

## A Form 990 Audit: What Triggers It?

10.10.17 | Linda J. Rosenthal, JD



It's a classic "cart before the horse" scenario.

Last year, in our 6-part *When the Revenue Agent Comes Calling* series, we discussed how the government official will use the IRS's [Form 14114](#), "Governance Check Sheet," to conduct an audit of your organization:

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*An IRS revenue agent knocking at the door of a 501(c)(3), tax-exempt, organization will have in hand that agency's Form 14114 , Governance Check Sheet, that includes six sections of questions that must be covered during the audit – (1) [Governing Body and Management](#); (2) [Compensation](#); (3) [Organizational Control](#); (4) [Conflict of Interest](#); (5) [Financial Oversight](#); and (6) [Document Retention](#)”*

But why, exactly, are they knocking at **your** door?

### What Triggers An Audit?

Each year, the Tax Exempt and Government Entities Division of the Internal Revenue Service issues a work plan for the upcoming fiscal year. The [plan in effect currently](#) was released in late September 2016 and then amended in March 2017.

In the nine months ended June 30, 2016, the IRS reported that it “examined” – that means “audited” – almost 5,000 nonprofit organizations. For 43 of these groups, it was not good news: their tax exemptions were revoked.

Why is an organization selected for examination? There may be a reason or no reason at all.

Some Form 990s are selected entirely at random. That's done partly to double-check that the formal audit-triggering criteria are effective and reasonable.

Otherwise, there are selection guidelines and factors. The *Tax Exempt and Government Entities FY 2017 Work Plan* is, according to the IRS, part of a "...compliance strategy to ensure organizations enjoying tax-exempt status complied with the requirements for exemption." This process is described as "data-driven" to focus in on "existing and emerging high risk areas of noncompliance" including:

- Private Benefit and Inurement
- Political Campaign and Lobbying Activities
- Unrelated Business Income and Employment Tax
- International Activities (including spending money outside the U.S.)

## *Form 990 Red Flags*

The "ultimate 'formula' for how the IRS assesses risk in selecting organizations for examination remains a secret," but the agency has revealed examples that can trigger an audit:

- "Information on a filed return (Forms 990-EZ, 990, 990-T, or 990-PF) appears to be inconsistent or incomplete.
- IRS receives a complaint (referral) from the public or a federal or state regulatory agency about potential noncompliance by an exempt organization.
- The Exempt Organizations Division participates in an IRS-wide examination initiative, such as initiatives generated by the National Research Program.
- Related returns may be selected for audit when they involve issues or transactions with other taxpayers, such as business partners or investors.
- One of the IRS' document matching programs identifies a discrepancy between information reported by a payor and payee, such as on Forms 1099 or W-2.
- A claim for refund or request for abatement requires further review."

"In some circumstances," the agency cautions, "an exempt organization may be selected for audit or review even though it has not filed a return, either because it has no filing requirement or it has not filed a required return."

For more information, the agency refers you right back to that *Tax Exempt and Government Entities FY 2017 Work Plan*.

## *Conclusion*

Of course, "the best chance to avoid an audit and/or successfully survive an audit is to demonstrate continued compliance with IRS regulations."