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PUBLIC FINANCE

ALERT

IRS FOCUSES ON TAX-EXEMPT BONDS ON NEW FORM 990

By Kevin B. Scott

The Internal Revenue Service has introduced a redesigned Form 990 – which was officially released on December 20, 2007, approximately six months after the IRS introduced a draft version for public comment.

While there are many changes to Form 990, of particular importance to institutions that issue (or have issued on their behalf) tax-exempt bonds is a new Schedule K, *Supplemental Information on Tax-Exempt Bonds*. According to the commentary that accompanied the draft Schedule K, the IRS was interested in tax-exempt bonds because it was aware of "significant non-compliance with recordkeeping and record retention requirements relating to tax-exempt bonds issued by or for the benefit of Section 501(c)(3) organizations."

According to many commentators, Schedule K is consistent with increased IRS scrutiny on issues such as the pricing of GICs (guaranteed investment contracts), interest rate swaps, and post-issuance compliance. The IRS also indicated it has concerns about the investment of proceeds that might circumvent existing arbitrage rebated requirements. The new Schedule K is also consistent with a questionnaire the IRS sent out last year attempting to gauge nonprofits' compliance with the rules surrounding tax-exempt bonds.

Schedule K will require information regarding all bonds that were issued after 2002. Of particular note are the following:

- a question regarding whether the organization maintains adequate books and records to support the final allocation of bond proceeds
- a detailed section on any potential private use including any management contracts or research agreements in place with respect to bond-finance property
- a question asking whether the organization has adopted management practices and procedures to insure post-issuance compliance with tax exempt requirements
- a question regarding the use of hedges (interest rate swaps) and GICs
- a question as to whether the regulatory safe harbor for establishing the fair market value of GICs was satisfied

Clearly, institutions will want to be able to answer affirmatively to many of the questions regarding whether proper procedures are in place and were followed.

For the 2008 tax year, only Part I of the Schedule K, which simply requires the basic identification of any tax-exempt bonds, is required to be completed. Beginning with tax year 2009, more detailed information regarding use of proceeds, private use, and investments will be required.

Nonprofit institutions should use the time wisely to make sure they have the proper procedures in place and can demonstrate compliance with the issues raised by new Schedule K.

If you should have any questions regarding this *Alert*, please contact the author at 215.299.2070 or kscott@foxrothschild.com. Visit us on the web at www.foxrothschild.com.

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