) Most helpful for the nonprofit sector would be for the Service to take the now-substantial database of denial and revocation letters and develop from it formal guidance on which indicators of governance structure and policies the IRS would like to impose as conditions for exemption.

The simultaneous developments of substance and process – of increased federal interest in charity governance and in the tool of disclosure – threaten to conflate an examination of the relative merits of each. It might be appropriate, for example, to require reporting of certain information to state regulators or to the Internal Revenue Service without also requiring that information to be made publicly available. It is important to recognize, however, that a large percentage of exempt organizations file forms other than the Form 990, or do not even file at all. Because of statutory exemptions, it can be difficult, if not impossible, to obtain much information on churches and on smaller charities. Moreover, hundreds of thousands of charities will fall below the governance radar when the cutoff between charities required to file the Form 990 and the simplified Form 990-EZ is fully phased in: The definition of “small” will double from less than $25,000 in gross receipts to less than $50,000. Finally, arguably the most important disclosures take place internally within the organization.

To explore these thoughts, Part I begins with the desirability of information flow to key
For example, a survey conducted by the charity watchdog BBB-Wise Giving Alliance suggested that the public does not accept fund raising costs over 15 percent, an unrealistically low number.

And now the dark side of sunshine. The largest practical impediment to relying on public disclosure is the unfortunately widespread assumption that providing charity is a free good—and so general overhead, much less fund raising expenses, should be zero or close to it.8 One of the great lost opportunities of the September 11th experience was the failure of charities to defend the costs of wisely allocating charitable resources. More broadly, charities resist increased standardized disclosures because they worry that the public will misunderstand or misinterpret the information. A public that does not understand cost constraints cannot perform effective oversight. A public whose oversight focuses on the wrong considerations induces charities to adopt inefficient and ineffective behaviors.

In this climate, the solution to the problem of a misinformed public is more disclosure—nothing prevents an organization from providing a more positive narrative of its goals and accomplishments. While the competing demands of the various stakeholders cannot always be reconciled, all involved will better appreciate the challenges faced by a charity that reveals rather than hides its costs of fund raising and administration; explains why its executives merit their pay and why its reserves are necessary; and describes its limits as well as its potential in delivering services and addressing social needs. Finally, the sector as a whole should also weigh in, denouncing unacceptable practices.

Compare a recent U.K. report addressing whether public confidence in charities would be affected by increased mandatory disclosure of expense reimbursements. The report opposed expanding mandated disclosure beyond what is already required, arguing, in part:

Practical difficulties exist in meaningfully interpreting and comparing expense amounts. Greater disclosure might risk being at best, of little interest or, at worst, of misinterpretation and even suspicion, possibly leading to damage to public trust and confidence. This might risk elevating expenses to become an inappropriate measure of charity effectiveness and distract attention away from more appropriate measures, namely those relating to a charity’s overall outcomes and impact. It might even lead to pressure to

8 For example, a survey conducted by the charity watchdog BBB-Wise Giving Alliance suggested that the public does not accept fund raising costs over 15 percent, an unrealistically low number.
inappropriately drive down certain costs.

Secondly, the issue of expenses is an important but comparatively small part of a much wider responsibility that trustees and staff have to ensure that the financial affairs of charities are well managed, scrutinised and accounted for through good governance and sound systems of internal control. Wider publication of expenses amounts alone is unlikely to lead to greater accountability on the part of trustees in discharging their responsibilities in this area.9

Rather, the 77-page report – which was based partially on a survey to which 575 registered charities responded – urged trustees to consider additional, appropriate voluntary public disclosure, in addition to ensuring the adoption, internal communication of, and compliance with an expense reimbursement policy.10

Indeed, the voluntary disclosure of information also serves charities that do not solicit donations. All nonprofits remain politically vulnerable – not just to the removal of subsidies, but also to the danger of unwise legislation and regulation.11

Regrettably, the most important information that both regulators and the public might want will continue to be unavailable – simply because performance measurement is an unsolved metric. As a society, we would want to be able to assess whether and which charities are producing favorable outcomes, but often we cannot even measure outputs because quality can be subjective. At the same time, while focusing on outputs (such as patient stays or unemployed trained) can lead to de facto quotas, focusing on outcomes (such as good health or jobs) holds nonprofits responsible for factors beyond their control. Thus, beyond the scope of this paper is the ultimate disclosure question: How do we challenge an organization that says it “does good”?  

I. SOUND GOVERNANCE AND INTERNAL DISCLOSURE

As I describe in the American Law Institute’s project on Principles of the Law of Nonprofit Organizations, for which I am the reporter, a charity’s governing board is responsible for “establishing appropriate procedures for internal controls, including financial controls, legal

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9 REPORT OF THE INDEPENDENT EXPERT GROUP ON EXPENSES 9 (Feb. 2010), available at www.ncvo-vol.org.uk/sites/default/files/ExpensesReportfinal.pdf. The study was prompted by a scandal that erupted in the United Kingdom over expense reimbursements claimed by members of Parliament. Id. at 16-17.

10 Id. at 50-51.

11 See generally Brody, supra note 2; Evelyn Brody, Accountability and Public Trust, in THE STATE OF NONPROFIT AMERICA 479 (Lester M. Salamon, ed. 2004).
compliance, and information flow to the board.\textsuperscript{12} Thus, as a matter of good governance, the board needs accurate and timely information from management, including financial reports, and accurate and timely information from board members themselves, such as when a transaction might present a conflict of interest for a particular fiduciary.

I am often asked by if there are any limits on the information to which a board member is entitled, and the answer is almost always no.\textsuperscript{13} More fundamentally, it seems that we cannot be too basic in explaining to nonprofit board members what information they should be seeking. A comment in the ALI project sets forth the documents which should be provided to every board member.\textsuperscript{14} The availability of Forms 990 from GuideStar’s website (discussed below), of course, means that board members – and prospective board members – can learn a great deal about the organization even if management is not forthcoming.

After all, organization formation and operations generally are private affairs. If the organization is itself a quasi-public entity, it might be subject to sunshine laws.\textsuperscript{15} Tax-exemption alone, however, does not convert a nonprofit organization into a public entity.\textsuperscript{16} (Separately, the

\begin{itemize}
  \item The charity’s trust instrument or articles of incorporation (charter).
  \item The bylaws (amended and restated, with dates, if appropriate).
  \item Board policies applicable to board members – including those relating to conflicts of interest, travel and expense reimbursement, and confidentiality – and any general ethical policy.
  \item A directory of board members and officers, with complete contact information.
  \item Descriptions and charts of any board committees, and current committee assignments.
  \item An organizational chart and contact information for senior staff.
  \item The current budget and recent financial statements, including the management letter from the outside auditor.
  \item Recent Forms 990.
  \item Minutes of recent board meetings and, if applicable, of executive committee meetings.
  \item The charity’s mission or vision statement, if separately prepared.
  \item A schedule of dates and locations of upcoming meetings of the board and of the membership (if any).
\end{itemize}


\textsuperscript{13} See id., § 340. The most common exceptions are for some personnel issues.

\textsuperscript{14} Id. § 320, comment g(6), suggests:

\textsuperscript{15} This topic is covered in the ALI project in draft section 140, comment __ (Council Draft No. 6 2009).

\textsuperscript{16} See exploration of this issue in Evelyn Brody & John Tyler, \textit{How Public Is Private}
government as grant-maker might impose transparency as a condition of funding; state laws vary.) Nevertheless, a great deal of internal information becomes public information because it must be set forth on regulatory reports, as explained in Part III.

Nonprofit governance practices have long remained a mystery. In 2007, the first comprehensive survey was published, by the Urban Institute’s Francie Ostrower.¹⁷ Notably, she found that charities commonly enter into transactions for goods and service (beyond board services) with members of the governing body, and that those transactions grew with charity size; but she further found that it was not even always known to a particular organization whether a fiduciary was on the other side of a transaction.¹⁸

Overall, 21 percent of nonprofits reported buying or renting goods, services, or property from a board member or affiliated company during the previous two years. Among nonprofits with more than $10 million in annual expenses, however, the figure climbs to more than 41 percent. Note however that among those nonprofits that say they did not engage in transactions with board members or affiliated companies, however, fully 75 percent also say they do not require board members to disclose their financial interests in entities doing business with the organization, and thus, respondents may have been unaware of transactions that do exist.¹⁹


¹⁸ Importantly, for the subset of charities dubbed “private foundations” by federal tax law are prohibited from entering into transactions with insiders – other than the payment of reasonable compensation for services rendered. I.R.C. § 4941 (Taxes on Self-Dealing). For a full discussion of interested transactions, see § 330 of the 2007 ALI draft Nonprofit Principle, supra note 12.

¹⁹ OSTROWER, supra note 17, at 8 (footnote omitted). Specifically, that study found:

According to respondent reports, among nonprofits engaged in financial transactions, most obtained goods at market value (74 percent), but a majority (51 percent) did report that they obtained goods below market cost. Under 2 percent reported paying above market cost. Keep in mind too that these are self-reports, and thus, if anything, the figures are likely to underreport transactions resulting in obtaining goods at above market value or at market value costs and overreport transactions resulting in obtaining goods below market cost.

Id. (footnote omitted).
Moreover, “smaller nonprofits were considerably more likely than larger ones to obtain goods and services from board members at below market cost: 58 percent of nonprofits with under $100,000 in expenses obtained goods or services at below market cost from a board member, but the percent drops to a low of 24 percent among nonprofits with over $40 million. The percent of nonprofits that received goods or services at market value, in contrast, was over 70 percent among nonprofits of every size . . .”20 Somewhat alarmingly, 45 percent of those charities engaged in business transactions with board members reported that “it would be at least somewhat difficult were they prohibited from purchasing or renting goods from board members, but only 17 percent said it would be very difficult. . . .”21

How has – and will be – nonprofit governance affected by the knowledge that internal information is public due to its presence on the Form 990 and other filings? (This topic is explored at length in Part III; specifically, see Part II for more discussion of the governance questions in the redesigned Form 990.) Will organizations change their decisions or pay more attention to documenting their decisions, providing additional explanation? Will organizations try harder to skew the information to what it perceives the public wants to see? There is a difference between perceived wrongdoing and actual wrongdoing. If the public misinterprets or demands the wrong “answers,” charities can suffer a loss of trust.

Let me give a personal example. I remember the first December, as I was sitting down to write our charitable contribution checks, when I realized I could and should consult the organizations’ Forms 990 from my home computer. Back then – and sadly, still too often today – you couldn’t expect to find this information on most charities’ own websites, but rather you would have to sneak, feeling somewhat guilty, to GuideStar. There I discovered that two of the organizations to which my husband and I had previously contributed generously reported high executive compensation (i.e., more than four times what I make) and high retained surpluses (i.e., an amount that overwhelms my intended contribution). Then I tried to get a grip on myself: “Hold on,” I muttered. “You’re a professional! Surely you appreciate why these important, well-run organizations need to pay the executive salaries and maintain the reserves they do.” But if that was the reaction of “a professional,” it’s easy to see why charities are loath to report to the public at large.

Even before the 2008 redesign of the Form 990, advisors focused on the importance of having the board know what will appear in the organization’s filing.22 Attention to executive

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20 Id.

21 Id.

compensation, interested transactions, and relationships among fiduciaries will be even more important once the redesigned Forms 990 are filed. As described in Part II, below, the new version of the form contains numerous questions about organizational structure and governance practices. (See also the last page of the Appendix, which reproduces the governance part of the form.) Despite the disclaimer, described in the introduction, above, that this portion of the form “request[s] information about policies not required by the Internal Revenue Code,” the expectation is that most organizations will want to answer “yes” to the questions. It will be interesting to see, as the next few years pass, the rise in adoption of the policies and practices asked about on the return.

More basically, if board members have not routinely been provided with the organization’s Forms 990, they likely will now: One question reads: “Was a copy of the Form 990 provided to the organization’s governing body before it was filed? All organizations must describe in Schedule O the process, if any, the organization uses to review the Form 990.” Not only will the typical board’s role in preparing or reviewing the 990 change, but also the relationship between the board and management could change as the board focuses on reported structures and events as it might not have in the past.

After all, if everyone in the outside world is readily able to review the EO’s Form 990 return, including the compensation and benefits provided to senior management, it is imperative that all board members know enough about executive compensation and benefits to explain and defend the entries on the Form 990. This information is best shared with the board at the time (or close to the time) when executive compensation decisions are made. Such a session will also help prepare the board for situations in which the executive compensation program could be publicly and negatively depicted (i.e., when the Form 990 is accessed and reported by the media). As part of this process, board members should be encouraged to meet privately with compensation committee members if they have more detailed questions or concerns. In addition, some board members may be uncomfortable voicing questions and concerns in an open forum.

23 Besides the questions in Line 12 asking whether the organization has a written conflict of interest policy, described in the introduction, above, other questions ask whether there are written policies addressing whistleblowers, document retention and destruction, and participation by the organization in joint ventures. The one question rooted in statutory and regulatory requirements relates to the process for determining the compensation of top management, officers, and key employees. See Code § 4958, addressing excess benefit transactions engaged in by 501(c)(3) and (c)(4) organizations. Treas. Reg. § 53.4958-6 sets forth a rebuttable presumption that a compensation arrangement or other transaction is reasonable if it is (1) approved in advance by an independent body acting for the organization (2) that obtained and relied on appropriate comparability data, and (3) that the body adequately documented its determination.

24 Form 990 (2008), Core Form, Part VI (Governance, Management, and Disclosure), line 10. It is unfortunate that this question does not allow for the alternative of review prior to filing by a board committee, as recommended in comments made on the draft redesign. It can be expected that many time-pressed charities will prefer to file under an extension than answer “no.”
At the extreme, a nonprofit might even be willing to forgo tax-exempt status in part to preserve the confidentiality of its activities, given that corporate income tax returns are not subject to public disclosure. More likely, a nonprofit might use a for-profit affiliate to carry out charitable activities for which tax exemption would be available, especially when taxable profits are expected to be nonexistent or low. While an organization might sacrifice some support (from employees, donors, or others) in forgoing exemption, other advantages of the for-profit form include the ability to raising equity capital; avoiding an IRS inquiry into whether the nonprofit has sufficient charitable purposes; and gaining some flexibility in providing levels and types of compensation.

II. REGULATORY REGISTRATION AND REPORTING

This Part looks at filings received by nonprofit regulators. Part III’s discussion of public disclosure includes the transparency of enforcement actions by the regulators.

A. State Regulation of Fundraising: Constitutional Limits

A nonprofit corporation typically obtains its certificate of incorporation from the state secretary of state, and makes annual filings with that office. Outside the well-regulated area of charitable solicitation, described below, Marion Fremont-Smith’s comprehensive survey chronicles the development – but lamentably limited extent – of attorney general registration and annual filing (7 states). (Fremont-Smith separately found that in four states the attorney general...)

25 A charity might be expected to have to ensure that it preserves its tax exemption, but a charity may relinquish tax exemption “so long as the charitable organization’s fiduciaries can demonstrate that they made a good faith determination that loss of exemption was in the best interests of the organization.” Marion R. Fremont-Smith, “Relinquishing Tax Exemption: State and Federal Constraints,” presented at the Nonprofit Forum, New York City (Oct. 16, 1991).

26 Compare the new requirement that Forms 990-T, on which an exempt organization reports its unrelated business taxable income, are now subject to public disclosure. See Part III, below.

27 This topic was the subject of an Emerging Issues in Philanthropy Seminar, sponsored jointly by the Urban Institute’s Center on Nonprofits and Philanthropy and by Harvard University’s Hauser Center for Nonprofit Organizations (Cambridge, Mass., Nov. 30, 2000).


29 Fremont-Smith identifies New York, California, Massachusetts, Ohio, Illinois, Minnesota, and New Hampshire. MARION R. FREMONT-SMITH, GOVERNING NONPROFIT ORGANIZATIONS: FEDERAL AND STATE LAW AND REGULATION 316-17 (Cambridge, Mass.: Belknap Press of the Harvard University Press...
must be notified when the nonprofit seeks tax-exemption. In 2008, drafting began on a new uniform statute for the regulation of charities; the project will focus on the authority of state attorneys general to protect charitable assets, notice requirements, remedies, and principles to guide attorneys general in interstate and multi-state cases.

Most state oversight of charity deals with the solicitation of contributions. In the 1960s and 1970s, the desire to protect charities from “wasting” resources on fundraising led a total of 28 States and countless municipalities to impose ceilings on the percentage of annual revenues that could be spent on fundraising expenses. In the 1980s, however, a trio of Supreme Court decisions blocked these restrictions, on First Amendment free-speech grounds. To the Court, Procrustean percentage limits on fundraising disproportionately impact new charities (with low name recognition and no established donor base) and unpopular causes (which require a greater expenditure to raise a dollar). States may punish fraudulent fundraising speech after-the-fact, but, as the Court recently confirmed, regulatory approaches seeking to equate fraud with fundraising efficiency are invalid.

Conceding their inability to mandate fundraising limits, the states have concentrated their efforts on requiring charities to increase public disclosure using standardized forms. Almost all the states require registration and sometimes annual filings, usually with the attorney general, for charitable trusts and nonprofit corporations that solicit charitable contributions. Most laws also cover professional fundraisers, advisors, and co-venturers. (Thirteen states, though, require no charitable filings.) Statutes commonly exempt small entities, educational institutions, hospitals, and churches – and membership organizations – but variations abound. A charity soliciting in many states will welcome the Uniform Registration Statement accepted in most states requiring registration. (Some localities also regulate fundraising.)

2004).

30 Id. at 317 (identifying California, Mississippi, Minnesota and Oregon).

31 Professor Laura Brown Chisolm, of Case Western Reserve School of Law, is the reporter. The webpage for this project is www.nccusl.org/Update/CommitteeSearchResults.aspx?committee=305.


34 Version v3.20 (Dec. 2008) supports 37 jurisdictions (36 states and the District of Columbia), and includes supplemental forms required by some of these states. Go to www.multistatefiling.org. This form resulted from a joint project of the National Association of State Charities Officials, the National Association of Attorneys General, and the Multi-State Filer Program, a consortium of nonprofits.
B. Federal Tax Filings: Governance Focus of Redesigned Form 990

Not surprisingly, the Form 990 focuses largely on financial reporting and transactions – the Internal Revenue Service’s core competency is, after all, tax collection, which is measured in dollar amounts. The Form 990 is not limited to financial results, though, because it also has to reflect specific requirements and prohibitions in the tax laws. Thus we find many questions about relationships among fiduciaries and conflict-of-interest transactions, as well as questions about two additional concerns of federal tax exemption for charities: unrelated business activity and lobbying and political activity.

As a threshold matter, one key piece of data that has not been readily available is the organizational form of an exempt organization. By one count, of the active, filing public charities (that is, excluding small charities, churches, and private foundations), 552,524 are nonprofit corporations, 11,840 are trusts, and 119,354 are unincorporated associations. It has long been known that charities overwhelmingly are formed as nonprofit corporations, but are really only two percent charitable trusts? Even assuming private foundations are more likely than operating charities to be trusts (think of the Gates Foundation), this is a startling picture. Of course, it is likely that small exempt organizations (not required to file a Form 990) are disproportionately unincorporated associations (the least formal of organizational forms) or trusts (which can be easier to set up than corporations). Because of legislation adopted in 2006, the IRS will be able to clean up its Business Master File to weed out those nonfiling small charities that have simply ceased to exist. Effective for tax years beginning in 2007, small organizations that fail to file an annual notice of their continued existence (and minimal other information) for three consecutive years will have their exemption revoked.

With the overhaul of the Form 990 effective for tax years beginning in 2008, we will finally have information about organizational form for most public charities.

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35 Telephone conference with Margaret Riley, Statistician, IRS Statistics of Income Division (Aug. 3, 2007). A question about organizational form appears on the Application for Recognition of Exemption Under Section 501(c)(3) (Form 1023). Even more interesting, the numbers for section 501(c)(4) social-welfare organizations – which might or might not be state-law charities – break down as follows: 39,000 corporations; 338 trusts; and 66,297 unincorporated associations. Riley, supra.

36 Churches (and their integrated auxiliaries) and small public charities (generally, less than $5,000 in gross receipts) are exempt from having to apply for recognition of tax exemption under Code § 501(c)(3), and churches and most small public charities (generally, less than $25,000 in gross receipts) do not have to file the annual Form 990. The requirement to file an “e-postcard” – Form 990-N can be filed only online – applies to small charities, but not to churches. The new legislation additionally requires notification to the IRS when an exempt organization terminates its existence. See I.R.C. §§ 6033, 6652, and 7428, as amended by the Pension Protection Act of 2006 § 1223.

37 A simplified Form, the 990-EZ, is available for organizations having revenue and assets below
top of the new Form 990 asks the filer to identify the type of organization, with boxes provided for corporation, trust, association, and other (with space to describe). In a comment letter on the 2007 draft of the redesigned Form 990, I suggested adding such a question.\footnote{See Comment Letter from Evelyn Brody to IRS (Sept. 14, 2007), available at pages 24-28 of www.irs.gov/pub/irs-tege/redesignedform990commentsgeneral_9_14_07_i.pdf.}

The most striking feature of the 2008 redesigned Form 990 is the new first page that highlights key information set forth elsewhere on the form. This summary page will make the form more accessible to donors, the press, and state regulators – not to mention to board members themselves. The form also adds a full page of questions about organizational structure and governance practices.\footnote{See generally Elaine Waterhouse Wilson, More Than You Ever Wanted to Know (or Tell!): Heightened Compensation Disclosure on the New Form 990, 60 EXEMPT ORG. TAX REV. 273 (June 2008).} (See the Appendix for the draft and final versions of those two pages.) I strongly supported this focus on governance in my comment letter on the draft redesign. Indeed, I proposed replacing the draft half-page of questions with a full page of my own. As I explained: “It seems to me that most useful for the Service, potential donors, the press, and anyone else who reviews the Form 990 would be a series of questions that describe the governance structure of the organization and that determine whether the organization has in place procedures to support good governance.” I added: “At the same time, it is important to recognize that these organizations are private entities, whose obligation to make public disclosures must be based on the requirements of the Code. I agree with those who have urged you make clear – on the Form itself and not just in the instructions – which of these items are legally required, so that readers do not draw inappropriate adverse inferences.”\footnote{Brody comment, supra note 38.}

Part VI as finalized tracks many of my suggestions. In particular, it requires the disclosure of whether the organization has a voting membership; the identity of voting board members (and which ones are independent); whether and how certain documents, including the organization’s Form 1023, Forms 990, and 990-T, financial statements, governing documents, and conflict of interest policies, are made available to the general public; and whether the organization became aware during the year of an embezzlement or other material diversion of the organization’s assets.

But the governance-focused part of the Form 990, which Steve Miller, Commission for the Tax Exempt and Government Entities Division (TE/GE), characterized as “the crown jewel” of the IRS’s recent activity in the nonprofit governance area, has proven somewhat controversial. The Advisory Committee on Tax Exempt and Government Entities (the “ACT”), a high-level
advisory body to TE/GE, issued a lengthy report in June 2008 focused on the IRS role in charity governance. The 2008 ACT report comments:

> We believe in large part the governance questions on the redesigned Form 990 for 2008 are appropriate and formulated in a relatively neutral manner, recognizing that true neutrality is an unattainable goal. The inclusion of the questions, however, inherently (and intentionally) suggests that the IRS supports adoption of specific governance policies and practices. The danger then is that organizations will take the path of least resistance and adopt the policies and practices whether or not they are appropriate for them, or effective in their context.\(^{41}\)

The ACT concludes that the public availability of the Form 990 will induce organizations to adopt practices that they might not need, as discussed in Part I, above: “Thus, while disclosure and transparency play a valid role in promoting compliance with the tax laws and in encouraging appropriate nonprofit governance, they also can impact behavior in a manner that can be harmful to the sector, and inappropriately suggest to the public and watchdog groups that the absence of specific governance policies or practices is in effect misgovernance. Accordingly, the IRS should carefully consider the public disclosures it requires.”\(^{42}\)

**C. What’s Not Publically Available from Federal Tax Filings**

As thorough as the redesigned Form 990 appears, we still have reporting holes.

1. **Filing Exceptions**

   Churches and small charities are exempt from Filing the Form 990, as mentioned above; separately, the IRS is phasing in the new Form 990 by the size of the organization.\(^{43}\) Moreover, the filing threshold – currently set administratively at $25,000 of revenue – doubles to $50,000

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\(^{42}\) *Id.* at 29 (PDF at 115). The report cites to Dana Brakman Reiser, *There Ought to Be a Law: The Disclosure Focus of Recent Legislative Proposals for Nonprofit Reform*, 80 CHI.-KENT L. REV. 559 (2005).

\(^{43}\) For tax years beginning in 2008, an exempt organization with annual revenue of at least $25,000 but not more than $1-million and assets of less than $2.5-million can file the simpler Form 990-EZ. For the 2009 year, the cutoff drops to $500,000 of revenue and the assets of less than $1.25-million. For 2010 and later, the revenue breakpoint is $200,000 and the asset breakpoint is $500,000. See Internal Revenue Service, *Overview of Form 990 Redesign For Tax Year 2008* (Dec. 20, 2007), at 2, available at www.irs.gov/pub/irs-tege/overview__form__990__redesign.pdf.
beginning in 2010. Thus many organizations will shift from filing the Form 990-EZ to filing the e-postcard, Form 990-N, which requires only such basic information as employee identification number, the name of a principal officer, a mailing address, and confirmation that gross receipts total less than the threshold. In sum, we will continue to lack information on what churches are doing, and – although I am sympathetic to saving costs (both on charities and on regulators) for organizations that lack significant resources – we could lose valuable information on hundreds of thousands of small organizations. This latter issue is of particular concern to state regulators that accept the series Form 990 as its annual filing document.

2. Data on Form 990 That Are Unclear or Not Collected

Some of the ambiguities on the prior Form 990 will be cleared up by the redesigned Form 990. Consider the fundamental example of determining who is in charge of the organization – particularly who actually has power in those arts and cultural or educational institutions with multiple advisory positions (the proliferation of titles, like “life trustee,” are uninformative). While the draft redesigned Form 990 asked simply for a listing of trustees or directors, the final form makes clear that it is looking for those with voting rights only.

As another example, my comment letter to the IRS noted the tendency of too many expenses winding up on the “other” line, which allows for the itemization of specific categories not listed above. In the redesigned Form 990, Line 24 of Part IX (Statement of Functional Expenses) of the Core Form cautions: “Expenses grouped together and labeled miscellaneous may not exceed 5% of total expenses . . . .”

Problems of inaccurate or incomplete filings will continue. The push to electronic filing will help with the latter problem: The system will not accept a return unless the fields are properly filled in. As to the former problem, though, as Floyd Perkins, former Illinois charities bureau chief, commented, “People don’t realize how poor the quality is.” (See Part I, above, for a discussion of the pressures to fudge numbers.) He admitted, though, that there are “not a lot of examples where people relied on phoney reports.”

Is there a duty to amend return discovered to contain a material misrepresentation? The tax system imposes no statutory duty to amend tax returns, although filing an amended return stops the accumulation of penalties and interest (but for an exempt organization, interest on what?). By contrast, the federal securities law require amendment of a filing if failure to amend would be materially misleading. The possibility of state-level enforcement of an inaccurate

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44 Id.

45 Note Urban Institute studies showing a high percentage of Forms 990 are filled out by professionals. Fremont-Smith, supra note 29, at 457-58. Thus this is not a question of amateurs not knowing what they’re doing.
return, where the Form 990 satisfies the state filing requirement, can provide an incentive to file an amended Form 990 at both the federal and state levels.  

III. PUBLIC DISCLOSURE OF REGULATORY FILINGS AND DETERMINATIONS

The discussion in this Part III examines the privacy interests of charities and relevant third parties; reviews what types of state and federal filings are made public; analyzes the possible rationales for public disclosure; and addresses the transparency (or not) of charity regulators.

In the federal tax system as a whole, Congress’ overarching lodestar with regard to tax return information is confidentiality. While individuals and business are compelled to report their activities to the IRS, the IRS may not release taxpayer identifying information to the public—or even, except as specifically permitted by statute, to other governmental agencies. Indeed, a taxpayer may recover damages from the government for unauthorized disclosure, and severe penalties apply to IRS employees who improperly disclose return information. This presumption of confidentiality, however, is reversed for tax-exempt organizations. Why does Congress view sunlight in this context as an important disinfectant?

A. Privacy Interests of Charities and Their Supporters

By longstanding law and practice a charity’s governance activities and operations are generally private affairs. Requiring regulatory filings and other information to be disclosed to the public intrudes even more than does reporting to regulators on the associational and operational autonomy of charities, and might even make board service or employment less attractive. (Thus the title for the talk from which this Article derives: “Governing in a Fishbowl.”) Indeed, the most controversial portion of the IRS Form 990 – and the primary reason for initial resistance by

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46 For example, in 2004, the Pennsylvania secretary of state filed suit against nonprofits and their officers for 1,200 false Forms 990’s (also filed with the state). See Department of State, Commonwealth of Pennsylvania, Department of State Files Charges Against Four National Charities (Oct. 18, 2004), available at www.dos.state.pa.us/dos/lib/dos/press/pr-state-charities101804.pdf. In a settlement reached in 2007 in which four national charities agreed to pay $150,000 and to stop fund raising in Pennsylvania, the charities “acknowledged they did not report, among other things: H.R. Wilkinson as a key employee; related-party transactions; and marital or blood relationships among officers, employees, directors or members.” Commonwealth of Pennsylvania, Four Nonprofits Pay $150,000 Settlement, Agree to Halt Pennsylvania Solicitations (Oct. 29, 2007), available at www.dos.state.pa.us/dos/lib/dos/press/2007/10-29-07_charities_michigan_case.pdf.

47 See generally Code § 6103.

48 See generally Code § 6104.
exempt organizations to requests for public disclosure – is the section reporting board member and executive compensation. (Often, the organization’s own employees and volunteers are the most curious!) As discussed below, policy makers and observers have identified a variety of justifications for state and federally required public disclosures by charities, the levels and types of which seem only to increase. Importantly, the summary cover page of the Form 990 will highlight certain information for donors, the press, and state regulators – not to mention to board members themselves.

Privacy interests are broader than the charity’s, of course, and in certain situations public disclosure can lead to harm for the charity or to its donors, members, or those it serves. One category of sensitive information includes the types of trade secrets and personnel information protected from disclosure, as described below, by Freedom of Information laws. Narrower examples of sensitive information protected from disclosure include the address of a battered women’s shelter (so that abusers cannot find clients) and the countries of operation of human rights organizations (note that Schedule F of the new Form 990 was redesigned to address this concern). Public disclosure of membership lists also can be sensitive, particularly for groups advocating on socially contentious issues; usually, membership lists are not even required to be filed with regulators. Churches receive special protection by their exclusion from the requirement to file an application for recognition of federal tax exemption and Forms 990.

The identity of donors is an area of particular focus. The names of contributors to private foundation are not redacted from the Form 990-PF, which is required to be made publicly available in full. Donors to state-related nonprofit institutions, such as alumni-created foundations affiliated with state universities, are often unprotected as well.\(^49\) By contrast, Congress exempts from public disclosure the names of donors reported on the list of major donors (Schedule B) to the Form 990 filed with the IRS by exempt organizations other than private foundations. As one result, only the IRS can fully review a charity’s claim to be publicly supported, and thus not a private foundation.\(^50\)

**B. What Filings Are Subject to Public Disclosure?**

The states typically make available – often online – corporate annual reports filed with the secretary of state, and annual reports filed with the attorney general in those states requiring

\(^{49}\) See Brody & Tyler, *supra* note 16, at __. But see February 2010 legislative proposal in Wisconsin.

\(^{50}\) Under federal election laws, because of the enhanced public interest in open and fair elections, generally all but the smallest donors and amounts contributed to federal political campaigns must be identified (some states have similar “clean government” rules); this result leads some strategists to advise conducting issue-related advocacy through Internal Revenue Code § 501(c)(4) organizations. Issues relating to political activity and election law and regulation, including tax-law rules and filing requirements, are generally beyond the scope of this essay.
reports, generally from those who solicit charitable contributions (see Part II, above). Confidential information can be protected from public disclosure. Uniquely, as far as I know, New Jersey requires that the audit submitted to the attorney general be accompanied by the auditor’s management letter, if one was prepared, although the management letter will not be released to the general public. Material supplied in the course of or subsequent to a state investigation remains confidential except as might be required under a state freedom of information law.

Specifically, Code sections 6104 and 6110 provide for disclosing applications for tax exemption, including supporting documents, and determination letters and rulings. All of these items are available from the IRS upon request. Moreover, the organization must make its exemption application, supporting documents, and determination letter or ruling available for public inspection without charge. Separately, the law obligates a charity to produce any of its last three tax returns upon request. Posting the Form 990 on the charities’ website satisfies this obligation – but the posted return must be complete. Evidently, of greatest interest to the press, the public, competitors, and even other workers in the organization are the salaries and other compensation paid to the top executives and independent contractors, and a return provided without this information does not satisfy the disclosure obligation.

Even though the filings made with the IRS are available from the regulator (the same is true for some of the states), it is a private group that revolutionized charity transparency. The searchable database on GuideStar – itself a privately funded charity that works with the IRS and the National Center for Charitable Statistics at the Urban Institute – makes this whole system work. The IRS itself offers for sale (no cost to the media and other government agencies) scanned copies of the last seven years of filed Forms 990 on DVD or CD-ROM.

A training program by the IRS Exempt Organizations Division explains some of the advantages of instantaneous, online disclosure: “Obtaining information from an organization had potential drawbacks if a requestor and the organization were not on friendly terms. Despite the


Go to www.guidestar.org. Registration is required, but free, to see an organization’s last three years’ Forms 990, 990-EZ, or 990-PF, and other resources are available for modest fees. The website provides the following quick facts: organizations in the database: 1.7 million; nonprofits voluntarily providing information beyond their IRS listings: 127,000; total Form 990 images in the database: 3.7 million; visits to www.guidestar.org annually: 10.8 million; and total registered users: 1.2 million. See www.guidestar.org/about/index.jsp?source=dnabout.

requirements of the law, some organizations simply refused to allow access to their returns. That article provides “a discussion of the more common errors made and an explanation of the reasons for some of the information requested.” (Regrettably, in 2005, the EO division discontinued drafting these training materials, which has been a great loss to practitioners as well as to the Exempt Organization staff.)

Some information sill remains private between the organization and the tax collector. The statute excludes from public disclosure the customary FOIA exceptions for “a trade secret, patent, process, style of work, or apparatus if the Service determines that the disclosure of the information would adversely affect the organization.” In addition, as mentioned above, Schedule B to the Form 990, on which public charities report the identities of their large donors, is disclosable only if the organization releases it. Exemption applications are not public until exemption is granted; nor must withdrawn applications for exemption be disclosed.

Finally, the Pension Protection Act of 2006 requires an exempt organization to make public its Form 990-T, on which it reports and pays any tax due on unrelated business taxable income. However, Congress did not impose a parallel requirement on the corporate returns of an exempt organization’s taxable affiliates (business tax returns, like the returns of individuals, are not public documents), giving charities one more reason to spin off unrelated businesses into a separate for-profit corporation. Unfortunately, because of a glitch in the statute, the IRS cannot provide the Forms 990-T to GuideStar, so anyone curious about unrelated business activity of a particular charity will have to ask the organization for the form, and there will not be a searchable database of these forms.

1. Applications for exemption – Form 1023.

The application form used to file for recognition of federal tax exemption under section 501(c)(3) was significantly revised in 2004. The 2008 ACT report on the IRS role in charity governance described the evolution of the IRS’s approach to governance during the exemption


57 The current version, revised in 2006, is available at www.irs.gov/pub/irs-pdf/f1023.pdf. It would be great if GuideStar would collect and post Forms 1023 once exemption is granted. The Forms 1023, especially the ones filed electronically, could provide an interesting database for study.
application process: “While the Form 1023 prior to the current version asked questions regarding organization structure and governance, it principally focused on the charitable activities of the organization. In contrast, the 2004 (the most current) version places an increased emphasis on an organization’s governance by focusing on board and management relationships (independence) as well as compensation and other potential opportunities for inurement.”

Commentator Jack Siegel praised the IRS for “attempting to identify those organizations that are likely to violate the rules governing Section 501(c)(3) organizations before granting tax-exempt status rather than relying on an audit process that is currently underfunded and spotty.” However, Siegel cautions future applicants for exemption:

Those who want to abuse tax-exempt status should be very careful when filling out this form. The questions are designed to highlight abusive plans. In the past, questions covering compensation, grant making, affiliations, and activities were very open-ended, permitting people who wanted to game the system to conveniently omit information without significant risk. The 2004 revised Form 1023 touches on all the same topics, but with very specific questions which will make it much more difficult to hide abusive arrangements without risking penalties of perjury. Those applicants who have a legitimate claim to exemption should have nothing to worry about if they answer the questions fully. Hopefully the revised form will deter some unscrupulous taxpayers from even entering the tax-exempt system.

Siegel adds: “We also suspect that certain answers to questions may not cost an organization its requested exempt status, but may place the organization in a special queue for subsequent audits focused on potential violations under the intermediate sanctions.”

Of course, failure to make full disclosure on the prior versions of the application form – which, like the Form 990, is filed under penalties of perjury – still had consequences. In an unusual but alarming case, the United States recently won a criminal conviction against a Muslim group that had failed to disclose on its Form 1023 what the Justice Department asserted were such terrorist activities as publishing newsletters and raising funds for jihad.

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58 ACT, supra note 41, at 32-33 (pages 18-19 of the PDF) (footnotes omitted).


60 Department of Justice Press Release, Former Officers of a Muslim Charity, Care International, Inc., Convicted (Jan. 11, 2008), available at www.usdoj.gov/opa/pr/2008/January/08_nsd_021.html:

In June 1993, MUNTASSER sought a tax exemption for Care International from the IRS
2. Forms 990: problems of accuracy and timeliness

Like other federal tax returns, the Forms 990 are self-reported. Many as filed contain errors, some materially misleading. Hopefully, compliance will improve as boards and top management become more involved in preparing the form. Even with the redesign, though, this document cannot provide much insight into the nature and quality of charity activities.

Moreover, many Forms 990 are filed under an automatic six-month extension. The blame for this commonly falls on the accountants, who can barely recover from having to prepare tax returns for individuals (due April 15) before gearing up to file Forms 990 (due May 15, for calendar-year organizations). No reputational sanction seems to follow from filing late, so many calendar-year exempt organizations file close to November 15. (You can tell because of all the news stories on nonprofit compensation that appear around Thanksgiving.) This means that events that occur in, say, January 2007 will likely not be disclosed to the public until November 2008, almost two years later.\footnote{61}

The IRS highlights the value of disclosure in describing its e-filing initiative: “Electronic filing is quick, secure, and more accurate than filing a paper return . . . E-filing reduces normal processing time and makes compliance with reporting and disclosure requirements easier.”\footnote{62} Indeed, e-filing is mandatory for large charities: “For tax years ending on or after December 31, 2006, the electronic filing requirement applies to exempt organizations with $10 million or more

pursuant to 26 U.S.C. §501(c)(3) on the basis that Care International was an exclusively charitable organization. On behalf of Care International, MUNTASSER executed, under the penalties of perjury, an IRS Form 1023 Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code (“1023 Application”). Although instructed to describe all current and proposed activities of Care International, when MUNTASSER completed this application, he did not disclose Care International’s current activities involving the promotion of jihad through the distribution of the [newsletter] Al-Hussam. Nor did he disclose an intention for Care International to solicit money for jihad or the mujahideen or to promote jihad and the mujahideen through the distribution of publications. . . .

But see Jonathan Saltzman, \textit{Former Head of Islamic Charity Freed in Fraud Case}, \textit{Boston Globe}, June 4, 2008, reporting: “A federal judge yesterday freed a former leader of a defunct Boston-based Islamic charity and set the stage to soon release another official from the group, after ruling that a jury should not have convicted them in January of most of the tax-related crimes for which they were tried.” The court set aside the conviction of Samir Al-Monla “of conspiring to defraud the United States and of scheming to conceal the origins of the tax-exempt charity, Massachusetts Care International Inc., which allegedly published newsletters promoting jihad and supporting Islamic militants overseas.”

\footnote{61} Mancino proposal: Report compensation currently and on annual 990 – cf. SEC quarterly filings.

in total assets ($100 million in 2005) if the organization files at least 250 returns in a calendar year, including income, excise, employment tax and information returns. . . . . Private foundations and non-exempt charitable trusts will be required to file Forms 990-PF electronically regardless of their asset size, if they file at least 250 returns annually.”65 Beginning in 2006, the Service started a federal/state filing system, and has begun working with individual states to test their systems.64 According to the EO Update 2008-12 (August 20, 2008),65 the Service has received the following numbers of electronically filed forms between January 1 and August 17, 2008: 33,791 Forms 990; 7,306 Forms 990-EZ; 152,137 Forms 990-N (the “e-postcard” for small charities, which can only be filed electronically); and 4,424 Forms 990-PF.66

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63 Id.

64 See also GuideStar’s service: “Gov@GuideStar offers a suite of tools designed specifically for government users of GuideStar data. These research and reporting tools enable government decision makers to perform critical tasks with greater ease and confidence.”

65 Available at www.irs.gov/charities.


The accuracy of the Business Master File will hopefully improve with the new filing requirement imposed on small organizations. Specifically, the numbers could drop precipitously as the Business Master File adjusts to reflect the requirement beginning after 2006 that small exempt organizations file an annual notice of their continued existence (and minimal other information). Failure to file either a series Form 990 or this notice for three consecutive years will result in revocation of exemption, unless the organization sooner notifies the IRS when it terminates its existence (as it should do). See I.R.C. §§ 6033, 6652, and 7428, as amended by the Pension Protection Act of 2006 § 1223. For guidance, see New Electronic Filing Requirement for Small Tax-Exempt Organizations – Annual Electronic Notice – e-Postcard (Form 990-N), www.irs.gov/charities/article/0,,id=169250,00.html, with a link to frequently asked questions. As explained in Q.2, Form 990-N must be filed electronically. As explained in Q.11, an organization “must apply (or reapply) and pay the appropriate user fee to have your tax-exempt status reinstated if it was revoked because you failed to file for three consecutive years. Reinstatement of tax-exempt status may be retroactive if you can show that you had reasonable cause for not filing. . . .” (Note, however, that there is no penalty for late filing of Forms 990-N.) Assuming this process works smoothly, it will clarify whether the many “missing” Forms 990 and 990-EZ, are attributable to small size, oversight, charities that ceased activities, or double-counting.

Complicating the headcounting, it turns out that the IRS is receiving more e-Postcards than
C. Rationales for Governmentally Mandated Disclosure to the Public

This subpart considers four possible rationales for mandating public disclosure of charity finances and other activities.

1. Disclosure without judgment: “disclose or abstain”

While, as mentioned above, the tax returns of businesses are confidential, in regulating the securities issued by publicly traded companies, Congress adopted a “disclose or abstain” model in lieu of much prescriptive regulation. Under such an approach, in general, if the issuer is honest (i.e., not materially misleading), we leave it to the market to make investment decisions. If we adopt this disclosure rationale for charity regulation, what are nondisclosing nonprofits supposed to abstain from? Soliciting the public for contributions (state registration model)? Something else? After all, the typical private foundation or government-funded agency is not seeking or expecting contributions from the public. Interestingly, Congress required private foundations to make their Forms 990-PF available on request in 1969, but did not obligate publicly supported charities to make their Forms 990 available until 1987.

2. Condition of tax subsidies

Is the rationale for public disclosure instead that the “public” benefits through providing support for tax subsidies, and therefore tax filings should be made public? (Generally, imposing requirements conditions on tax-exempt status does not give rise to the argument of “unconstitutional conditions,” because exemption is not a constitutional right.67) In 2000, the staff of the Joint Committee on Taxation released a congressionally-mandated study of the disclosure rules in the tax system, devoting a full volume to those that apply to exemption organizations.68 The Joint Committee called for increased public disclosure of exempt-

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expected. The IRS identified 640,000 potential e-Postcard filers in its database, and mailed survey questions to each of them; based on survey results and historical filing patterns, it expected 166,000 e-Postcard filers. EO Annual Report and Work Plan 12 (Nov. 2008), available at www.irs.gov/pub/irs-tege/finalannualrptworkplan11_25_08.pdf. By the end of September 2008, 167,000 Forms 990-N had been filed. Id. Evidently, the IRS is getting filings from organizations too small to have ever had to file an exemption application (and thus do not appear on the Business Master File). The only exception from having to file the e-Postcard is for organizations that do not have to apply for recognition of exemption because they are churches or their integrated auxiliaries.


68 U.S. Congress, Joint Committee on Taxation. 2000. Study of Present-Law Taxpayer Confidentiality and Disclosure Provisions as Required by Section 3802 of the Internal Revenue Service
organization information, including the release of (1) complete private letter rulings and technical 
advice memoranda, without redaction of information identifying the entity and its transaction; (2) 
the results of all audits of tax-exempt organizations, also without redaction; (3) applications for 
exemption, not just exemptions once issued; (4) Forms 990-T (unrelated business income tax) 
and the returns of taxable affiliates; and (5) a description of lobbying activities, and amounts 
spent on self-defense lobbying and on nonpartisan research and analysis that includes a limited 
“call to action.” Many of the Joint Committee’s recommendations attracted strong criticism. As 
mentioned above, Congress now requires disclosure of Forms 990-T (but not the returns of 
taxable affiliates); and as discussed below, the IRS must release determination letters denying or 
revoking exemption, although in redacted form.

The Joint Committee asserted the following rationale for public disclosure: “Disclosure 
of information regarding tax-exempt organizations also allows the public to determine whether 
the organizations should be supported – either through continued tax benefits or contributions of 
donors – and whether changes in the laws regarding such organizations are needed.” That is, 
informing potential donors is one aspect, but only one, of this rationale. Just as important is 
allowing the public to judge the legitimacy of tax-exemption, and whether it should be altered.

3. Condition of nonprofit (specifically, charitable) status

The Independent Sector, a leading trade association of charities, proposed an alternative 
rational for transparency. In commenting on the Joint Committee’s 2000 report, the Independent 
Sector declared: “IS believes that charities’ public disclosure obligations derive from charities’ 
fundamental nature as voluntary associations formed by private citizens to advance the public 
good – not from charities’ receipt of favorable tax treatment.” After all, the Independent Sector 
oberved: “Charities were recognized as separate entities with legal rights and responsibilities 
long before there was a federal income tax code. The need for disclosure stems from charities’ 
unique social role. A charity must be transparent enough to make donors, volunteers, and 
partners confident that the charity will, in fact, advance public rather than private interests.”

Organizations. JCS-1-00, Jan. 28. Available at www.house.gov/jct/s-1-00vol2.pdf. Pages 89-90 of the 
report provide a background to Form 990 public disclosure.

69 See Grant Williams, Tax Report Shakes Up Charities, Chron. of Philanthropy, March 9, 
2000.

70 Independent Sector Comments on Joint Committee on Taxation Study on 
Disclosure by Tax-exempt Organizations 3 (no date), available at 
www.independentsector.org/programs/gr/Comments.PDF.

71 Separately, the Independent Sector “[took] issue with the JCT Report’s characterization of tax 
exemption and the charitable deduction as government subsidies and the Report’s view that the receipt of
As a general comment, the Independent Sector challenged the utility of counting on the Form 990, as it existed then, as the vehicle of informing the public:

Without an understandable user’s guide – and no such guide exists – the public derives little benefit from much of the information already reported by charities. Thus, there is a deep need for tools to help the public understand the information that is already disclosed. We believe that oversight of the charitable sector by both the government and the public could be dramatically improved by revising the Form 990 so that it highlights critical information and facilitates the reader’s understanding of the significance of the information being presented. A top priority for the IRS in this regard should be providing, either directly or through nongovernmental intermediaries, on-line access to all Forms 990.\(^{72}\)

4. We can’t think of a better alternative

Finally, we have to admit the possibility that we rely on public disclosure because we don’t know what else to do (or who should do it). Betsy Adler nicely summarized the current regulatory approach with the acronym “FED”: “funding, enforcement, disclosure.”\(^{73}\) In our laissez-faire system, we don’t want government telling charities what to do and how to do it.\(^{74}\) The absence of shareholders goes to why we disclose to regulators: Public disclosure seems driven by regulators’ lack of resources, expertise, or inclination.

Nor should we sell short the ceremonial value of sunshine. Public disclosure – even in the absence of enforcement action or other repercussions – is useful because knowing that information will be disclosed induces the fiduciaries to pay more (and better) attention not just to how they report, but also to what they do. At the same time, this leads to the possibility of fudging the reporting due to the pressures described in Part I. As the 2002 CPE text commented:

\(^{72}\) Id. at 8. A few year’s later, however, the IRS included in its 2003 Exempt Organization Continuing Professional Education text a great set of Q&A’s on how to fill out (and therefore read) the Form 990. Go to www.irs.gov/pub/irs-tege/otopich03.pdf.

\(^{73}\) Oral comment of Betsy Adler, then-chair of the Exempt Organizations Committee of the American Bar Association Tax Section, Senate Finance Committee Staff Roundtable (Washington, D.C., July 22, 2004) (author’s notes).

Several things must happen in order for this increased disclosure of Form 990 to be of maximum benefit to the public. First, the information entered on Form 990 must become more standardized and reliable. Second, potential users of the data must become more familiar with the requirements for proper completion of the return so that they will understand the data they are viewing. The Service itself will benefit if these things occur. Public disclosure promotes accountability and discourages inappropriate activities which, in turn, enhances voluntary compliance and thereby assists the IRS in the administration of the tax law.\textsuperscript{75}

D. Disclosure of State and Federal Enforcement Activity

1. What are the states doing?

It is not easy to figure out how to spur nonprofit board members into performing better. Increasing monetary sanctions might make things worse: Indeed, we might improve nonprofit governance by \textit{reducing} what’s at stake. In large part regulators are so timid (at least publicly) because they don’t want to discourage volunteers acting in good faith. As a result they don’t send a sufficient signal (at least publicly) of the problems they encounter on nonprofit boards. In my project for the American Law Institute, I suggest:

[T]hese Principles support a higher level of appropriate activism by charity regulators and the courts in crafting nonfinancial remedies to wayward fiduciary behavior. Application of these Principles could lead to increased settlements and injunctions mandating governing board and management training, and adoption of “best practices” policies and procedures; removal of fiduciaries; and even the closing down of charities and the transferring of assets from charities that will not adopt and follow appropriate safeguards to those charities that will.\textsuperscript{76}

But lack of transparency in their regulation of charities makes it impossible to assess the effectiveness of regulators in improving charity governance – or even whether they are acting at all. Few cases involving nonprofit fiduciary issues have reached the courts. Reform rather than punishment is generally the goal of the charity regulator, and charities as well prefer a chance to improve their behavior while avoiding embarrassment and personal liability. Most settlements are kept confidential. Finally, state attorneys general can act – or not act – out of parochial and political motives.\textsuperscript{77}

\textsuperscript{75} Chasin, et al., \textit{supra} note 53.

\textsuperscript{76} ALI, \textit{supra} note 5, at Introductory Note to Topic 2 (Remedies for Breach of Fiduciary Duties).

Regulators have limited (financial and political) resources. In that case, we might expect attorneys general to publicize their enforcement actions in order to benefit from the leveraging effect – miscreants in a similar position would recognize themselves in the press release, and voluntarily straighten out. Indeed, attorneys general do trumpet cases in which they catch someone violating the law. In other cases, where there’s no real “bad guy” – but rather well-meaning fiduciaries caught in governance failures – I’d be satisfied if states would issue aggregate annual reports on the types of enforcement activities they undertook and outcomes achieved.

On a related note, I have observed with frustration that even the limited official reporting of enforcement activity tends to have a short shelf-life. Press releases often vanish from attorney general websites when a new attorney general comes into office, thus undercutting the educational and deterrent value of publicizing enforcement actions.

Moreover, as recently as 2004, the Massachusetts attorney general maintained on the charities webpage an extremely helpful “Final Judgment Database” of legal actions, with links to the specific cases. As then described on the website: “The Public Charities Division has developed the database below to give the public information about the settlements and final court orders obtained by the Division over the past twenty years. These settlements and court orders have arisen out of legal actions taken against fundraisers who were allegedly raising charitable funds as well as actions taken against charities.” Alas, this database has disappeared into the ether.

Hope may be on the way. In 2008, the Charities Law Project at Columbia Law School began developing a website to assist attorneys general in fulfilling their responsibilities over

78 Id. Garry Jenkins conducted a survey, to which all but one of the states responded, finding that 79 percent of the states had one or fewer full-time-equivalent attorneys devoted to charitable oversight, and that 17 states assigned no attorneys to that function. Garry W. Jenkins, Incorporation Choice, Uniformity, and the Reform of Nonprofit State Law, 41 GA. L. REV. 1113, 1128-29 (2007). Legal staffs exceeding 2.5 FTE’s are found in California (12), Connecticut (5), Illinois (7), Indiana (4), Massachusetts (6), Minnesota (5), New York (20.5), Ohio (10), Pennsylvania (12), Texas (6). Id. at table 1.

79 (Recall Dr. Strangelove’s complaint: “Deterrence is the art of producing, in the mind of the enemy, the fear to attack. The whole point of the Doomsday Machine is lost if you keep it a secret! Why didn’t you tell the world, ay?!”) See www.uselessmoviequotes.com/umq_d010.htm.

80 Then available then at www.ago.state.ma.us/sp.cfm?pageid=1218.

81 The database was divided into four categories, assurances of discontinuance; final judgment by consent; final judgment by default; and final judgment.
charitable assets. As explained on the Charities Law Project’s home page:

> The Project is a resource to Attorneys General in three ways. First, Attorneys General who find themselves in need of external advice or direction on a charities issue can receive it from the experienced Project staff. . . . Second, a clearinghouse for information relating to the law of charities is being created. The clearinghouse will contain articles and papers on charities law generally, as well as Attorneys General enforcement activities and best practices. Third, the Project will convene forums at which Attorneys General and their staffs will hear about and discuss what other offices have done and are doing to protect their citizens and their states’ charitable assets.

Although a separate intranet just for attorneys general might be created, so far all of the posted material is available to the public. The clearinghouse contains links to state and IRS websites (and specifically to state best practice guides) and summaries of law review articles. No enforcement materials have been posted yet, but a few recent settlements from around the country are available through links to materials for a panel on remedies presented at the March 2008 conference.

2. IRS determination letters denying or revoking exemption

Because there’s no other place to say it, let me mention here that despite the Service’s fearsome reputation, it is as resource-constrained as the states. IRS Exempt Organizations Division Director Lois Lerner commented in June 2008 that the IRS has only 800 staff members assigned to the oversight of 1.7 million tax-exempt entities, and that seven managers in the Examinations branch will retire this year.

Throughout the tax-practice world, practitioners and their clients have long benefited from the public availability of redacted versions of private letter rulings, audit memoranda, and other taxpayer-specific agency positions. Marion Fremont-Smith explains how this type of transparency can improve tax administration in general. “Members of the bar were also able to identify issues needing study or revision, and call these to the attention of the Service as a group

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82 Go to www.law.columbia.edu/center_program/ag/CharitiesProj/.

83 Go to www.law.columbia.edu/center_program/ag/CharitiesProj/conference#131135.

84 Christopher Quay, Redesigned Form 990 Might Lead to New Compliance Projects, 119 Tax Notes 1223 (June 23, 2008).

85 The IRS did not agree to give out this information lightly. It took a series of Freedom of Information Act lawsuits by Tax Analysts, publisher of Tax Notes magazine and the Exempt Organization Tax Review.
The Service, however, long refused to release redacted determination letters relating to denial or revocation of tax exemption. In a milestone decision issued in 2003, however, the District of Columbia Circuit held “that the portions of Treasury regulations sections 301.6110-1(a) and 301.6104(a)-1(i) that include denials and revocations ‘within the ambit of section 6104’ and prevent their disclosure violate section 6110’s plain language.”

In annual revenue procedures, the Service set forth the process for issuing determination letters and rulings on exempt status, both in response to applications for recognition of exemption and in cases of revocation or modification of determination letters or rulings. Section 8 of the revenue procedure describes the rules for disclosure. Notably, “[u]pon issuance of the final adverse determination letter or ruling to an organization, both the proposed adverse determination letter or ruling and the final adverse determination letter or ruling will be released under section 6110” . . . “after the deletion of names, addresses, and any other information that might identify the taxpayer”, as set forth in Code section 6110(c). Importantly, section 6104 applies only to material furnished by the organization or issued by the IRS, and not to

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86 Fremont-Smith, supra note 29, at xiv.

87 Tax Analysts v. Internal Revenue Service, 350 F.3d 100, 104-05 (D.C. Cir. 2003). The court described the legislative history:

. . . Congress passed the Tax Reform Act [of 1976] to protect taxpayer privacy while requiring the IRS to disclose written determinations. Our holding advances that purpose: the IRS must disclose determinations denying or revoking tax exemptions, but do so in redacted form, thus protecting the privacy of the organizations involved. The Treasury regulations, in contrast, keep denials and revocations completely secret, preventing the very monitoring of the IRS that the Tax Reform Act was designed to facilitate. See . . . [legislative history] (explaining that the Tax Reform Act of 1976 would require the IRS to disclose written determinations because “the secrecy” surrounding those documents, in particular IRS rulings, had “generated suspicion that the tax laws [were] not being applied on an even-handed basis” and because disclosure would “tend to increase the public’s confidence that the tax system operates fairly”).

Id. at 104.

88 (July 9, 2007).


90 Because a closing agreement is a “bilateral agreement signed by both IRS and taxpayer,” it was “not issued by” the IRS and thus was not subject to the clause of Code § 6104(a)(1)(a) making disclosable information issued by IRS with respect to organization’s application for tax-exempt status. Tax Analysts v. Internal Revenue Service, 2004 U.S. Dist. LEXIS 28032, 93 AFTR 2d 1250, n.2 (D.D.C.
settlement agreements (termed “closing agreements”) between the IRS and the organization unless the organization consents.91

These redacted denial and revocation letters began to appear in 2004. An early redacted denial letter was issued to a recreation center in which the Service found an inbred governance structure not likely to ensure public benefit:

Since all three members of your original board were related and receiving compensation, we asked you to expand your board of directors by three to four non-related members of the community. [You added three new members.] Three members of your board of directors are the founding family members who hold the position of President, Vice President, and Secretary/Treasurer. At the present time these directors receive a total combined compensation of * * *. The file does note indicate that the current board will put the organization’s exempt interests above the interests of the three related board members.

. . . A full copy of your approved bylaws have not been received by the Service. The limited information provided indicates that the * * * may appoint and remove the directors. The * * * appear to be the three related directors.92

Incidentally, when faced with the prospect of a denial, why doesn’t the applicant simply withdraw the application (this would not be a disclosable event)? Evidently, the denial letters are for groups that want judicial review, and the determination letter is the ticket to court.

With the continued issuance of denial and revocation letters, we have seen a flood of up to a dozen a week, adding up to hundreds a year. An adverse ruling generally falls into one (or more) of three categories: private benefit, “commerciality,” with, most recently, the return of the ground that the charity failed to conduct a charitable program “commensurate-in-scope” with its

2004), citing to prior decision at 53 F. Supp. 2d 449, 452-53 (D.D.C. 1999). This litigation ended when the D.C. Circuit upheld the district court’s refusal to compel the Service to disclose the closing agreement referred to in a press release issued by the Christian Broadcasting network.

91 The IRS Chief Counsel’s office recently issued a notice to its attorneys of the procedures to follow “when advising Internal Revenue Service employees concerning a determination that publicizing a closing agreement between a taxpayer and the Internal Revenue Service advances tax administration.” When “[t]here are occasions in which the Service and a taxpayer agree that public disclosure of a closing agreement (or any of its terms), which resolves a particular tax matter, is warranted[,] in general, the public disclosure would be through an IRS news release, or a jointly authored statement, which would be released at the time the closing agreement is executed.” Chief Counsel Notice CC-2008-014 (April 14, 2008).

resources. The Service has denied exemption to nonprofits engaged in a variety of activities including adoption, insurance, financial services, religious publishing, conference centers, low-income housing, and retreats for caretakers – generally on the basis of their resemblance to similar for-profit businesses. Examples of recent determination letters with governance implications include the following, as summarized in the 2008 ACT report:

PLR 200736031 (Dec. 7, 2006) (noting that married couple were sole officers and directors, there was no conflict of interest policy and couple did not recuse themselves when causing organization to contract for management services with for-profit company of which husband was sole shareholder); PLR 200535029 (June 9, 2005) ("Finally, despite the expansion of your governing board from three (3) to five (5) members, and the enactment of a conflict of interest policy, we still have some concern that your actual operations will be controlled and directed by B and his daughter C. We acknowledge that there is no evidence of any inurement to the benefit of these individuals, but then there has been no financial activity on your part to date."); PLR 200514021 (Jan. 13, 2005) ("There seems to be great likelihood of inurement to these individuals in that they all serve on the Board of Directors, and have a vote on compensation arrangements, leasing arrangements, and other financial matters that would affect the organization’s financial interests as well as their own. This situation gives rise to an inherent conflict of interests that would potentially, adversely impact the financial well being of the organization. Thus, you have failed to show that B, C, D and E, through their positions on the Board, would not benefit from inurement…."); PLR 200510031 (Nov. 15, 2004) ("There is not even one outside, disinterested board member to speak for the community. We must conclude that you violate the second fundamental rule for exempt organizations, and operate for private, not public benefit.")

Unfortunately, the IRS website makes these determination letters available only as part of its general release of all determination letters. Given how many of these determination letters we now have, and how cumbersome the process is of reviewing them, the Service – or another institution, with either public or private funding – could usefully collect and sort these

93 ACT, supra note 41, at 34, n.116 (page 120 of PDF).
94 Go to www.irs.gov/foia/lists/0,,id=97705,00.html. While the website makes it possible to sort determination letters by something called the UIL number, the letters are coded in obscure and unhelpful ways. For example, UIL 501.06-02 begins helpfully, under Code section 501, but “06-02” means “Conduct of Business for Profit.” This category is to be distinguished from “501.06-02 Conduct of Business for Profit.” And what to make of “501.03-30 Organizational and Operational Tests” and “Profit v Not for Profit”? Moreover, categorical assignments do not seem to be made with great care. For example, Determination Letter 200634046 (Aug. 25, 2006), available at www.irs.gov/pub/irs-wd/0634046.pdf, which involves a nonprofit corporation that lost its exemption on grounds of private inurement, is filed under “501.03-04 Unincorporated Associations.” Of course, no single category is going to be helpful when the reasons for revocation are manifold.
documents. The easiest way to find specific issues in these letters is to search a commercial electronic database, such as LEXIS or Westlaw.

Even when one can find a particular determination letter, the redactions are simple elisions. As with all private rulings and memoranda, the redactors make no effort to give a sense of the substance underlying the facts. Thus, we get such baffling indications as “$j” or “$ * * * ” rather than, say, orders of magnitude, percentages, or relationships that would give a sense of the materiality of the problem.

The steady stream of denial and revocation letters has allowed the Service to “informally” stake out positions on basic substantive issues such as whether a particular activity is eligible for exemption. For example, it is understood that the Service demands a minimum of three

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95. Leading practitioner and author Bruce Hopkins maintains a collection of citations, organized by the reason for denial or revocation (or for continued exemption), at www.nonprofitlawcenter.com/Resources.jsp?docId=117.

96. In the case of private rulings, the redactors, in the first instance, are the requesting taxpayers themselves.

97. In comments on the Joint Committee’s 2000 disclosure study, the Independent Sector “strongly oppose[d],” among other JCT recommendations, those that would require the Service to make unredacted disclosure of written determinations and related file documents, closing agreements and audit results, exemption applications at the time of filing, and Forms 990-T (for its unrelated business taxable income) and 1120 (of any affiliated organizations of tax-exempt organizations). The Independent Sector supported, assuming technical refinement, giving greater flexibility for IRS information sharing with state charity regulators, a proposal enacted in the Pension Protection Act, as described below.

98. For example, in a 2008 letter denying recognition of tax-exempt status under § 501(c)(3), the IRS set out “12 specific conditions” for recognizing an LLC under the organizational test of section 501(c)(3); while the letter cited no authority for these conditions, they appear in McCray & Ward L. Thomas, Limited Liability Companies as Exempt Organizations – Update, IRS Exempt Organizations Continuing Professional Education Text for FY 2001, at www.irs.gov/eo. (In the case at issue, the sole member of the LLC was an individual, and the articles of the organization provided that the member was entitled to distributions; the letter also ruled that the LLC failed to meet the operational test.) Determination Letter 200827041 (April 10, 2008, released July 4, 2008), states that “[t]he Service will recognize the section 501(c)(3) exemption of an LLC that otherwise qualifies for exemption if it satisfies 12 specific conditions. . . .” These include: “c. The organizational language must require that the LLC’s members be section 501(c)(3) or (c)(4) organizations or governmental units or wholly owned instrumentalities of a state or political subdivision thereof”; “h. The organizational language must prohibit the LLC from merging with, or converting into, a for-profit entity”; “j. The organizational language must contain an acceptable contingency plan in the event one or more members ceases at any time to be an organization described in section 501(c)(3) or a governmental unit or instrumentality”; and “k. The organizational language must state that the LLC’s exempt members will expeditiously and vigorously enforce all of their rights in the LLC and will pursue all legal and equitable remedies to
unrelated board members, although, because such a requirement does not appear in the statute or regulations, the Service cannot deny exemption on this basis alone. The 2008 ACT report comments: “We were not able to find guidance as to how the IRS takes governance issues into account in the determination process, except in limited instances in the health care and low-income housing joint venture areas. We certainly appreciate that governance can bear on the operational test, among other issues. Our personal experience and research for this report suggest, however, that the IRS may require specific governance practices on an ad hoc and inconsistent basis.” The Report cites two illustrations: “[D]etermination specialists may require organizations seeking exemption to have independent boards or at least some independent board members. Similarly, despite the fact that the Form 1023 specifically states that a conflict of interest policy is recommended but not required, our experience and interviews suggest that determination specialists often require adoption of such a policy, and occasionally require adoption of the sample form of policy included with the Form 1023 instructions.”

99 Note, as the 2008 ACT report, adds: “There typically is no public record where taxpayers agree to make the changes required, strongly urged, or recommended by the IRS in the determination process and receive an exemption; or where an application is withdrawn.”

The ACT concludes: “We appreciate we have only anecdotal evidence regarding governance issues in the determination process. It is, however, our impression that the ‘when’ and ‘what’ are unclear and not uniformly applied. We are concerned about the IRS having this level of discretion in cajoling or requiring specific governance process, particularly in the determination phase, where there usually is no track record evidencing operational failures. Now, six years on, it is time for the Service to take this substantial database of published denial and revocation letters and use it to develop formal guidance. While the Service has published a revenue ruling on housing down-payment assistance organizations, and while Congress has backed up the Service’s position on credit-counseling agencies, many evidently routine positions on governance structures and practices remain unformalized. The sector is entitled to revenue rulings or even regulations setting forth the Service’s positions on organizational and operational issues, including nonprofit governance, that jeopardize exempt status. Such

99 ACT Report, supra note 41, at 3 (page 89 of the PDF).

100 Id. at 33 (page 119 of the PDF).

101 Id. at 3 (page 89 of the PDF).


103 I.R.C. § 501(q), added by the Pension Protection Act of 2006.

104 See, for example, Fred Stokeld and Sam Young, IRS Pursuing Excess Benefit Transactions
guidance would allow the Service to provide examples that show specific or relative dollar amounts and other facts masked by the redaction process.

3. Disclosure from IRS to state attorneys general

Amendments to Code section 6104 in the Pension Protection Act of 2006 broadened the authority of the Internal Revenue Service to provide certain information to state charity regulators, especially regarding exemption applications and denials. As described in Revenue Procedure 2010-9:

.03 The Service may notify the appropriate State officials of a refusal to recognize an organization as tax-exempt under section 501(c)(3). See section 6104(c) of the Code. The notice to the State officials may include a copy of a proposed or final adverse determination letter or ruling the Service issued to the organization. In addition, upon request by the appropriate State official, the Service may make available for inspection and copying the exemption application and other information relating to the Service’s determination on exempt status.105

Separately, the Service “may disclose to State officials the name, address, and identification number of any organization that has applied for recognition of exemption under section 501(c)(3).”106 The Pension Protection Act extends to those state charity officials the section 6103(a) obligation to protect the confidentiality of the taxpayer information it receives.

In January 2008, the Service issued a notice explaining: “Returns and return information shall not be disclosed under this subsection or any of the aforementioned proceedings, to the extent that the Secretary determines that such disclosure would seriously impair Federal tax

Involving EOs, Tax Notes, Sept. 25, 2006, at 1117:

“Marvin Friedlander, Exempt Organizations technical manager, TE/GE, . . . reported that the IRS has received applications from organizations that purchase health insurance on behalf of the working poor at group rates and charge a fee for that service. . . .

‘We have been unable to find an alternative basis for exemption when the demo phase ends, because these programs are not limited to a charitable class and seem too commercial,’ Friedlander explained. ‘We are taking a fairly hard-nosed line: approving the demonstration projects; but as soon as that ends, we view these as commercial-type products.’”


administration. Disclosures under IRC 6104(c) will be made pursuant to a memorandum of understanding executed with state charity (including tax) officials that is similar in format to the Basic Agreements entered into under IRC 6103(d). On February 1, 2008, Hawai‘i announced that “it has become the first state in the nation to enter into an information sharing agreement with the Internal Revenue Service to strengthen the state’s oversight of charitable organizations.”

E. Congressional Oversight

In a class by itself, and generally beyond the scope of this essay, is Senator Grassley’s devotion to publicizing abuses in the charitable sector. His efforts range from the systematic – notably, a 2004 hearing and staff white paper on governance that spurred the Independent Sector to convene a blue-ribbon Panel on the Nonprofit Sector, which produced three influential reports – to a continuing series of “love letters” to specific nonprofit organizations inquiring about practices. This latter group includes the American Red Cross, American University, the Nature Conservancy, and the Smithsonian Institution. Industry-wide inquiries, often joined by


On January 29, 2008, state Attorney General Mark Bennett and the Exempt Organizations Division of the Internal Revenue Service entered into an information sharing agreement pursuant to provisions of the Pension Protection Act of 2006 (PPA). The PPA for the first time authorized the IRS to share confidential tax return information with state charity oversight agencies, provided that adequate safeguards are established to maintain the confidentiality of such information.


110 Available at www.nonprofitpanel.org. See also Part IV, below.

111 These letters and, often, the responses, can be found in the press releases pages at http://finance.senate.gov.
Finance Committee chair Max Baucus, have asked extensive questions about nonprofit hospitals’
charity-care practices,\textsuperscript{112} higher educations’ endowment spending,\textsuperscript{113} and, most recently, a group
of televangelists of the “Prosperity Gospel” bent.\textsuperscript{114} These investigations seem to have greater
legitimacy when they cover nonprofit subsectors (rather than individual nonprofits) and the
oversight of the IRS’s performance in administering the laws. Indeed, Senator Grassley deserves
much of the credit for the extensive exempt-organization reforms in the Pension Protection Act
of 2006.\textsuperscript{115} However, the IRS, as part of the executive branch, has the enforcement responsibility
and expertise to prosecute individual cases; moreover, as described above, the IRS must function
under confidentially constraints that Senator Grassley feels unencumbered by. Indeed, the first
sign of public resistance to providing the information “requested” came from some of the
televangelists.\textsuperscript{116}

\textsuperscript{112} For example, by letter to the American Hospital Association, in addition to asking about
discounts to the uninsured and developing a standardized accounting of charity care, Senate Finance
Committee Chairman Chuck Grassley identified other areas of “serious concern”: “investments in joint
ventures, taxable subsidiaries, venture-capital funds and other financial arrangements, contracts for
health care, management and administrative services, executive compensation, travel and expense
reimbursement, billing and debt collection practices, use of tax-exempt bond proceeds, conflicts of
interest and other governance issues, and accounting, reporting, public disclosure and general
transparency issues.” Chuck Grassley, Letter to Richard J. Davidson, president of the American Hospital

\textsuperscript{113} Press Release, “Baucus, Grassley Write to 136 Colleges, Seek Details of Endowment
Pay-outs, Student Aid” (Jan. 24, 2008), available at

\textsuperscript{114} See Chuck Grassley, Press Release, \textit{Update on Ministry Responses in Tax-Exempt Policy

\textsuperscript{115} See generally Transcript of Remarks of Dean Zerbe, CLE Program on Representing and
Managing Tax-Exempt Organizations, Georgetown University Law Center, April 24, 2008, in 13 E0
Tax J. 38, 39 (July/August 2008) (setting forth reflections on the congressional oversight process and
goals by a former key tax aid to Senator Grassley).

\textsuperscript{116} For example, attorney Marcus Owens, on behalf of one of the target churches, wrote to
Senators Baucus and Grassley on November 27, 2007:

If Senator Baucus, or the majority of the Senate Finance Committee, believes that it is
appropriate for the Church to respond to Senator Grassley’s questions, then we respectfully
request that the Senate Finance Committee provide an appropriate legal context for the review, as
would be reflected by a formal subpoena for the information. Congress has wisely determined
that religious organizations should not be subject to the same public filing requirements as other
charitable organizations and, likewise, we believe that the religious doctrine and practices of a
church should not be held out for the world to evaluate as a result of responding to Congressional
IV. VOLUNTARY DISCLOSURE BY THE ORGANIZATION AND DISCLOSURE BY PRIVATE PARTIES

A. Voluntary Disclosure by the Organization Itself

Charities often make disclosures to various constituencies without the compulsion of law. Prospective donors and grantmakers might condition funds on the production of satisfactory financial or other information. For example, before making grants to charities, many community foundations insist on being advised of such information as the names and relationships of board members and officers, the compensation of officers and relevant relationships, the identities of beneficiaries, audit data, and basic performance metrics. Government contracting rules, too, might demand reporting and audited financial statements. Beyond statutory requirements, the bylaws of membership organizations might require certain disclosures to the members. As discussed in Part II, charities have no excuse for refusing to provide basic information to members of the governing board, who should not be compelled to bring litigation to obtain that information on a timely basis.

While we mentioned in Part III that the affairs of a nonprofit, non-governmental entity are private, and generally are not subject to public disclosure, many of the reported troubles that have befallen charities in recent years could have been avoided – to the betterment of the performance and reputation of the nonprofit world and presumably the communities at large – had there been routine, timely and consistent public disclosure of basic information. Some of this information is already available in certain instances through the regulatory and tax filings described in above, but this material is usually available only much after the fact (even when timely filed) and in a form that can be difficult for laymen to parse. The Panel on the Nonprofit Sector’s Principles for Good Governance and Ethical Practices recommends: “A charitable organization should make information about its operations, including its governance, finances, programs, and activities, widely available to the public. Charitable organizations also should consider making information available on the methods they use to evaluate the outcomes of their work and sharing the results inquiries. We are concerned, for example, that some of the information requested would not be in the public domain even if churches were required to comply with these same filing requirements as other charitable organizations. In this regard, we are acutely aware of the potential for some members of the general public to disparage or belittle the Church’s sincerely held religious beliefs, and we want to protect the Church and its members from this possibility. If a subpoena were issued, the Church and its members could be afforded certain confidentiality protections, which, like the privacy protections of section 6103, would reduce the likelihood of any public discourse regarding its religious beliefs.

This letter is available on LEXIS in the Fedtax Library, Tax Notes Today file, as Attorney Urges Grassley to Defer to IRS on Ministry Inquiry, 2007 TNT 235-29, Dec. 6, 2007.
of those evaluations.”

Charities should consider making clear in their bylaws or policies that transparency with the public is to be the norm, and deviations from that norm ought to require board consideration. The fact that transparency is the norm itself would deter many of the abuses made public.

For the benefit of the general public, nonprofits commonly post annual reports to their websites, but it is not so common to see Forms 990 and financial statements. For a laudable example of transparency, see the website of the Ford Foundation, which sets forth organizations’s articles of incorporation; bylaws; committee charters and membership; standards of independence; trustee code of ethics; staff code of conduct and ethics; procedures for approving affiliated grants; procedures for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls and auditing matters; and annual reports and financial statements.

In a crisis, whether as a matter of damage control or to sincerely get ahead of the story, nonprofits are learning to make information available. For example, prior to the 2008 settlement, the dueling websites of the litigants over the Robertson gift to Princeton University to fund the


A good first step is to provide an annual report that lists the organization’s board and staff members, describes its mission, shares information on program activities, and details financial information including, at a minimum, its total income, expenses, and ending net assets. Such reports need not be elaborate, can be produced in paper or electronic form, and can direct the reader to other readily available documents (such as the Form 990 return or audited financial statements) for further information. If an organization chooses to produce such reports on a less frequent basis, such as every two or three years, it should ensure that any intervening changes in its board and staff or programs and its current financial statements are provided as an attachment or are otherwise made known to readers of the report.

Useful websites often provide such essential information as the organization’s vision and mission statements; lists of board and staff members; statement of values and code of ethics; and policies on conflicts of interest, whistleblower protection, and travel.

Information on an organization’s results and how they are measured can be an especially valuable means of explaining its work and accounting to donors and the public. Such information, and the ability to provide it, will vary considerably from one organization to another. To the extent evaluation or information on outcomes is available, some version of it should be included in annual reports, websites, and other forms of communication. More information about program evaluation is provided in principle #19.

118 Go to www.fordfoundation.org/about/governance. Annual reports are available at www.fordfoundation.org/about/annualreports, and its latest financial statement is available at www.fordfoundation.org/about/financials.
Woodrow Wilson School represented an attempt to influence the court of public opinion. Other recent scandals include the Smithsonian Institution and the J. Paul Getty Foundation (discussed in Part IV.C, below).

B. Media

Spurred by the perceived fund raising abuses in response to September 11, media interest in nonprofit governance has exploded. In a 2007 pep talk to journalists covering the nonprofit sector, I had to restrain myself to lauding just 18 cases in which reporters broke or kept up pressure on an important story implicating nonprofit governance. For those trying to keep up, important resources include the Chronicle of Philanthropy’s daily posting of summaries (with links) of news stories published around the country, as well as such legal nonprofit blogs as Don Kramer’s Nonprofit Issues, a group of legal academics’ Nonprofit Law Prof Blog, and Jack Siegel’s CharityGovernance blog.

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119 Only Princeton’s webpage survives. See www.princeton.edu/robertson.

120 See the governance material posted at www.si.edu/about/regents.

121 See, for example, the Getty’s governance page at www.getty.edu/about/governance/. The posted material includes the Getty’s mission statement, trust indenture, bylaws, board of trustees, board committees, trust officers and program directors, policies, financial information, annual and other reports, and the California attorney general’s 2006 investigative report and the 2008 closure of the state’s monitoring process.


124 Available at www.nonprofitissues.com.

125 Available at http://lawprofessors.typepad.com/nonprofit/.

126 Available at www.charitygovernance.com.
Reporters often dwell on “fraud and abuse” in the nonprofit sector.\textsuperscript{127} We run the risk, however, of over-reaction to anecdotal information – since we don’t know the denominator, is the fact that we’re seeing more stories an indication of increasing problems, or of increasing observation? In general, the increased availability of information on nonprofit operations increases the public expectation for more transparency.

\textbf{C. Peer regulators and charity “watchdogs”}

Peer regulation in the nonprofit sector comes in two flavors – the third-party watchdogs and the trade associations. The watchdogs are donor-focused, and they typically provide assessments (sometimes using a star system or letter grades) regardless of whether the charity knows about the review or supplies information. However, the BBB Wise Giving Alliance – which assesses whether a given charity meets or does not meet its Standards for Charity Accountability – relies on information from the charity and states cases in which the organization failed to respond.\textsuperscript{128}

By contrast, membership in the trade associations is voluntary, with the organizational member submitting both to the groups’ standards\textsuperscript{129} and to any disciplinary process for violation. Most groups are not as open as the Evangelical Council for Financial Accountability, which posts a chart of former members, indicating the reason – voluntary resignation or termination.\textsuperscript{130} For


\textsuperscript{128} See the Implementation Guide available at \url{www.give.org}. As explained in the preface to the Standards: “The overarching principle of the BBB Wise Giving Alliance Standards for Charity Accountability is full disclosure to donors and potential donors at the time of solicitation and thereafter. However, where indicated, the standards recommend ethical practices beyond the act of disclosure in order to ensure public confidence and encourage giving. As voluntary standards, they also go beyond the requirements of local, state and federal laws and regulations.” Note that I have served on the board of the BBB Wise Giving Alliance since 2006.

\textsuperscript{129} See, e.g, the Evangelical Council for Financial Accountability, “Seven Standards of Responsible Stewardship,” \url{www.ecfa.org/Content.aspx?PageName=7Standards}. Standard 5, titled Financial Disclosure, reads: “Every member shall provide a copy of its current financial statements upon written request and provide other disclosures as the law may require. If audited financial statements are required to comply with Standard 3, they must be disclosed under this Standard. A member must provide a report, on request, including financial information, on any specific project for which it is soliciting gifts.”

\textsuperscript{130} The most common reason for termination was failure to submit renewal information. Go to \url{www.ecfa.org/Content.aspx?PageName=FormerMember}. 
example, Brian Gallagher, head of the United Way of America, said at the July 22, 2004 Senate Finance Committee roundtable that the UWA has decertified 30 UW’s around the country in the previous two years. This information should have been more widely known – I couldn’t even find it on the UWA’s website. Peer organizations generally seem loathe to publicly discipline noncompliant members. While still an anomaly, compare the Council on Foundation’s brief suspension of the J. Paul Getty Trust’s membership:

Citing “positive and significant” reforms implemented by the J. Paul Getty Trust to address governance and management concerns, the Council restored the trust to full membership. “We appreciate the cooperation and constructive dialogue between our organizations over the past few months and respect the hard work they’ve done to provide the information we requested,” said Steve Gunderson, the Council’s president and CEO. He added that the Council will offer continued assistance as the trust moves forward in ways that enhance its work and the public’s confidence. Getty spokesman Ron Hartwig said in the Los Angeles Times that the reforms include new training and evaluation tools for board members, strengthened conflict-of-interest provisions, increased board oversight of real estate deals, and increased transparency of staff compensation and performance reviews. For more information, read the Council’s press release.\footnote{Council on Foundation, \textit{Council Restores Membership of Getty Trust}, CFSource, Volume III, Issue 10 (May 2006), available at \url{www.cof.org/Council/newsletter.cfm?ItemNumber=4285&navItemNumber=2499}. Note that the press release is no longer posted on the Council’s website!}

Finally, there is the behavior of nonprofit groups speaking out – or, more likely not – about specific misbehaving organizations or unacceptable practices as they occur. Isn’t protection of the sector’s reputation a duty of nonprofits themselves? The Independent Sector’s Panel on the Nonprofit Sector energetic response to Senator Grassley’s 2004 staff white paper culminated in a report containing 33 principles of self-regulation.\footnote{Panel on the Nonprofit Sector, \textit{supra} note 116.} Some members of the working group, however, were disappointed that the principles are precatory only, and that the Nonprofit Panel could not achieve consensus around adopting a mechanism for certification and discipline. Deciding how to bell the cat is never easy.

\section*{CONCLUSION}

The Internal Revenue Service does not have the resources to verify all tax exemptions on a routine basis. Rather, the IRS conducts a relatively small number of examinations (including targeted correspondence audits) of specific charities, either as part of a system of examining Forms 990 or pursuant to a particular compliance initiative (such as on political campaign
activity, hospitals, and institutions of higher education). According to its [November 2008] annual report, the IRS Exempt Organizations Division employs only [826] staff members in its three offices, Examinations, Rulings and Agreements, and Customer Education and Outreach, plus a dozen employees in the EO Director’s office – to oversee 1.8 million registered tax-exempt entities, including almost 1.2 million registered charities.

In early December 2009, the Exempt Organizations Division released a Governance

133 See also Commissioner Shulman’s Nov. 28, 2008 talk to Independent Sector: “We’re . . . taking other proactive action like starting to check up on young exempt organizations to ensure that after a few years in operation they are in fact fulfilling an exempt purpose.” Speech available at www.irs.gov/newsroom/article/0,,id=188567,00.html.

134 For fiscal year 2008, the IRS’s Exempt Organizations Division employed 461 employees in its Examinations office, 355 employees in its Rulings and Agreement office, and 10 employees in its Education and Outreach office. In the two largest functions, 677 of the staff are Tax Law Specialists (a majority of whom are attorneys) and Revenue Agents. See EO FY 2008 Annual Report and Work Plan 2 (Nov. 2008), available at www.irs.gov/pub/irs-tege/finalannualrptworkplan11_25_08.pdf. This level of staffing has stayed much the same since 2000. See the Government Accountability Office report written for a 2005 House Ways and Committee Hearing, Tax-Exempt Sector: Governance, Transparency, and Oversight Are Critical for Maintaining Public Trust 41, table 6 (GAO-05-561T 2005) (finding that for fiscal year 2005, the IRS budgeted 856 fulltime-equivalent employees to the tax-exempt function: 467 for examinations, 37 for determinations, and 42 for other activities); id. at 17 (“From fiscal year 2000 through 2004, IRS staffing for overseeing tax-exempt entities stayed relatively flat as measured by the number of FTE staff assigned to oversee tax-exempt entities.”). TE/GE has a mind-boggling potential workload. According to the 2009 IRS Data Book (released March 11, 2010), in 2008, the Service processed 901,000 exempt-organization tax returns (mostly Forms 990, 990-EZ, and 990-PF); and in 2009 processed 1,132,000, an increase of 25.6% (presumably reflecting mostly filings of the e-Postcard, Form 990-N). See tbl 2, available at www.irs.gov/taxstats/article/0,,id=102174,00.html. Of this number, the Service examined only 3,767 Forms 990 (and similar) returns and 6,420 related taxable returns (primarily employment tax returns and Form 990-T). Id. at tbl 13.

As for IRS enforcement activities, the IRS finalized 78 closing agreements with § 501(c) organizations in fiscal year 1999; 72 in fiscal year 1998; and 65 in fiscal year 1997. See Joint Comm. on Taxation, Study of Present-Law Taxpayer Confidentiality and Disclosure Provisions as Required by Section 3802 of the Internal Revenue Service Restructuring and Reform Act of 1998, Volume II: Study of Disclosure Provisions Relating to Tax-Exempt Organizations 38 n.97 (JCS-1-00, Jan. 28, 2000), available at www.house.gov/jct/s-1-00vol2.pdf (citing the IRS Exempt Organization Return Inventory and Classification System). In fiscal year 1999, the IRS revoked the exempt status of 97 organizations, of which 20 were exempt under § 501(c)(3); in fiscal year 1998, the IRS revoked the exemption of 97 organizations, 38 of which were described in § 501(c)(3); and in fiscal year 1997, the IRS revoked the exemption of 89 organizations, 38 described in § 501(c)(3). Id. at 27 n.56 (citing the IRS Audit Information Management System, Tables 41 and 42).
Check Sheet and a Governance Project Guide Sheet for Completing the Project Check Sheet to be used by IRS exempt organization examination agents in connection with their examinations of Code section 501(c)(3) exempt organizations. The public can access these guidelines from a new webpage that explains: “A check sheet will be used by IRS’ Exempt Organizations Examination agents to capture data about governance practices and the related internal controls of organizations being examined. The data will be included in a long-term study to gain a better understanding of the intersection between governance practices and tax compliance.” The webpage links to the Check Sheet and Guide Sheet and to other governance materials on the website, notably an article entitled “Governance of Charitable Organizations and Related Topics” included in the Life Cycle on-line educational tool for charities.

The IRS’s recent focus on exempt-organization governance has attracted thoughtful commentary on both sides of the issue. Thomas Silk supports this endeavor of the IRS:

It is not far-fetched to imagine a national scandal featuring a prominent charity in violation of standards of charitable governance but incorporated in a state with inadequate charitable enforcement. In the congressional hearings that might follow, the IRS would surely be in a far more defensible position if it had already gone forward to educate the charitable sector about the importance of good governance practices. Later legislation introduced by a supportive Congress may easily resolve any jurisdictional ambiguities about governance of charitable organizations and enforcement.

On the other hand, Bonnie Brier (lead author of the 2008 ACT report quoted above) recently expressed skepticism that the described governance practices actually lead to good governance, and worries that charities will adopt them just to satisfy the IRS regardless of whether they are appropriate for the organization. Marcus Owens, former top exempt organization official at the IRS, questions the IRS’s authority to include governance questions on the Form 990. Senator

137 Go to www.irs.gov/charities/article/0,,id=216068,00.html.
Grassley responded to such objections by proposing legislation to provide statutory authority for the IRS to assert an interest in charity governance as an indicator of compliance with the federal tax-exemption regime.

I generally disagree with those critical of a role for the IRS in charity governance, at least to the extent these criticisms apply to the governance questions on the redesigned Form 990. Indeed, as described above, I submitted comments to the IRS on the 2007 draft of the redesigned Form 990, proposing for inclusion a series of questions on organizational structure and governance practices\(^{142}\) – many of which were added in the final version. At that time, I had in mind the usefulness of the Form 990 to the governing board itself and to state regulators, to donors, to the media, and, yes, to researchers, even aside from what uses the IRS might make of the data. On balance, I believe, the privacy interests of the charity do not outweigh the benefits of transparency of the organization’s governance structure to these outside constituencies. If a particular “best” practice is inappropriate for the charity, it can and should provide an explanation on the Form 990. Thoughtful additional disclosure is an opportunity for the organization to demonstrate – if it is able – how its structure and policies appropriately safeguard charitable assets.

**APPENDIX:**

**SUMMARY AND GOVERNANCE PAGES OF CORE FORM OF REDESIGNED FORM 990**

(2007 DRAFT AND 2008 FINAL VERSIONS)

[See next four pages]

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\(^{142}\) Brody, note 38 *supra.*
Return of Organization Exempt From Income Tax

Under section 501(c), 527, or 4947(a)(1) of the Internal Revenue Code (except black lung benefit trust or private foundation) the organization may have to use a copy of this return to satisfy state reporting requirements.

A For the 20XX calendar year, or tax year beginning , 20XX, and ending , 20XX

D Employer Identification number

E Telephone number

F Name and address of Principal Officer

G Website

H Enter amount of gross receipts

J Books

K Organization type (check only one) 501(c) 527 4947(a)(1) Telephone number

L Year of Formation

M State of legal domicile

Part I Summary

1 Briefly describe the organization's mission:

2 List the organization's three most significant activities and the activity codes (Part IX):

   a Code  
   b Code  
   c Code

3 Enter the number of members of the governing body (Part III, line 1a)  

4 Enter the number of independent members of the governing body (Part III, line 1b)  

5 Enter the total number of employees (Part VIII, line 2a)  

6 Enter the number of individuals receiving compensation in excess of $100,000 (Part II, line 2)  

7 Enter the highest compensation amount reported on Part II, Section A (sum of columns D and E)  

8a Enter officer, director, trustee, and other key employee compensation (Part V, line 8, column (B))  

9a Enter total gross unrelated business revenue from Part IV, line 14, column (C)  

9b Enter net unrelated business taxable income from Form 990-T, line 34  

10 Check this box if the organization discontinued its operations or disposed of more than 25% of its assets and attach Schedule N.

Revenues

11 Contributions and grants (Part IV, line 1g, column (A))  

12 Program service revenue (Part IV, line 2g, column (A))  

13 Membership dues and assessments (Part IV, line 3, column (A))  

14 Investment income (Part IV, lines 4, 5, 6, 8, 10d)  

15 Other revenue (Part IV, lines 3, 7, 9d, 11c, 12c, and 13a, column (A))  

16 Total revenue add lines 11 through 15 must equal Part IV, line 14, column (A)  

Expenses

17 Program service expense (Part V, line 24, column (B))  

18 Management and general expenses (Part V, line 24, column (C))  

19a Fundraising expenses (Part V, line 24, column (D))  

19b Percentage of contributions (divide line 19a by line 11)  

20 Total expenses (must equal Part V, line 24, column (A))  

21 Net income line 18 minus line 20  

Net Assets or Fund Balances

22 Total assets (Part VI, line 17)  

23 Total liabilities (Part VI, line 27)  

24a Net assets or fund balances line 22 minus line 23  

24b Total expenses (line 20) as percentage of net assets (line 24a)  

Amount % of Total

For Privacy Act and Paperwork Reduction Act Notice, see the separate Instructions.

Cat. No. 112220 Form 990 (20XX)
Part II: Statements Regarding Governance, Management, and Financial Reporting

1a Enter the number of members of the governing body. ☐Yes ☐No
1b Enter the number of independent members of the governing body. ☐Yes ☐No

2 Did the organization make any significant changes to its organizing or governing documents? If "Yes", briefly describe these changes.

☐Yes ☐No

3a Does the organization have a written conflict of interest policy?

☐Yes ☐No

b If "Yes," how many transactions did the organization review under this policy and related procedures during the year?

☐Yes ☐No

4 Does the organization have a written whistleblower policy?

☐Yes ☐No

5 Does the organization have a written document retention and destruction policy?

☐Yes ☐No

6 Does the organization contemporaneously document the meetings of the governing body and related committees through the preparation of minutes or other similar documentation?

☐Yes ☐No

7a Does the organization have local chapters, branches or affiliates?

☐Yes ☐No

b If yes, does the organization have written policies and procedures governing the activities of such chapters, affiliates and branches to ensure their operations are consistent with the organization’s?

☐Yes ☐No

8 Does an officer, director, trustee, employee or volunteer prepare the organization’s financial statements? Indicate whether an independent accountant provides any of the following services:

☐Compilation ☐Review ☐Audit

9 Does the organization have an audit committee?

☐Yes ☐No

10 Did the organization’s governing body review this Form 990 before it was filed?

☐Yes ☐No

11 How do you make the following available to the public? Check all that apply.

Organizing/Governing Documents ☐n/a ☐website ☐other website ☐office ☐other

Conflict of Interest Policy ☐n/a ☐website ☐other website ☐office ☐other

Form 990 ☐n/a ☐website ☐other website ☐office ☐other

Form 890-T ☐n/a ☐website ☐other website ☐office ☐other

Financial Statements ☐n/a ☐website ☐other website ☐office ☐other

Audit Report ☐n/a ☐website ☐other website ☐office ☐other

12 List the states with which a copy of this return is filed:

☐Yes ☐No
Form 990
Return of Organization Exempt From Income Tax

Under section 501(c), 527, or 4947(a)(1) of the Internal Revenue Code (except black lung benefit trust or private foundation)

For the 2008 calendar year, or tax year beginning , 2007, and ending , 2008

A. For the 2008 calendar year, or tax year beginning, 2007, and ending, 2008

B. Check if applicable:

☐ Address change
☐ Name change
☐ Initiative return
☐ Termination
☐ Amended return

C. Name of organization:

D. Employer identification number:

E. Telephone number:

F. Name and address of principal officer:

G. Gross receipts:

H(1) Is this group return for affiliated: Yes ☐ No ☐
H(2) Are all affiliates included? Yes ☐ No ☐

J. Website:

K. Type of organization:

L. Year of formation:

M. State of legal domicile:

Part I Summary

1. Briefly describe the organization's mission or most significant activities:

2. Check the box if the organization discontinued its operations or disposed of more than 25% of its assets:

3. Number of voting members of the governing body (Part VI, line 1a):

4. Number of independent voting members of the governing body (Part VI, line 1b):

5. Total number of employees (Part V, line 2a):

6. Total number of volunteers (estimate if necessary):

7a. Net gross unrelated business revenue from Form 990-T, line 12, column (C):

7b. Net unrelated business taxable income from Form 990-T, line 34:

Part II Financial Information

8. Contributions and grants (Part VIII, line 11):

9. Program service revenue (Part VIII, line 29):

10. Investment income (Part VII, column (A), lines 3, 4, and 7d):

11. Other revenue (Part VIII, column (A), lines 5, 6d, 8c, 9c, 10c, and 11e):

12. Total revenue—add lines 8 through 11 (must equal Part VIII, column (A), line 12):

13. Grants and similar amounts paid (Part IX, column (A), lines 1-3):

14. Benefits paid to or for members (Part IX, column (A), line 4):

15. Salaries, other compensation, employee benefits (Part IX, column (A), lines 5-10):

16. Professional fundraising fees (Part IX, column (A), line 11a):

17. Total fundraising expenses (Part IX, column (D), line 25):

18. Other expenses (Part IX, column (A), lines 11a-11d, 11f-24f):

19. Total expenses, add lines 15-17 (must equal Part IX, column (A), line 25):

20. Revenues less expenses. Subtract line 18 from line 12:

21. Total assets (Part X, line 16):

22. Total liabilities (Part X, line 28):

23. Net assets or fund balances. Subtract line 20 from line 22:

Part II Signature Block

I, the undersigned, do solemnly swear or affirm that the information in this return is true and correct to the best of my knowledge and belief.

Signature of officer

Date

Type or print name and title

Paid Prepare's
Use Only

Preparer's signature

Date

Check if self-employed

Preparer's identifying number

Yes ☐ No ☐

May the IRS discuss this return with the preparer shown above? (See instructions)

For Privacy Act and Paperwork Reduction Act notice, see the separate instructions.

Cat. No. 15282Y
Form 990 (2008)
Part VI  Governance, Management, and Disclosure (Sections A, B, and C request information about policies not required by the Internal Revenue Code.)

Section A. Governing Body and Management

For each “Yes” response to lines 2–7b below, and for a “No” response to lines 8 or 9b below, describe the circumstances, processes, or changes in Schedule O. See instructions.

1a  Enter the number of voting members of the governing body

1b  Enter the number of voting members that are independent

2  Did any officer, director, trustee, or key employee have a family relationship or a business relationship with any other officer, director, trustee, or key employee?

3  Did the organization delegate control over management duties customarily performed by or under the direct supervision of officers, directors or trustees, or key employees to a management company or other person?

4  Did the organization make any significant changes to its organizational documents since the prior Form 990 was filed?

5  Did the organization become aware during the year of a material diversion of the organization’s assets?

6  Does the organization have members or stockholders?

7a  Are any decisions of the governing body subject to approval by members, stockholders, or other persons who may elect one or more members of the governing body?

7b  Are any decisions of the governing body subject to approval by members, stockholders, or other persons?

8  Did the organization contemporaneously document the meetings held or written actions undertaken during the year by the following:

8a  The governing body?

8b  Each committee with authority to act on behalf of the governing body?

8c  Does the organization have local chapters, branches, or affiliates?

8d  If “Yes,” does the organization have written policies and procedures governing the activities of such chapters, affiliates, and branches to ensure their operations are consistent with those of the organization?

10  Was a copy of the Form 990 provided to the organization’s governing body before it was filed? All organizations must describe in Schedule O the process, if any, the organization uses to review the Form 990.

11  Is there any officer, director or trustee, or key employee listed in Part VII, Section A, who cannot be reached at the organization’s mailing address? If “Yes,” provide the names and addresses in Schedule O.

Section B. Policies

12a  Does the organization have a written conflict of interest policy? If “No,” go to line 13.

12b  Are officers, directors or trustees, and key employees required to disclose annually interests that could give rise to conflicts?

12c  Does the organization regularly and consistently monitor and enforce compliance with the policy? If “Yes,” describe in Schedule O how this is done.

13  Does the organization have a written whistleblower policy?

14  Does the organization have a written document retention and destruction policy?

15  Did the process for determining compensation of the following persons include a review and approval by independent persons, comparability data, and contemporaneous substantiation of the deliberation and decision?

15a  The organization’s CEO, Executive Director, or top management official?

15b  Other officers or key employees of the organization?

16a  Describe the process in Schedule O. (see instructions)

16b  Did the organization invest, contribute assets to, or participate in a joint venture or similar arrangement with a taxable entity during the year?

16c  Did the organization adopt a written policy or procedure requiring the organization to evaluate its participation in joint venture arrangements under applicable federal tax law, and taken steps to safeguard the organization’s exempt status with respect to such arrangements?

Section C. Disclosure

17  List the states with which a copy of this Form 990 is required to be filed.

18  Section 6104 requires an organization to make its Forms 1023 (or 1024 if applicable), 990, and 990-T (501(c)(3)'s only) available for public inspection. Indicate how you make those available. Check all that apply.

☐ Own website  ☐ Another’s website  ☐ Upon request

19  Describe in Schedule O whether (and if so, how) the organization makes its governing documents, conflict of interest policy, and financial statements available to the public.

20  State the name, physical address, and telephone number of the person who possesses the books and records of the organization.

Form 990 (2008)