



The IRS 990 Return—It’s More Important Than You Think

IRS officials aren’t the only ones scrutinizing your 990. Be sure you’re giving this important return the attention it deserves.

BY KAREN A. FROELICH

“The annual IRS 990 return—just another time-consuming form to fill out. No one has ever asked to see it.” “The 990 return is a major headache and waste of time. It’s not all that helpful, just another government requirement.”

“We don’t even look at it. The CPA takes care of it.”

Do these comments sound familiar? If so, you’re like most nonprofit practitioners, who don’t see the IRS 990 return as high priority. Rather, they view it as a routine IRS form.¹

But is it really a routine, low-priority item? Let’s take a closer look.

Is Your Approach Too Casual?

All 501(c) nonprofits with revenues over \$25,000 a year must fill out an annual 990 return. On it, they must detail their financial activity, including income, expenditures, assets, liabilities, fund balances, and excess or deficit at year-end. IRS officials use this information in several ways:

- They check each 990 return to be sure the organization is legally eligi-

ble for nonprofit status.

- They make sure that each nonprofit is complying with financial requirements.
- They combine all the 990 data to describe the nonprofit sector’s size and scope.
- They use the combined data to track financial trends such as shifts in revenue sources.

These straightforward and primarily internal uses of the 990 return by the IRS has helped create a more annoyed than conscientious attitude about its preparation. Overburdened with a multitude of reporting requirements, nonprofit managers place the 990 far down on their priority list. They often delegate 990 preparation to a CPA firm. Or they give the

organization’s accountant full responsibility.

But beware! Such a hands-off approach to the IRS 990 return may no longer be wise.

Why Is the Role of the 990 Growing?

The information you provide on the 990 return may travel far beyond the IRS. The 990 is becoming one of the most important sources of information about nonprofit organizations today, due to a combination of factors:

- Financial information on the 990 makes it attractive to researchers who need numerical measures for their statistical studies. Investigations of revenue diversification,

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debt management, and overall financial health in the nonprofit sector have been based on data from the 990 return.² So have studies investigating nonprofit competition with small businesses.³

- The information is used by regulatory and oversight groups, including the media, to examine the potentially sensitive areas of management and fundraising expenses and the proportion of funds generated by fees or other commercial activity. For example, a Midwest state's attorney general's office compiled and distributed a major report on over 130 large charities, publicizing management and fundraising expenses compared to total program expenses for each organization. And newspaper stories detailing for-profit enterprise and revealing executive compensation figures are increasingly common. This type of information often becomes a backdrop for public policy debates at both the national and state levels, which can have substantial impact on major segments of the nonprofit population.
- Foundations and other grantmaking bodies use entries from the 990 return as they strive to develop objective, defensible rationales for awarding scarce dollars.
- Several highly visible scandals have raised public skepticism and heightened scrutiny of nonprofit organizations. The public is looking for unbiased sources of information in order to compare organizations and make

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conclusions about their trustworthiness and value.

- Recently, the IRS has begun offering national samples of 990 returns for purchase. A variety of state and private agencies also provide 990 data. Subgroupings according to region, size, or organizational purpose can easily be obtained. The information is formatted on data tapes or computer diskettes ready to be statistically analyzed.
- Many people find 990 returns more useful than annual financial statements, which aren't public documents and must be obtained directly from each individual organization. The 990 return provides the same entries year after year for all filers, allowing direct comparisons across organizations and greater continuity for identification of trends. And because the 990 return can't be tailored for individual situations, it can be viewed as a more unbiased source of information, with less potential for crafting as a public relations device.

The IRS 990 return is likely to become even more widely dispersed in the near future. The recently passed Taxpayer Bill

of Rights II makes it easier for individuals to obtain returns directly from the nonprofit organization itself.⁴ The new law also increases the penalties for nonprofits who don't open their 990s to public scrutiny. The law requires nonprofits to do the following:

- Give copies of 990 returns immediately to anyone who asks for them in person.
- Fill written requests for 990s within 30 days.
- Charge only a reasonable copying fee when filling requests for copies of 990 returns.

Even greater 990 accessibility is on the horizon. The IRS is exploring the idea of letting nonprofits file their 990s electronically. It also plans to post 990s on the Internet so that the public has even easier access to them.

How Should You Manage Your 990?

Considering the expanding role of the 990 return, it is crucial that you manage its preparation carefully. Three guidelines are helpful:

1. **Take Care in Choosing Your Preparers.** Be sure that those who prepare your 990 return have sufficient training and information. Lack of experience and insight can lead to errors, omissions, and questionable results. Select internal preparers who understand financial and accounting matters. Give them detailed IRS guidelines (rather than just a copy of last year's return). Be sure they have adequate lead time. If necessary, bring in experienced consultants to help them.

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When using consultants, describe your organization and any possible problem areas in detail. Make sure they give special attention to revenue sources and expense allocations, especially those involving management or fundraising.

2. Be Consistent. If possible, use the same preparers each year. Such consistency leads to greater precision and sophistication in the filing process. It avoids the problem of widely fluctuating entries over time, which can be a red flag to anyone examining your organization. Also, use the same people to prepare both your internal financial statements and your 990 return. A lack of correspondence between the two can be another red flag.

3. Be Involved. Above all, take an active part in managing your 990 preparation. Don't simply delegate it and forget it. It's too important a document for such a nonchalant attitude. Remember, this

document can lead to unfavorable press and affect your organization's reputation. It can cause you to lose funding. Considering its growing reach and impact, a proactive management approach is vital. ■

Footnotes

¹Support for study of the IRS 990 return from the Aspen Institute's Nonprofit Sector Research Fund is gratefully acknowledged.

²For a more complete review, see Karen A. Froelich & Terry W. Knoepfle, "Internal Revenue Service 990 Data: Fact or Fiction?", *Nonprofit and Voluntary Sector Quarterly*, Vol. 25, No. 1 (March 1996), pp. 40-52.

³See Jeffrey Haber's articles in *Nonprofit World*, including "The Nonprofit Advantage—Fire or Smoke?" (March-April 1997) and "Nonprofit Competition with Small Business: A Roadmap Leading to Answers" (May-June 1994).

⁴For more information on the Taxpayer Bill of Rights II (officially Public Law 104-168), see "Nonprofits Ask IRS to Clarify New Law," *Nonprofit World*, May-June 1997.

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