New Form 990 Requires Attention to Three Policies

Take note of whistleblower, document destruction, and conflict of interest policies

by Kathryn M. Vanden Berk

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The many requirements included in the new Internal Revenue Service (IRS) Form 990 calls for careful planning. My summer 2008 column described how the new Form 990 will require nonprofits to list compensation information for some employees, details of governance systems and how they work, and information on supporting organizations and tax-exempt bond issues.

This fall 2008 column provides details on several important policies that must be in place per the requirements of the new Form 990.

At this time, the IRS is engaged in a massive educational initiative for the new Form 990. Detailed instructions were issued in August, and the IRS has been meeting with nonprofit organizations and their agents and representatives since December 2007, when the new Form 990 was first made available to the public.

Luckily, you will not need to use the Form 990 until next year when you report your current fiscal year's activities. Nevertheless, now is the time to get your books and governance practices in order to respond to the changes in the form. In particular, the new Form 990 wants you to answer "yes" to a number of questions about certain governance policies which must be in effect the year before you file the new Form 990.

The specific governance policies that must be in place are: whistleblower, document destruction, and conflict of interest. Let's look at the requirements. You can review sample policies on the *Alliance for Children & Families Magazine* website at alliance1.org/magazine.

Whistleblower Policy

A good whistleblower policy includes the following key elements:

Code of Conduct. A Code of Conduct establishes the general expectation that your organization requires ethical conduct of its leaders and staff. You may be general or you may include more detailed descriptions of the kinds of conduct that is expected and/or prohibited.

Reporting Process. Your policy should require employees to report concerns whenever they suspect that something is amiss. This mandatory reporting requirement establishes that you are serious about the matter and protects you from the employee who learns about ethical lapses but does nothing. Under the sample policy I have provided, it is a disciplinary issue for an employee to suspect unethical misconduct and stay silent.

I should note that a good policy offers multiple avenues for reporting. This eliminates the possibility that someone will not speak up because he/she fears or does not trust the person to whom a report is to be made.

Investigations. You will need to appoint someone within the organization to be a compliance officer. The sample policy requires that person to chair your board's audit committee, but you may adopt any suitable structure. All reports must be fully investigated to ensure that you live up

to your side of the bargain. If employees find out that complaints hit a dead end, they won't report future incidents. An employer that has a history of non-response will be more likely by far to be found to have violated their own policy.

No Retaliation. Finally, the key to a good whistleblower policy is protection for the person who, in good faith, reports a suspected violation of the code. The reporter must be given benefit of the doubt, and no action should be taken against him/her unless the report is clearly made with the intent to harm someone or to harm the organization.

You should be aware that whistleblower lawsuits are becoming more and more common. Plaintiffs' attorneys will often add a cause of action for retaliation to an ordinary employment action in hopes that the employer's actions in response to an incident will be worthy of damages. Employees who fail to prove their underlying charge of discrimination will often succeed on a retaliation claim if they have been subjected to adverse action by their employer.[1]

Document Retention and Destruction Policy

A good document retention and destruction policy includes the following key elements:

Document Destruction Dates. Not all documents must be kept indefinitely. A good document retention policy will call for destruction after certain benchmark dates have occurred, which is based on your state's statutes of limitations. These are dates after which your organization may not be sued. Please note that any organization involved in work with children should know that statutes of limitation do not begin to run for children until they reach their 18th birthday, and documents related to their care must be retained until at least seven years after that date.

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Destruction Techniques. Most business-related documents must be shredded in order to ensure confidentiality. Documents that contain protected health information must be shredded crossways to ensure maximum privacy. Digitally recorded documents (voicemail, email) are erased electronically.[2]

Backup Storage. Documents stored electronically should be backed up off site. This may be accomplished by backup drives or by backup service providers.

"Legal Hold" on Destruction. The most important part of your policy is that you must stop all destruction when your organization is notified that an official investigation has been started. The Sarbanes Oxley Act makes it a crime to alter, cover up, falsify, or destroy any document (or to persuade someone else to do so) to prevent its use in a federal investigation or other government proceeding. If an official investigation is underway or even suspected, you must stop any document purging in order to avoid criminal obstruction charges.

Conflict of Interest Policy

The conflict of interest policy should not be new to most of you. The IRS has been asking whether or not your board has adopted a conflict of interest policy for a number of years. But because of the IRS' new emphasis on governance, it is a good time to review your own policy and how it affects your organization.

Basic conflict of interest principles require at least the following:

Disclosure of the Potential Conflict. The interested director or officer, who knows that a conflict may exist, must inform the board of that possibility.

Disclosure of the Facts and Circumstances. The director or officer must disclose all of the facts and circumstances so that the board may determine whether or not a conflict does, in fact, exist.

Removal from Discussion. Interested directors and officers must remove themselves from the discussion so that their presence does not inhibit the board from a full deliberation.

Determination of the Best Interests of the Organization. Best practice would require the board to obtain competing bids on any transaction. At the very least, the board must be persuaded that the transaction with the interested director or officer is at least as good for the organization as a transaction with anyone else.

Removal from Decision. The interested person must remove himself or herself from the board room as a decision is made. Any dissenting vote should be noted for the record.

Document the Decision. The transaction should be fully documented so that the decision, and all considerations, may be shared with anyone who questions the transaction.

Take Steps Now

If you have not discussed the new Form 990 with your board chair, do this as soon as possible. I suggest that you also call your tax preparer to find out what he/she will require when preparing your Form 990 at the conclusion of your current fiscal year.

As with all major changes in any field, the Form 990 changes will cause some confusion. If you prepare now, you will minimize disruption to your organization and compliance problems during your audit. ■

ENDNOTES

1. For example, in *Fine v. Ryan Int'l Airlines*, 305 F.3d 746, 2002 WL 31086302 (7th Cir. 2002), the court determined that an airline pilot was entitled to the jury's award of damages for retaliation, even though she did not prove actual discrimination. She was fired after she complained in good faith about what she reasonably considered was sex discrimination and harassment in the workplace.
1. In litigation, corporations are not required to produce records that are "not reasonably accessible." The limits of reasonableness are now being tested in cases that involve large corporations and information storage systems that may have been intentionally designed to make it impossible to produce records.

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