

THE PPC NONPROFIT UPDATE

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Document Retention and Destruction Policy



Every tax-exempt organization (EO) must adopt a document retention and destruction (DRD) policy. The DRD policy should create an ongoing, coordinated administrative effort to systematically manage documents and records. The purpose of the DRD policy is to ensure that documents are secure, accessible, maintained, and destroyed according to business practices that are practical, while still meeting the legal requirements applicable to the EO. It should assure that authorized individuals have access to all organizational documents. The policy should provide guidelines for the retention and destruction of paper documents, text messages, voice mail, social media sites, and other electronic files, as well as how to store and destroy computer backup files. The policy should also require that document destruction cease upon notification of a federal investigation or lawsuit. If the DRD policy is followed, it should provide a defense to employees accused of wrongful destruction of documents.

The policy should balance retaining the documents necessary for business or

legal purposes and destroying documents that no longer have value for the EO. When creating the schedule of destruction, the EO should consider the risks the organization faces and how retaining documents manages or minimizes those risks. Since the statutes of limitations for various risks vary greatly under both federal and state laws, the EO's attorney should review and approve the EO's schedule of destruction.

Retention Guidelines

Documents should be maintained until the end of the identified retention period and should then be destroyed in an appropriate manner.

Corporate Records

- Board and committee meeting agendas and minutes—Permanent
- Bylaws and Articles of Incorporation—Permanent
- Conflict-of-interest disclosure forms—5 years
- Corporate resolutions—Permanent
- Correspondence on legal, insurance, and important matters—Permanent

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- Correspondence-general—4 years
- Trademark registrations, patents, and copyrights—Permanent

Finance and Administration Records

- Accounts payable and receivable ledgers—7 years
- Annual grant listing—Permanent
- Auditor management letters—7 years
- Authorization for expenditures—3 years
- Bank deposits and deposit statements—7 years
- Bank statements and reconciliations—10 years
- Chart of accounts—7 years
- Check register and checks—7 years
- Checks for important expenditures—Permanent
- Contracts and agreements—7 or 10 years after all obligations end
- Correspondence-general—3 years
- Depreciation schedules—Permanent
- Donation records, except for those records related to endowment funds or significant restricted funds—10 years
- Donation records for endowment funds and significantly restricted funds—Permanent
- Donor credit card information—Retain as required by merchant agreements
- Equipment files and maintenance records—7 years after disposition
- Expense analysis/distribution schedules—7 years
- Financial statements (audited and year-end prepared in house)—Permanent
- General ledgers—Permanent
- Internal reports-miscellaneous—3 years
- Inventory reports—Permanent
- Investment performance reports—7 years
- Invoices (from vendors or to customers)—7 years
- Payroll records and summaries—7 years
- Retirement and pension records—Permanent

Insurance Records

- Accident reports—Permanent
- Claims (after settlement)—7 years
- Group disability records—7 years after end of benefits
- Policies—claims-made type—Permanent
- Policies—occurrence type—Permanent
- Safety (OSHA) reports—7 years

Real Estate

- Building and site drawings—Permanent
- Deeds — Permanent
- Leases (expired)—Permanent
- Mortgages and security agreements—7 years after all obligations end

Tax

- Charitable Organizations Registration Statements (filed with State Attorney Generals)—7 years
- Correspondence from IRS or any taxing authority—Permanent
- Forms 1099—Permanent
- Forms 941—Permanent
- Forms W-2/W-3—Permanent
- IRS exemption determination and related correspondence—Permanent
- IRS Forms 990—Permanent
- IRS Forms 990-T plus all related worksheets—Permanent
- Sales tax returns—Permanent

Human Resources

- Background checks—Permanent
- Employee handbooks—Permanent
- Employee orientation and training materials (for all who work with children or youth)—Permanent
- Employee orientation and training materials (for all others)—7 years
- Employee personnel files (for all who work with children or youth)—Permanent
- Employee personnel files (for all others)—7 years after termination
- Employment applications—3 years
- IRS Form I-9 (store separate from personnel file)—Greater of 1 year after end of service or 3 years
- Retirement plan benefits (plan descriptions, plan documents)—Permanent
- Timecards—3 years
- Volunteer records (if the volunteer works with children or youth)—Permanent
- Volunteer records (for all others)—3 years
- Withholding tax statements—7 years
- Workers comp claims (after settlement)—7 years

Technology

- Software licenses and support agreements—7 years after all obligations end
- Electronic documents (Microsoft Office, Adobe Acrobat, etc.)—Subject matter determines retention period
- Voice Mail—1 month in native form; subject matter determines period if transferred to a document management system
- Email—6 months in native form; subject matter determines period if transferred to a document management system

Document Security and Destruction

The EO is responsible for preserving the safety and confidentiality of the documents possessed. Documents should be maintained at the EO's offices to provide for their security and preserve their usefulness to the

organization. Without specific authority to the contrary, no documents should be retained in the personal possession of a director, officer, staff member, or volunteer, including being stored at a personal residence, on a personal computer, or as a part of a personal email account. Documents stored off premises or outside the control of the EO will not be considered a part of the organization's documents until properly secured by the EO. Security measures should be employed to ensure appropriate disclosure when confidential or private information is given to board members or others. Sensitive documents such as those containing financial, account, or personnel information should be destroyed with no reasonable risk of the information being recovered.

Electronic documents should be retained in the same manner as paper documents. Electronic documents created from paper documents may be retained rather than the paper copies as long as the documents are true and correct copies of the actual documents. Due to security issues, all hard drives located in computers, printers, scanners, and copiers are to be separately purged prior to the organization disposing of any machine.

Implementing the Policy

The DRD policy is only helpful if followed by the EO. By regularly scheduling the destruction of documents, the EO keeps its records as long as needed for legal or management purposes. Once a federal agency launches an investigation of the EO, or the EO is served with a lawsuit, the EO must *immediately suspend* its normal schedule of document destruction. The EO must work with its attorneys to determine the schedule of document destruction during pending investigations.

Practical Consideration:

Form 990, Part VI, asks about the existence of a written document retention and destruction policy. To answer affirmatively, the policy must be adopted by the end of the filing year of the EO. If a policy is not adopted by the governing body before the EO's year-end, but is in place before filing the annual return, the EO can disclose this information in Schedule O (Form 990 or 990-EZ), although the Part VI question must still be answered "No." The IRS allows the policy to be adopted by a properly authorized committee of the board. However, states may not allow this.

IRS Syncs Terms on Form 990 with Instructions

The IRS and the public are interested in loans both to and from an organization, grants or other assistance, and business transactions with an organization's movers and shakers. They are looking for private benefit and private inurement in organizations.

Both private benefit and private inurement can jeopardize exempt status. Additionally, Section 4958 excess benefit transactions (EBTs) in Section 501(c)(3), (c)(4), and (c)(29) organizations are subject to significant penalties.

Part IV, "Checklist of Required Schedules," of Form 990 contains what are referred to as the trigger questions. An affirmative answer to these probing questions may trigger a filing requirement for one or more of Schedules A through R.

Since 2014, portions of the language in the trigger questions for Schedule L on Form 990, Part IV, questions 26–28 have not matched the instructions. The instructions were changed in 2014 when the IRS harmonized the definitions used for Schedule L with the definitions used for Form 990, Part IV. However, the trigger questions have continued to reflect the previous language that erroneously referred to "highest compensated employees or disqualified persons."

The 2019 draft Form 990 includes corrected trigger questions on lines 26–28, Part IV, and now asks about transactions with the organization's interested persons (as harmonized by the IRS in 2014). An interested person can be a current or former officer, director, trustee, key employee, creator or founder, substantial contributor or employee thereof, a grant selection committee member, or a 35% controlled entity (including an employee thereof) or family member of any of these persons.



AICPA Issues Omnibus SAS 135—Part 2

As discussed in Part 1 of this article published in the November 2019 issue of *The PPC Nonprofit Update*, in May 2019, the AICPA issued SAS 135, *Omnibus Statement on Auditing Standards—2019*, which amends 13 sections of the Statements on Auditing Standards. The amendments result from the evaluation of three auditing standards that have recently been issued by the Public Company Accounting Oversight Board (PCAOB).

Changes relating to communications with audit committees (AU-C 260, *The Auditor's Communication With Those Charged With Governance*), related parties (AU-C 550, *Related Parties*), and significant unusual transactions (AU-C 240, *Consideration of Fraud in a Financial Statement Audit*) were discussed in the November 2019 issue. This article highlights some of the key changes in other AU-C sections made by the SAS to enhance guidance regarding related parties and significant unusual transactions.

Practical Consideration:

The SAS is on Checkpoint at checkpoint.riag.com.

Significant Unusual Transactions Terminology and Other Procedures

Most of the changes in the following SASs are conforming terminology changes related to significant unusual transactions:

- AU-C 265, *Communicating Internal Control Deficiencies Identified in an Audit*;
- AU-C 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*;
- AU-C 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*;
- AU-C 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*;
- and AU-C 940, *An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements*.

AU-C 330 also states substantive procedures that consider the types of potential misstatements that could

result from significant unusual transactions may be necessary when determining risks of material misstatement due to error or fraud.

Opening Balances Information from Predecessor Auditor

AU-C 510, *Opening Balances—Initial Audit Engagements, Including Reaudit Engagements*, includes an amendment to enhance guidance relating to obtaining information about related parties and significant unusual transactions from predecessor auditors.

Subsequent Events Information

AU-C 560, *Subsequent Events and Subsequently Discovered Facts*, includes an amendment intended to enhance guidance relating to obtaining information about subsequent events by expanding the list of possible inquiries to include related parties and significant unusual risks.

Related Party Representations

AU-C 580, *Written Representations*, and AU-C 930, *Interim Financial Information*, were amended to add several additional representations an auditor may want to obtain about whether—

- any related party transactions were conducted on terms equivalent to an arm's-length transaction.
- any written or oral side agreements or other arrangements exist that haven't been disclosed to the auditor.

Effective Date

SAS 135 is effective for audits of financial statements for periods ending on or after December 15, 2020. Early implementation is permitted.

Practical Consideration:

The practice aids in the 2019 edition of *PPC's Guide to Audits of Nonprofit Organizations* (NPO) were not updated for SAS 135 because the SAS had not yet been issued when that edition of NPO was released. The 2020 edition of NPO will have updated practice aids when it becomes available in the spring of 2020.



AICPA Issues SAS 137 on Other Information in Annual Reports

In July 2019, the AICPA issued SAS 137, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports*, which supersedes AU-C 720, *Other Information in Documents Containing Audited Financial Statements*. The superseded standard is now codified in AU-C 720A and SAS 137 is codified in AU-C 720.

The amendments result from the evaluation of three auditing standards that have been issued by the Public Company Accounting Oversight Board (PCAOB) since the AICPA's Auditing Standards Board (ASB) completed its auditing standards clarity project: AS 1301, *Communication With Audit Committees*; AS 2701, *Supplementary Information*; and AS 2410, *Related Parties*. The ASB determined that these PCAOB standards included guidance not found in current SASs that enhance audits of the financial statements of nonissuers, including nonprofit organizations. The new SAS is modeled after International Standard on Auditing (ISA) 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*.

The revised standard clarifies, but doesn't significantly change, existing guidance on the auditor's responsibility for other information. The following paragraphs discuss certain of the significant matters being made by the SAS.

Practical Consideration:

The SAS is on Checkpoint at checkpoint.riag.com.

What Is Other Information?

Under the extant standards, the ASB believes the auditor's procedures are frequently applied too broadly to other information, so SAS 137 seeks to clarify the scope of documents that would be subject to the auditor's procedures. The title of the revised standard is changed to focus the auditor on other information included in *annual reports*.

AU-C 720.12 defines an *annual report* as a document (or a combination of documents) prepared by management or those charged with governance, generally annually as required by law, regulation, or custom, to provide owners and/or other stakeholders with information about the entity's operations, financial results, and financial position. It contains, accompanies, or

incorporates by reference the financial statements, the auditor's report thereon, and often includes information about other developments, the entity's future outlook, risks and uncertainties, a statement from the entity's governing body, and reports covering governance matters.

AU-C 720.A9 notes that even if a document is referred to as an *annual report*, it might not meet the new definition. AU-C 720.13 requires the auditor to have a discussion with management and obtain a written acknowledgment as to which document(s) comprise the annual report and the manner and timing of issuance of those document(s).

What Are the Auditor's Objectives in Reading Other Information?

After reading the other information, AU-C 720.11 indicates that the auditor's objectives are to consider if there are material inconsistencies between (a) the other information and the financial statements and (b) the information and the knowledge that the auditor obtained during the audit. If one or more material inconsistencies exist or if the auditor becomes aware that the other information appears to be materially misstated, the auditor should respond appropriately. The SAS provides guidance on what constitutes a misstatement of other information.

Additionally, the SAS provides guidance regarding other information that may omit or obscure information that may be necessary to understand a matter. The SAS states, at AU-C 720.18, that the auditor is *not* responsible for testing the completeness of the other information.

What Is the Effect on the Report?

The new SAS requires the auditor's report to include a separate section with an appropriate heading such as "Other Information." Extant standards don't require the auditor to reference the other information in the auditor's report.

The other information report section should include the following information:

- A statement that management is responsible for the other information.
- Identification of the other information, specifically noting that it doesn't include the financial statements or auditor's report.
- A statement that the auditor's opinion doesn't cover the other information and the auditor expresses no opinion or assurance on it.
- A statement that the auditor is responsible for reading the other information, considering any

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material inconsistency with the audited financial statements or other material misstatements.

- A statement that any uncorrected material misstatements of the other information are required to be described in the auditor’s report.
- If applicable, a statement that the auditor has concluded that an uncorrected material misstatement of the information exists and a description thereof.

When Is the SAS Effective?

SAS 137 is effective for audits of financial statements for periods ending on or after December 15, 2020. Early implementation isn’t permitted.

Practical Consideration:

The practice aids in the 2019 edition of *PPC’s Guide to Audits of Nonprofit Organizations* (NPO) were not updated for SAS 137 because the SAS had not yet been issued when that edition of NPO was released. The 2020 edition of NPO will have updated practice aids when it becomes available in the spring of 2020.



Websites of Interest

The following websites may be of interest to the nonprofit sector.



[www.salsalabs.com/resources/nonprofit-best-practices;](http://www.salsalabs.com/resources/nonprofit-best-practices) www.salsalabs.com/blog

Salsa Labs is a technology company that develops fundraising, advocacy, and marketing engagement software for nonprofit organizations. In addition to marketing and sales efforts relating to its products, Salsa’s website offers some free resources that include best practices guides and videos. Topics include a campaign messaging tip sheet and an annual development plan checklist.

There’s also a blog with an assortment of interesting BuzzFeed-style articles (for example, “23 Strategies to Take Your Fundraising to the Next Level,” “21 Key Performance Indicators Nonprofit Management Needs to Track,” and “7 Tips for Creating an Awesome Nonprofit Website”). Finally, we even uncovered a compilation of 60 fundraising event ideas.

www.sos.state.tx.us/corp/nonprofit_org.shtml

The Texas Secretary of State webpage for nonprofit organizations provides information specific to Texas nonprofit organizations, including information related to tax issues and nonprofit resources.