



# The NOT-FOR-PROFIT INDUSTRY EDITION SUMMER '08 Bottom Line

A PUBLICATION DESIGNED TO KEEP AN EYE ON "THE BOTTOM LINE"

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## Main Requirements for Filing Form 990

Of course, a qualified charitable organization qualifies for tax-exempt status, so you generally don't have to worry about paying income taxes. But this hardly eliminates all your responsibilities towards the IRS. Significantly, your not-for-profit must file annual information returns.

**Action idea:** Know the requirements for filing Form 990 or one of the related forms. We have provided a brief summary below of the key rules for non-profit managers.

First, let's cover some basic information. There are actually three versions of the not-for-profit reporting form: Form 990, 990-EZ and 990-PF. Form 990 is filed by tax-exempt organizations, nonexempt charitable trusts and certain types of exempt political organizations. This includes those organizations granted tax-exempt status under Internal Revenue Code Sections 501(a), 527 or 4947(a)(1), unless a special exception applies.

On the other hand, if your not-for-profit has gross receipts of less than \$100,000 and total assets of less than \$250,000, you can file the short form (Form 990-EZ). Form 990-PF is used by private foundations.

What types of organizations are exempt from filing Form 990? Predominantly, this extends to not-for-profits with an annual income of \$25,000 or less. However, under the Pension Protection Act of 2006, beginning in 2008 most organizations with gross receipts of \$25,000 or less will be required to file new Form 990-N (an electronic e-postcard) to maintain their tax-exempt status.

The list of other organizations that may be exempt also includes:

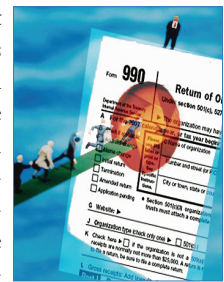
- Faith-based organizations;
- Subsidiaries of other not-for-profit; religious schools;
- Missions or missionary organizations;
- Certain state institutions (e.g., universities); and
- Government corporations.

Finally, if you operate a not-for-profit in your state but have not yet applied to the IRS for an exemption from federal income tax, you are not technically required to file Form 990 (although you still may want to do so).

The due date for filing Form 990 or a related version is generally the 15th

day of the fifth month after the end of your accounting period. For calendar-year entities, the due date for 2007 is May 15, 2008.

Not-for-profit organizations are required to make these forms, as well as their exemption application, available for public review without charge at their regional and district offices during regular business hours. A not-for-profit that does not maintain a formal office can make the documents available at a reasonable location. Any request to view the documents must be honored within a reasonable amount of time.



**Action idea:** The simplest thing to do is to make this information accessible on your Web site. Your business advisers can provide assistance with the appropriate language.

## New Case Extends 100% Penalty to Board Member

One of the harshest provisions in the tax law is often called the “100% penalty” by tax practitioners. Essentially, a person who is responsible for a company’s unpaid payroll taxes may be held personally liable for 100% of the required amount of tax. The unpaid taxes come right out of the responsible person’s pocket.

**Action idea:** Do not assume that you are immune from this penalty. As a new case shows, liability may be extended to a person serving on the board of directors of a tax-exempt organization or an officer of a not-for-profit. This penalty is not strictly limited to managers and owners of for-profit businesses.

Furthermore, you may still be held liable if you delegate the job of depositing payroll taxes to someone else. Similarly, liability may attach even if you thought the payroll taxes had been paid on time. To avoid a personal assessment, you must show that the failure was due to “reasonable cause” and not “willful neglect.” Merely knowing about the delinquency may be treated as a willful failure.

**Facts of the new case:** Mr. Verret served on the board of directors of a not-for-

profit hospital for more than two decades. After he became chairman of the board, Verret often devoted about 22 to 30 hours weekly to the hospital, receiving annual compensation of between \$70,000 and \$80,000.

Verret actively participated in the hospital’s daily management. In addition, he maintained authority to sign checks and hire and fire employees. As chairman of the board, he communicated regularly with hospital officials.

Despite the best efforts of Verret and others, the hospital’s economic fortunes began to decline. Eventually, it failed to remit the required payroll taxes for the last two quarters of 2001. Verret was aware of this delinquency, but he did not take any affirmative steps to correct it. The IRS imposed the 100% penalty against Verret and two other hospital officers. Verret challenged the IRS decision in federal court.

**Result:** The District Court determined that Verret was a “responsible person” under the tax law’s definition. His participation in the management of hospital affairs indicated that his position was much more than honorary. Therefore, Verret was personally liable for the 100% penalty. Note: As in this case, multiple parties may be held jointly and severally liable for the un-

paid payroll taxes.

Obviously, there is no foolproof method for avoiding the 100% penalty, but you can minimize potential problems by taking a few precautions. For instance:

- 1. Designate the task of paying taxes to one person. Have another employee verify that payment has been made.**
- 2. Assign backups to both employees in case of illness, vacations or other absences.**
- 3. Require that a report be issued to you indicating that the responsibility has been completed.**
- 4. Make it your business to personally check to ensure that payment has been made on time.**

**Action idea:** The importance of meeting this payroll tax responsibility cannot be overstated. Do not fall victim to this common occurrence. Coordinate an overall plan with your tax advisers.

## Can You Pass the Commensurate Test?

According to recent comments from an IRS official, the agency intends to refocus on the “commensurate test” as a basis for ensuring that charities are acting in furtherance of their tax-exempt functions.

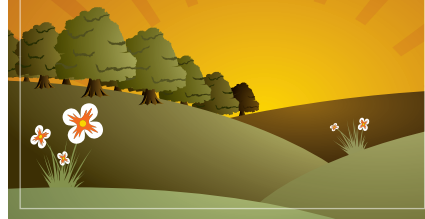
**Basic premise:** This test is used to determine if a charity is fulfilling, through contributions and grants, a charitable purpose that is “commensurate” with its financial resources. Over the next year and a half, the IRS will develop a broad program initiative based on the commensurate test.

The renewal of the commensurate test is based in part on recent congressional inquiries into the manner in which not-for-profit colleges and universities are using their resources, especially their endowments, to further charitable purposes. Several members of Congress are urging stricter standards akin to the requirements for private foundations.

It is critical for charitable organizations to continue to show the public that contributions are being put to good use.

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