

United States General Accounting Office

GAO

Report to the Chairman, Subcommittee on  
Commerce, Consumer, and Monetary  
Affairs, Committee on Government  
Operations, House of Representatives

September 1988

# TAX ADMINISTRATION

## Availability and Completeness of Returns for Tax- Exempt Organizations



043613 / 137104

---

1 2

---

1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36 37 38 39 40 41 42 43 44 45 46 47 48 49 50 51 52 53 54 55 56 57 58 59 60 61 62 63 64 65 66 67 68 69 70 71 72 73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 100

1



United States  
General Accounting Office  
Washington, D.C. 20548

---

**General Government Division**

B-217690

September 30, 1988

The Honorable Doug Barnard, Jr.  
Chairman, Subcommittee on Commerce,  
Consumer, and Monetary Affairs  
Committee on Government Operations  
House of Representatives

Dear Mr. Chairman:

This report responds to your request that we review the availability and completeness of Form 990 information returns, which are filed annually with the Internal Revenue Service (IRS) by many tax-exempt organizations. The report contains recommendations to IRS on making more of these returns available to the public upon request and ensuring that the returns filed are complete.

We are sending copies of this report to the Commissioner of Internal Revenue and other interested parties.

Sincerely yours,

A handwritten signature in cursive script that reads "Richard L. Fogel".

Richard L. Fogel  
Assistant Comptroller General

---

# Executive Summary

---

## Purpose

Each year over 300,000 tax-exempt organizations file annual information returns (Form 990) with the Internal Revenue Service (IRS). These returns are designed to provide IRS and the public with detailed information useful for monitoring tax-exempt organizations' activities and their sources and uses of funds. In addition, 32 states accept the Form 990 return for state reporting purposes. IRS makes the Form 990 returns available for public inspection and has a program designed to identify whether tax-exempt organizations file complete annual information returns.

The Commerce, Consumer, and Monetary Affairs Subcommittee, House Committee on Government Operations, asked GAO to evaluate whether (1) IRS can locate and provide requested Form 990 returns to the public and (2) Form 990 returns filed by tax-exempt organizations are complete.

---

## Background

IRS requires that requests for public inspection of Form 990 returns be made in writing to the national office or to a district office. The national or district office then sends the request to the appropriate service center for retrieval of the return. Once the return is retrieved, a requester may either review it at the national office or the district office where the request originated, or obtain a copy of the return from the service center.

Using criteria in its Incomplete Returns Program, IRS reviews Form 990 returns at the time of filing to ensure that they are complete. This program requires service center staff to review Form 990 return line items and to correspond with tax-exempt organizations to get additional information if the lines are incomplete.

GAO requested a sample of 450 Form 990 returns from three service centers to determine whether IRS could provide them and whether they were complete. The returns were for tax year 1986. The sample is representative of the Form 990 returns filed at these service centers, and estimates based on the sample can be projected to the tax year 1986 Form 990 returns received by these service centers. IRS officials said that the results obtained at these service centers should reflect the nationwide retrievability and completeness of Form 990 returns.

---

## Results in Brief

Based on an analysis of the 450 sample Form 990 returns and discussions with IRS officials, GAO found the following:

- IRS could usually locate and provide a requested Form 990 return if the name the organization used to obtain tax-exempt status was provided.
- Almost half of the Form 990 returns were missing supporting schedules, such as for investments or payments to affiliates, required by filing instructions and needed for public inspection and tax administration purposes. Even with the schedules missing, most of the sample Form 990 returns were considered complete under IRS' Incomplete Returns Program criteria.

---

## GAO's Analysis

---

### Annual Information Returns Could Usually Be Located and Made Available

Projecting the sample results to the universe of Form 990s filed at the Brookhaven, Cincinnati, and Fresno Service Centers, GAO estimates that IRS could locate about 99 percent of requested Form 990 returns when provided the name that the organization used to obtain tax-exempt status. GAO further estimates that IRS would provide about 95 percent of the Form 990 returns to the requesters. Returns that would not be provided would usually be in use internally. However, IRS officials said that with a procedural change, copies of these returns could be obtained and provided to satisfy public inspection requests. (See ch. 2.)

---

### Annual Information Returns Were Often Missing Supporting Schedules

Based on analysis of the sample results, GAO estimates that about 48 percent of Form 990 returns were missing one or more supporting schedules required by the Form 990 return filing instructions. GAO estimates that 95 percent of Form 990 returns were considered complete by IRS' Incomplete Returns Program criteria. These supporting schedules are to provide detailed information concerning such activities as fund-raising and payments to affiliates. Without these schedules, a requester has limited information concerning how the amounts included on the return for these activities are being used. But, the supporting schedules were not included in IRS' Incomplete Returns Program criteria. Although there would be some additional cost for ensuring that supporting schedules have been provided, GAO believes such costs would diminish over time as compliance improves. (See ch. 3.)

---

## Recommendations

To ensure full disclosure of tax-exempt organization information, GAO recommends that the Commissioner of Internal Revenue

- 
- establish procedures to ensure that copies of requested Form 990 returns being used internally are provided to requesters, and
  - expand the criteria for the Incomplete Returns Program to ensure that missing Form 990 return supporting schedules are obtained from tax-exempt organizations.

---

## Agency Comments

IRS officials agreed with GAO's recommendations and said they plan to take actions to implement them. (See pp. 15 and 19.)



---

# Contents

---

|   |   |    |
|---|---|----|
| <b>Executive Summary</b>  |   | 2  |
| <b>Chapter 1</b>  |   | 8  |
| <b>Introduction</b>   | How IRS Provides Form 990 Returns to the Public                         | 8  |
|   | How IRS Processes Form 990 Returns                                      | 9  |
|   | Objectives, Scope, and Methodology                                      | 10 |
| <b>Chapter 2</b>  |   | 13 |
| <b>Annual Information Returns Could Usually Be Located and Made Available</b> | Information Returns Could Be Located                                    | 13 |
|   | Located Returns Are Not Always Made Available                           | 14 |
|   | Conclusions   | 15 |
|   | Recommendation  | 15 |
|   | Agency Comments   | 15 |
| <b>Chapter 3</b>  |   | 16 |
| <b>Annual Information Returns Were Often Missing Supporting Schedules</b>     | Many Different Supporting Schedules Were Missing                        | 16 |
|   | Supporting Schedules Needed for Returns to Be Complete                  | 17 |
|   | Obtaining Missing Supporting Schedules                                  | 18 |
|   | Conclusions   | 19 |
|   | Recommendation  | 19 |
|   | Agency Comments   | 19 |
| <b>Appendixes</b>   | Appendix I: Sampling Methodology and Statistical Projections            | 20 |
|   | Appendix II: Form 990 Examination Program                               | 22 |
|   | Appendix III: How IRS Assures That Form 990 Returns Are Filed           | 24 |
|   | Appendix IV: Form 990 Return Line Items Requiring a Supporting Schedule | 25 |
| <b>Tables</b>   | Table 3.1: Frequently Missing Supporting Schedules                      | 16 |
|   | Table I.1: Sample Size by Service Center and Organization Income Level  | 20 |
|   | Table I.2: Confidence Limits for Selected Universe Estimates            | 21 |
|   | Table II.1: Form 990 Returns Filed and Examined From 1985 to 1987       | 23 |

---

---

**Contents**

---

---

**Abbreviations**

|     |                           |
|-----|---------------------------|
| EO  | Exempt Organization       |
| GAO | General Accounting Office |
| IRS | Internal Revenue Service  |

# Introduction

Each year over 300,000 tax-exempt organizations file information returns with the Internal Revenue Service (IRS) as required by Internal Revenue Code Section 6033. Most tax-exempt organizations with gross receipts in excess of \$25,000 are required to file this "Return of Organization Exempt from Income Tax"—Form 990—annually. The Form 990 return provides IRS and the public with information concerning tax-exempt organizations' activities and their sources and uses of funds. In addition, 32 states accept the Form 990 return for state reporting purposes. IRS and the states use these Form 990 returns to administer the tax laws; the public uses this information, among other things, to determine how contributions are used by these organizations.

The Internal Revenue Code requires IRS to make Form 990 returns available for public inspection. In order to be useful for public inspection purposes these returns must be complete. To ensure completeness, IRS service center staff review the Form 990 returns when they are filed and correspond with organizations that file incomplete returns to obtain missing information. Once IRS has reviewed a Form 990 return for completeness and it has been processed, the return becomes available for public inspection, as well as for IRS' internal use.

## How IRS Provides Form 990 Returns to the Public

Internal Revenue Code Section 6104(b) requires that IRS make Form 990 returns filed by tax-exempt organizations available for public inspection. IRS requires that requests for Form 990 returns be made in writing to either the national office or to a district office and must include the name and address of the tax-exempt organization and the requested tax year. Upon receipt, these requests are sent to the appropriate IRS service center responsible for storing and retrieving the returns, and service center staff determine whether the requested returns have been filed and are available for public inspection.

If a requested return has been filed and is available, a copy of the return is made and sent to the requester or to the location, e.g., district office, where the requester wishes to review the return. If the requested return has been filed and is being used internally, IRS usually notifies the requester that the return is unavailable. If the requested return has not been filed, the requester is notified that there is no record of a return for that tax year.

Section 10702 of the Omnibus Budget Reconciliation Act of 1987 requires that certain tax-exempt organizations make their three most recent Form 990 returns available for public inspection at their offices

for years beginning after December 31, 1986. This provision of the act does not relieve IRS of the requirement for providing Form 990 returns for public inspection, and we believe the number of requests IRS receives may not decline substantially. Under the law tax-exempt organizations are only required to make their returns available for inspection at their offices; they are not required to send copies of the returns to requesters. Thus, individuals who are unable to visit those offices or unable to obtain copies directly from exempt organizations must turn to IRS. Also, we believe that many requesters may prefer the anonymity of obtaining a return for review directly from IRS, a third party, rather than reviewing the return at the office of the organization of interest.

IRS does not maintain annual statistics concerning the number of requests for copies of Form 990 returns received from the public or the number of returns provided. As a result, we were unable to determine how many requests for Form 990 returns IRS receives or provides annually nationwide.

---

## How IRS Processes Form 990 Returns

IRS service center staff review and process the Form 990 returns received from tax-exempt organizations. Before review and processing, they microfilm returns of organizations with assets of \$10 million or more and maintain a file of the filmed returns at the service center. They use this microfilm file to provide copies of requested Form 990 returns listing assets of \$10 million or more because these returns seem to be the ones most often requested by the public, according to IRS officials.

Service center staff review Form 990 returns for completeness using Incomplete Returns Program criteria contained in the Internal Revenue Manual. These criteria require service center staff to (1) review the completeness of Form 990 return line items that IRS considers necessary to meet statutory reporting requirements and (2) correspond with tax-exempt organizations that fail to provide complete information concerning these line items. For example, if an organization fails to complete the section of the return concerning compensation paid to officers, service center staff will correspond with the organization to obtain the missing information. Some other line items that require correspondence with the organization if incomplete include revenues and expenses, assets and liabilities, and lobbying activities. IRS does not include in its Incomplete Returns Program criteria various supporting schedules required by the Form 990 instructions, such as a description of various investments or the amount of payments to affiliated organizations.

Service center staff said that they correspond a maximum of twice with tax-exempt organizations to obtain missing return information. If they do not receive the information within 45 days of the second request, they process the organization's Form 990 return and assess the organization a delinquency penalty of \$10 a day, not to exceed \$5,000.

---

## Objectives, Scope, and Methodology

The Subcommittee on Commerce, Consumer, and Monetary Affairs, House Committee on Government Operations, asked us to determine whether (1) IRS can locate and provide requested Form 990 returns to the public and (2) Form 990 returns filed by tax-exempt organizations are complete.

To accomplish our objectives, we selected a stratified random sample of 450 Form 990 returns from a universe of 74,503 tax year 1986 returns filed at three IRS service centers. We used IRS' Exempt Organization Business Master File to obtain our sample because it contains a listing of all tax-exempt organizations with a Form 990 return filing requirement.<sup>1</sup>

We provided IRS with the name and employer identification number for the requested sample returns as shown by IRS' master file and asked IRS to retrieve the returns for us. The Form 990 return filing instructions say requesters should provide IRS with the name and address of the organization for which the Form 990 return is requested. IRS officials said that requesting a return using a name other than the correct organizational name impedes IRS' ability to provide a requested return, because IRS' computer search capabilities depend on the correct organizational name. If a requester supplied IRS with the correct organizational name, as shown on the master file, we believe IRS could accurately obtain the corresponding employer identification number. Therefore, we supplied IRS with the name and the corresponding employer identification number that we obtained from the master file.

We selected 150 sample returns each from the Brookhaven, Cincinnati, and Fresno Service Centers. Of the 150 returns from each service center, we selected 50 returns from each of three income ranges: \$25,000 to \$499,999; \$500,000 to \$9,999,999; and \$10,000,000 and greater. We

---

<sup>1</sup>Although the IRS master file contains a complete listing of over 300,000 tax-exempt organizations that file Form 990 returns each year, we limited the size of our sample universe by the following: (1) we selected returns from three of the seven IRS service centers that process Form 990 returns; (2) we selected returns with gross receipts of \$25,000 or greater; and (3) we selected returns for 1986. We selected 1986 because it was the most recent year for which essentially all Form 990 returns had been posted to the master file.

stratified the sample because the Subcommittee was interested in knowing whether the completeness of a Form 990 return was related to the size of a tax-exempt organization. (See app. I for a detailed description of our sampling methodology.)

The results of our sample are representative of the Form 990 returns filed at the three service centers for tax year 1986. Although estimates based on this sample can only be projected to these three service centers, IRS officials said that the results obtained at these service centers should reflect the nationwide retrievability and completeness of Form 990 returns. We selected these three service centers because they received about half of the Form 990 returns filed nationwide by tax-exempt organizations with income over \$25,000 for tax year 1986 and for their geographic distribution.

To evaluate whether IRS could locate and provide requested Form 990 returns, we compared the returns IRS provided to the list of returns we requested. For returns not provided, we obtained reasons from IRS as to why they were unavailable. Because IRS officials said that most of the unavailable returns were being used by Statistics of Income or Exempt Organization Examination staffs, we contacted officials from these offices to verify that their staffs were in fact using these returns.

To evaluate whether Form 990 returns filed by tax-exempt organizations were complete, we reviewed the copies of the sample Form 990 returns that IRS provided, as well as related correspondence files maintained at the respective service centers. We determined whether each tax-exempt organization had filed a complete return with IRS and evaluated actions taken by IRS to obtain complete returns. We used IRS' Incomplete Returns Program criteria to determine whether the sample returns were complete. We also reviewed the returns to determine whether all supporting schedules required by IRS' instructions for Form 990 returns were provided. Such supporting schedules, although required by Form 990 filing instructions, are not a part of IRS' Incomplete Returns Program criteria.

The Subcommittee also asked us to describe how IRS selects Form 990 returns for examination and ensures that tax-exempt organizations file required Form 990 returns. We discussed these issues with national office, district office, and service center staffs responsible for the Form 990 examination and compliance programs. Appendix II describes the examination program, and appendix III describes the compliance program.

---

We did our field work from May 1987 through February 1988 at the IRS National Office; the Brooklyn, Cincinnati, and Los Angeles District Offices; and the Brookhaven, Cincinnati, and Fresno Service Centers. We did our work in accordance with generally accepted government auditing standards. We obtained IRS' official comments orally on a draft of this report, and those comments are highlighted on pages 15 and 19.

# Annual Information Returns Could Usually Be Located and Made Available

IRS could usually locate and make available a requested Form 990 return if provided the name the organization used to obtain tax-exempt status. Of the 1986 Form 990 returns filed at the three service centers we visited, we estimate that IRS would make available about 95 percent of those requested. Most of the returns not made available would be "in use" within IRS. We believe these returns should be copied and also made available.

## Information Returns Could Be Located

IRS' Form 990 return filing instructions indicate that requesters must provide the name and address of the organization for which a Form 990 return is requested. IRS service center staff said that failure of requesters to provide a correct organization name impedes their ability to determine whether the requested return is available, because IRS' computer research capabilities are dependent on receiving the correct organization name.

Using the correct organizational name from IRS' exempt organization master file, we requested, from 74,503 tax year Form 990 returns filed at IRS' Brookhaven, Cincinnati, and Fresno Service Centers, a sample of 450 returns. Of these, IRS was able to locate 443 returns. Projecting these sample results to the 74,503 returns filed at the three service centers, we estimate that IRS could locate about 99 percent of the requested returns.

IRS provided us with 382 of the 443 returns it was able to locate. Of the 61 returns that IRS had located but did not provide, 59 were being used internally by either Statistics of Income or Exempt Organization (EO) Examination, and 2 were located but inadvertently not provided. Projecting these sample results to the 74,503 returns filed at the three service centers, we estimate that IRS would provide about 95 percent of them. Statistics of Income and EO Examination staffs would be using most of the returns not provided.<sup>1</sup>

<sup>1</sup>These estimates are based on weighted sample data. Appendix I includes a detailed description of how the sample data were stratified and the weights used for the projections. Table I.2 of appendix I provides confidence limits for these and other numbers used in this report.

## Located Returns Are Not Always Made Available

According to service center staff, requested Form 990 returns are frequently being used by either Statistics of Income or EO Examination. Each year IRS' Statistics of Income staff review a sample of Form 990 returns to develop statistical data concerning tax-exempt organizations' finances. Also, EO Examination staff in district offices review individual Form 990 returns each year to determine whether tax-exempt organizations have complied with the tax laws. Although service center staff can identify when a requested Form 990 return is being used by these staffs, they generally do not retrieve and provide these returns to requesters unless the organization has assets of \$10 million or more and the return is on the service center microfilm file.

None of the service centers we visited had regularly obtained copies of requested returns from Statistics of Income. Although staff at one service center have recently attempted to do so, they said it was too soon to determine whether such efforts would be successful. According to staff at the other two service centers, specific procedures to obtain copies of returns from Statistics of Income have not been established and, because the returns were being used by Statistics of Income staff at another service center, they did not attempt to obtain copies. Rather, requesters were informed that these returns were unavailable at the time of the request and could be requested at a later date.

Only one of the service centers we visited had regularly obtained copies of requested returns from EO Examination, according to service center staff. Staff at the other two service centers advised us that past efforts to obtain copies of returns from EO Examination had limited success. Usually, they either did not receive copies of the requested returns or they did not receive them in a timely manner.<sup>2</sup>

Internal Revenue Manual 1272, Disclosure of Official Information Handbook, Chapter 900, Section 9(12)0(9), states that "service center processing should include all actions necessary to secure a copy of a requested return or to establish that the return cannot be located." Section 9(12)0(11) further states that "adequate research and retrieval action will be taken to secure a return or to conclude that despite a thorough search, it cannot be located."

<sup>2</sup>Internal Revenue Manual 1272, Disclosure of Official Information Handbook, Chapter 900, Section 9(12)0(8), states that "service center processing of requests of EO returns should be completed within a maximum of thirty workdays from receipt."

---

Discussions with National Office Statistics of Income officials indicated that copies of Form 990 returns being used by their staff could be made available for public inspection. Exempt Organization officials at the National Office and at the three district offices we visited also said copies of requested Form 990 returns being used by EO Examination staff could be made available to meet IRS' public inspection responsibilities.

---

## Conclusions

IRS could usually locate and provide a requested Form 990 return if the requester furnished IRS with the name the organization used to obtain tax-exempt status. IRS officials indicated that failure to receive the correct organizational name from requesters impedes their ability to determine whether a return is available. Most of the returns IRS did not provide were being used by other IRS components. Officials from the principal IRS users of these returns—Statistics of Income and EO Examination—told us that with a procedural change, they could provide copies of the returns to service center staff for public inspection purposes. The Internal Revenue Manual requires IRS service center staff to take all actions necessary to obtain a copy of a requested return. With a minimal effort, we believe IRS could provide copies of returns being used internally, thus better fulfilling its responsibilities under Internal Revenue Code section 6104(b).

---

## Recommendation

We recommend that the Commissioner of Internal Revenue establish procedures to ensure that copies of requested Form 990 returns being used internally are provided to requesters.

---

## Agency Comments

IRS officials agreed with our recommendation in oral comments on September 19, 1988, and said they will implement our recommendation to ensure that copies of requested Form 990 returns being used internally are provided to requesters.

# Annual Information Returns Are Often Missing Supporting Schedules

The annual Form 990 returns that IRS provides to requesters are often missing supporting schedules. We estimate that about 48 percent of the tax year 1986 Form 990 returns at the service centers we visited were missing required supporting schedules, even though about 95 percent of the tax year 1986 returns were complete according to IRS' Incomplete Returns Program criteria. As a result, many Form 990 returns lacked detailed information that could have been used by IRS, the states, and the public to oversee tax-exempt organizations' activities and their sources and uses of funds.

## Many Different Supporting Schedules Were Missing

We reviewed the 382 sampled Form 990 returns we received from IRS to determine whether they were complete, including applicable supporting schedules, and found that 173 sample returns were missing one or more supporting schedules. On the basis of these results, we estimate that about 33,796, or 48 percent, of the 70,703<sup>1</sup> Form 990 returns that would be provided to requesters would lack one or more supporting schedules. Table 3.1 lists the supporting schedules most frequently missing.

**Table 3.1: Frequently Missing Supporting Schedules<sup>a</sup>**

| Supporting schedule   | Number of returns requiring the schedule | Percent missing |
|---|--|-----------------|
| Receivables due from officers, directors, trustees, and key employees | 11                                       | 71.9            |
| Investments—land, buildings, and equipment                            | 26                                       | 60.2            |
| Payments to affiliates  | 16                                       | 55.0            |
| Special fund-raising events and activities                            | 63                                       | 48.9            |
| Mortgages and other notes payable                                     | 130                                      | 41.2            |
| Gross sales minus returns and allowances                              | 56                                       | 39.3            |
| Land, buildings, equipment, and accumulated depreciation              | 248                                      | 38.5            |
| Support and revenue designated for future periods                     | 47                                       | 39.0            |
| Investments—securities  | 115                                      | 35.4            |

Note: Appendix IV contains a list of the supporting schedules required by the Form 990 instructions.

<sup>a</sup>Includes all schedules missing at least 35 percent of the time they were required. Supporting schedules are required when the organization has an entry for the corresponding line item on the Form 990.

Source: GAO analysis of sample Form 990 returns.

Applying IRS' Incomplete Returns Program criteria to the sample returns, we estimate that 95 percent of the tax year 1986 Form 990

<sup>1</sup>This figure is our estimate of the number of Form 990 returns IRS would locate and make available to requesters from 74,503 tax year 1986 Form 990 returns filed at the Brookhaven, Cincinnati, and Fresno Service Centers.

returns filed at the three service centers would have been classified as complete by IRS. We found no major differences among small, medium, and large tax-exempt organizations in the extent to which their returns included supporting schedules or would be classified as complete by IRS' Incomplete Returns Program criteria.

Because supporting schedules are not included as part of IRS' Incomplete Returns Program, IRS service center personnel do not correspond with tax-exempt organizations to obtain missing supporting schedules. Exempt Organization Examination staff at IRS' National Office and the district offices we visited said that an examining agent attempts to obtain missing supporting schedules during an examination of the organization's Form 990 return. However, since less than 5 percent of Form 990 returns are examined annually, IRS does not usually obtain the supporting schedules missing from most returns.

---

## Supporting Schedules Needed for Returns to Be Complete

Internal Revenue Code Section 6033(b) requires tax-exempt organizations to provide IRS certain information annually, such as income and expenses. It also authorizes IRS to request other information considered necessary to carry out the internal revenue laws. IRS, in issuing instructions for completing Form 990, has determined that detailed supporting schedules for various line items are necessary to ensure complete public disclosure and for federal and state tax administration purposes.

Supporting schedules can provide valuable information for public disclosure purposes. For example, if an organization has investments, IRS requires a detailed schedule describing each investment, including either the investment's cost or year-end market value. If an organization makes payments to affiliates, it must include a schedule listing the name and address of each affiliate receiving a payment, as well as the amount and purpose of the payment. Special fund-raising events and activities also require a supporting schedule. The gross receipts, direct expenses, and net income attributable to each of the three largest fund-raising events must be reported. The total for each of these supporting schedules appears as a line item on the Form 990. Without the supporting schedule, however, the usefulness of the return for public disclosure purposes is limited. IRS could enhance public disclosure by ensuring that it receives required supporting schedules. The schedules would be available from IRS, and we believe an exempt organization would be more likely to make them available to a requester if he or she goes directly to the organization to review the Form 990 return, an option now generally available under the law.

Supporting schedules are also extremely useful for tax administration purposes. National Office Exempt Organization officials said the supporting schedules are important to IRS, various states, and the public in overseeing the activities of tax-exempt organizations because they provide a more complete description of these organizations' sources and uses of funds. EO Examination staff and many states use the supporting schedules to determine tax-exempt organizations' compliance with tax laws. Thirty-two states accept the Form 990 return for state reporting purposes, and IRS requires some of the supporting schedules because of agreements with these states. Also, EO Examination staff consider whether supporting schedules have been provided when deciding whether to examine a return. One official told us that returns lacking supporting schedules usually receive greater scrutiny in the examination selection process, because the failure to provide information may be an indication that the organization is attempting to conceal information.

If IRS were to receive all supporting schedules from organizations required to submit them, the information on the schedules would be useful for selecting and screening returns for examination. IRS has developed computerized formulas to identify potentially noncompliant tax-exempt organizations that take into account Form 990 return line items that IRS has determined historically result in significant compliance problems. Supporting schedules could provide additional information that IRS eventually could incorporate into its examination selection formulas to help identify such noncompliant organizations.

---

## **Obtaining Missing Supporting Schedules**

IRS excluded Form 990 supporting schedules from its Incomplete Returns Program in order to reduce the amount of time, and therefore costs, service center staff spend reviewing the returns for completeness. If IRS took steps to obtain all of the required schedules missing from Form 990 returns, it would incur certain additional costs, primarily the costs of reviewing the returns to identify which schedules are missing and corresponding with organizations to obtain the missing schedules. We believe, however, these costs would substantially diminish over time for several reasons. First, organizations would become aware that IRS was enforcing compliance with the requirement to provide supporting schedules, and, as a result, compliance would probably increase. Second, in the next few years, IRS plans to consolidate EO returns processing operations from the seven service centers currently doing the processing to three or four service centers. We believe staff at these centers, by concentrating on EO returns, would attain a greater familiarity with EO return requirements

and would become much more proficient at corresponding with exempt organizations for obtaining missing information and/or schedules.

---

## **Conclusions**

Many of the Form 990 returns that IRS considered complete were missing detailed supporting schedules that could be used by IRS, the states, and the public to oversee tax-exempt organizations' activities and their compliance with the tax laws. To ensure that Form 990 returns filed by tax-exempt organizations provide full disclosure, we believe IRS service center staff should ensure that tax-exempt organizations provide Form 990 return supporting schedules, just as they do for other information on the Form 990 return through the Incomplete Returns Program. Although there would be some additional cost for ensuring that supporting schedules have been provided, we believe such costs would diminish over time as compliance improves. Also, we believe obtaining missing supporting schedules would aid EO Examination staff in selecting Form 990 returns for examination.

---

## **Recommendation**

We recommend that the Commissioner of Internal Revenue expand the criteria for the Incomplete Returns Program to ensure that missing Form 990 return supporting schedules are obtained from tax-exempt organizations.

---

## **Agency Comments**

IRS officials agreed with our recommendation in oral comments on September 19, 1988, and said they would implement our recommendation to ensure that missing Form 990 return supporting schedules are obtained from tax-exempt organizations.

# Sampling Methodology and Statistical Projections

This appendix describes how we selected our sample of IRS Form 990 returns and how we projected the sample data. Statistical sampling errors for the major figures in the report are included in this appendix.

## Sample Selection

Initially, we extracted a listing of the Form 990 returns from the IRS Master File of Tax Exempt Organizations for tax year 1986, the latest year for which essentially all Form 990 returns had been posted to the master file. The master file includes all tax-exempt organizations that file Form 990 returns. Then we selected returns filed at three IRS Service Centers: Cincinnati, Ohio; Fresno, California; and Brookhaven, New York.

We selected these centers for inclusion in our review because about half of all Form 990 returns for organizations with income in excess of \$25,000 are filed at these three centers and because of their geographic distribution. The results of our analysis are representative of the three service centers selected for tax year 1986 returns.

To ensure sufficient representation of organizations at varying income levels, we stratified our sample according to three income ranges: \$25,000 to \$499,999; \$500,000 to \$9,999,999; and \$10,000,000 and greater. We excluded returns of organizations with incomes less than \$25,000 in 1986 because they were not required to file returns.

We randomly selected 150 Form 990 returns from each service center, 50 from each income level. Table I.1 presents the locations and income levels from which our samples were drawn.

**Table I.1: Sample Size by Service Center and Organization Income Level**

| Income level          | Service center |            |            | Total      |
|-----------------------|----------------|------------|------------|------------|
|                       | Brookhaven     | Cincinnati | Fresno     |            |
| \$25,000-\$499,999    | 50             | 50         | 50         | 150        |
| \$500,000-\$9,999,999 | 50             | 50         | 50         | 150        |
| \$10,000,000 or more  | 50             | 50         | 50         | 150        |
| <b>Total</b>          | <b>150</b>     | <b>150</b> | <b>150</b> | <b>450</b> |

The results of our analysis are representative of 74,503 Form 990 returns from the three service centers selected. This universe does not include 451 high-income organizations we inadvertently omitted from the sample universe. Because the omitted organizations represent less

than 1 percent of the universe, we believe that the impact of this omission is negligible and would therefore not affect the validity of the conclusions that we have drawn.

**Projection of Sample Results**

Each of the 450 Form 990 returns represents a portion of the larger universe, and we projected the data from these returns to the universe in proportion to their size in the universe. This allows us to estimate the universe statistics on the basis of the sample statistics.

**Sample Errors**

We computed sampling errors for all estimates in our review. Our sampling plan was designed to provide a sample size that would yield an expected sampling error of not greater than 5 percent at the 95 percent confidence level. However, the actual sampling error for any characteristic, such as the number of returns lacking supporting schedules, depends upon the percentage of the sample having that characteristic and the variance of the characteristic. Table I.2 presents the sampling errors for the major figures in this report.

**Table I.2: Confidence Limits for Selected Universe Estimates**

| Description of item   | Confidence interval (95 percent) |             |             |
|---|----------------------------------|-------------|-------------|
|   | Universe estimate                | Lower limit | Upper limit |
| Percent of requested returns provided (p. 13)                                   | 94.9                             | 92.5        | 97.3        |
| Percent of returns lacking supporting schedules (p. 16)                         | 47.8                             | 41.2        | 54.3        |
| Number of returns provided (p. 16)  | 70,703                           | 68,915      | 72,491      |
| Number of returns lacking supporting schedules (p. 16)                          | 33,796                           | 29,130      | 38,392      |
| Percent of returns complete according to IRS Incomplete Returns Program (p. 16) | 94.7                             | 91.8        | 97.6        |

# Form 990 Examination Program

Form 990 returns are examined by Exempt Organization staff in various district offices and may be selected for examination in several ways. First, tax-exempt organizations that have filed Form 990 returns may be selected for examination if they meet a profile of potential highly noncompliant organizations on the basis of an analysis of specific Form 990 return line items. IRS has developed formulas to identify potentially noncompliant organizations that take into account Form 990 return line items that IRS has determined historically result in significant compliance problems.

Second, Form 990 returns may be selected for examination as part of a Taxpayer Compliance Measurement Program. In such a program, IRS selects a random sample of returns for detailed examination to determine taxpayer compliance characteristics and to update and improve its selection formulas. IRS completed a Taxpayer Compliance Measurement Program for Form 990 returns in 1985, and related adjustments to the formulas became effective in January 1987.

Third, Form 990 returns may be selected for examination as part of a special emphasis program targeting specific types of organizations. For example, fiscal year 1988 program objectives include special emphasis examinations for organizations exempt from income tax under Internal Revenue Code Sections 501(c)(3) or 501(c)(4) and involved in lobbying and political activities.

Finally, Form 990 returns may be selected for examination as a result of information received from other sources, such as the general public or other IRS functions, suggesting that a tax-exempt organization may not be operating in accordance with the purposes for which it was granted tax-exempt status.

The main focus of Form 990 return examinations is threefold: to ascertain that (1) tax-exempt organizations are operating in accordance with the purposes for which they received tax-exempt status; (2) all unrelated business income has been reported for tax purposes; and (3) individuals associated with the organizations, such as officers, are not personally benefiting from the assets and income of the organizations.

The number of Form 990 returns filed and examined by IRS between 1985 and 1987 is shown in table II.1.

---

**Appendix II**  
**Form 990 Examination Program**

---

**Table II.1: Form 990 Returns Filed and Examined From 1985 to 1987**

| <b>Year</b> | <b>Form 990s filed</b> | <b>Form 990s examined</b> |
|-------------|------------------------|---------------------------|
| 1985        | 345,473                | 11,835                    |
| 1986        | 345,141                | 12,706                    |
| 1987        | 376,570                | 10,179                    |

Source: IRS Exempt Organization statistical reports.

---

# How IRS Assures That Form 990 Returns Are Filed

---

When IRS determines that an organization is tax-exempt, district office staff establish an account that indicates whether the organization has a Form 990 return filing requirement and includes the organization's accounting period ending date.

If a tax-exempt organization with a Form 990 return filing requirement fails to file a return within 5-1/2 months after the end of its accounting period, the organization is listed on a computer tape of delinquent filers. The tape is sent to the appropriate service center and is used to generate failure-to-file notices that are sent to the delinquent organization.

A tax-exempt organization with a Form 990 return filing requirement may receive up to four failure-to-file notices. If the organization fails to respond to IRS with either a return or a satisfactory reason why a return has not been filed, it is referred to the Collection Division for a taxpayer delinquent investigation. If the Collection Division does not secure the delinquent return, the organization is referred to district office Exempt Organization staff for potential revocation of the organization's tax-exempt status. IRS officials at one of the service centers we visited said that most organizations file the required return after receiving a failure-to-file notice.

Every 3 years IRS also contacts tax-exempt organizations that are not required to file a Form 990 return because their gross receipts are normally less than \$25,000. At this time, the organization must certify that its annual gross receipts remain below \$25,000.

# Form 990 Return Line Items Requiring a Supporting Schedule

| <b>Form 990 line number</b> | <b>Schedule name</b>  |
|-----------------------------|---|
| Line 8                      | Gross amount from sale of assets other than inventory                 |
| Line 9                      | Special fund-raising events and activities                            |
| Line 10                     | Gross sales minus returns and allowances                              |
| Line 16                     | Payments to affiliates  |
| Line 20                     | Other changes in fund balances or net worth                           |
| Line 22                     | Grants and allocations  |
| Line 42                     | Depreciation, depletion, etc.   |
| Line (e)                    | Other program service activities rendered                             |
| Line 50                     | Receivables due from officers, directors, trustees, and key employees |
| Line 54                     | Investments—securities  |
| Line 55                     | Investments—land, buildings, and equipment                            |
| Line 56                     | Investments—other   |
| Line 57                     | Land, buildings, equipment, and accumulated depreciation              |
| Line 62                     | Support and revenue designated for future periods                     |
| Line 63                     | Loans from officers, directors, trustees, and key employees           |
| Line 64                     | Mortgages and other notes payable                                     |







---

Requests for copies of GAO reports should be sent to:

U.S. General Accounting Office  
Post Office Box 6015  
Gaithersburg, Maryland 20877

Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

---

United States  
General Accounting Office  
Washington, D.C. 20548

Official Business  
Penalty for Private Use \$300

First-Class Mail  
Postage & Fees Paid  
GAO  
Permit No. G100

---