

**Remarks of Steven T. Miller**  
**Commissioner, Tax Exempt and Government Entities**  
**Before the Los Angeles Benefits Conference**  
**January 28, 2005**

I want to thank you for inviting me. This is my first appearance in an Employee Plans forum since I took over from Evelyn Petschek as TE/GE Commissioner this past summer.

I am not new to benefits, but I am rather rusty. I started my career in the mid 80's with the Section 89 effort, along with a dash of pension funding and Medicare catastrophic issues.

I have come today for two reasons:

First – to begin my reacquaintance with the benefits community, and, second, to lend my personal support to these conferences. You have been, and I hope it will continue to be, a key partner in our work to ensure both the vitality and the compliant behavior of the benefits community.

I want to talk with you today about compliance. It is an important topic, a matter of special concern to the Commissioner and to Congress, and one that now receives a great deal of attention within the IRS.

My guess is that you have read about this concern in the tax press, and that it is already on your minds.

Let me begin, however, by offering some words of reassurance about the continuing respect that I have personally, and that we in TE/GE have institutionally, for the professionalism and dedication of the benefits community. We have long appreciated, and prided ourselves, on the close and cooperative relationship we have built up with the benefits practitioners. I very much want this relationship to continue.

We are going to help it continue by maintaining our robust outreach programs, a vigorous and improved determination program, our programs in which you come to us to correct problems, and our commitment to do all we can to help you and your clients comply.

However, I am sorry to say that the time has come to deliver a message to a small number within the benefits community who have begun to taint our important public purposes with abuse.

As I set out to deliver what I intend to be a strong message, I am confident that I am among friends and that we are of one mind about this. I know you recognize that in keeping our community compliant, and in rooting out abuse, we are creating the environment in which professionalism can flourish, in which we can live up to the highest standards of our professions, in which we can carry forward the important public mission that has been placed in our hands, and in which we can do our work without

concern that abusers and shady operators will steal our livelihoods by pandering to those who want easy, and clever, but ultimately destructive ways around the rules.

So I am here today to also discuss how the Employee Plans office of TE/GE needs to change in order to ensure that the IRS is effective in the future in its mission of promoting and protecting retirement benefits.

I will not surprise anyone if I say that in my view, in Carol Gold's view, and perhaps most importantly, in Commissioner Everson's view, EP does need to change direction.

How much it needs to change ultimately is something that time will tell. The change will certainly be less than 180 degrees, as I suggested a moment ago, but EP must change more than "ever so slightly."

Given that change is needed, in what direction must we steer, and how fast must we go to get to our destination?

In my mind, we need to rebalance our efforts with the goal of establishing a prominent IRS enforcement presence in the benefits community. And we need to do it at once.

Let me step back for a moment and put this in context.

You may be aware that the Commissioner has rebalanced the Service, moving it toward increased enforcement while at the same time maintaining our current level of service. He sees both enforcement and service as necessary for compliance. He also rightly observes that enforcement efforts have suffered in recent years.

Late last year, we published the IRS 2005 - 2009 Strategic Plan. One of the strategic goals of the Service over this period will be to "enhance enforcement of the tax law." To achieve that goal, the strategic plan establishes four specific Service-wide objectives. Two of these are especially relevant to this group today.

The first objective is noteworthy because, for the first time, the Service has recognized the singular importance of our sector – to the tax system as a whole and to the economy. As a result, one of the four IRS-wide objectives is to:

*Deter abuse within tax-exempt and governmental entities and misuse of such entities by third parties for tax avoidance or other unintended purposes.*

Trust me when I tell you that your clients are included in this objective.

The second objective supporting the strategic goal of enhancing enforcement of the tax law involves you personally, and your relationship with the Service. It is stated this way:

*Ensure that attorneys, accountants, and other tax practitioners adhere to professional standards and follow the law.*

It seems simple, and self-evident. It should not be a matter of pride to us as professionals that things have come to the point that this objective had to be expressed this way.

Bear these objectives in mind as I outline, first, the elements of our change in direction, and, second, some of the steps we are taking to implement those objectives.

You can see that our intention to enhance enforcement is in keeping with the strategic plan and Commissioner Everson's vision, but is this shift really necessary? Is it justified?

It is right on the mark.

Even if the strategic plan were not so plain, the need to boost enforcement is clear. And a directional shift is imperative.

Why is that?

Let me build the case for an invigorated enforcement program by laying out three rationales.

First, the TE/GE community, as we all know, is immense. There are more than 3 million plans and entities that TE/GE is responsible for. Collectively these plans and entities control more than \$8 trillion in assets, pay over \$300 billion in employment tax and income tax withholding, and employ more than 20% of the work force of the United States. Moreover, the annual federal tax expenditure for plans and entities within TE/GE's jurisdiction exceeds \$280 billion.

The Employee Plans component of this breaks down as follows: more than 950,000 plans with a filing obligation, assets of more than \$4 trillion, 99 million plan participants (not including IRAs, 457s, 403(b)s and the like), and a tax expenditure of \$146 billion.

We cannot afford to ignore or under-serve this huge slice of our economy. Nor can we be casual about such an enormous tax expenditure.

Second, we need to be involved with a vigorous enforcement program because we are finding increasing numbers of abusive transactions in every segment of the TE/GE community – every segment! It is difficult to say whether this increase reflects a prior uptick in abuse, a continuing and permanent increase in abuse, or whether we are just getting better at finding schemes and devices that have always been present. But it is not difficult to say that the abuse is there – and the increase in our workload is clear as well.

Our EP Examinations Director, Michael Julianelle, has already discussed our efforts in this area, but I will note that the EP community has not been immune to the lure of the huckster or the promoter.

Evidence of this is readily apparent when you look through the details of the “listed transactions.” Listed transactions are tax schemes the IRS has formally designated as abusive. When we list a transaction, the listing triggers special reporting requirements.

I am sorry to say that when we look at the current universe of 30 or so listed transactions, fully half of them involve, in one form or another, an entity that is a TE/GE customer. This is a real concern.

Some within the benefits community have played an unfortunate role – certain municipal pension plans acting as accommodation parties, Sub-S ESOPs, 401(k) plans, and 412(i) plans have all been involved in listed transactions.

And we are responding. Sixty ESOPs are under exam. We are working closely with the IRS’s Large and Mid-Size Business Division on the 401(k)s, and we have pulled an initial sample of thirty 412(i) cases for exam.

There also are abuses outside of the listed transaction area. To cite one example, we are currently examining management corporation ESOPs, and in December we expanded our look at ESOPs by sending out 1,700 soft contact letters, which will be followed up on.

I’ve just noted that abuse exists among TE/GE customers, but does that mean that I believe the benefits community is rife with abuse? No, I do not.

As I mentioned at the outset, I believe it is a distinct and very small number of individuals who have involved themselves and their plans in these deals. Moreover, I know that the overwhelming majority of those in this room, and throughout the professional benefits community, have had, and will have, nothing to do with those who set out to abuse the system.

Part of our job in government, however, is to ensure there are consequences for those who do go beyond what is reasonable.

The third and final rationale for our decision to re-invigorate the EP enforcement program is that we have been away from this work for too long.

Paul Shultz and Michael Julianelle discussed the impact that the GUST amendments had on our examination program. In 1999, we performed 14,066 employee plans exams. By 2003, that figure had fallen to 6,119 exams. That figure is less than half of what it should be, even for a modest examination program. In response to this trend, we committed ourselves to rebuilding our examination capability, and we already have made an impressive start. We will conduct 11,000 exams this year, and 12,500 next year.

In short, we are returning to the field of play.

This, in a nutshell, is why we needed to change direction in EP. The benefits community is big, it’s important, and it needs attention. Abuse, often abetted by disregard of

professional standards, had begun to appear in our midst. And our enforcement capabilities at the Service were beginning to atrophy.

In this part of my discussion, I would like to outline some of the steps we have begun taking in our effort to change direction. I'll talk about four areas where change is underway in Employee Plans:

- Increased resources,
- Infrastructure and business practice improvements,
- The Form 5500, and
- More exacting enforcement of standards of professional conduct in the benefits area.

Let's talk first about resources.

We will never have all the resources we could use – that is the nature of government. We are, however, moving in the right direction.

The 2005 budget for the Service showed a very small increase – less than 1 percent. This was, in fact, a bit of a cut.

Nonetheless, because of decisions made at the very top of the IRS, TE/GE is hiring this year, and we have a generous budget increase. Part of this increase will go to EP Examinations. We are going to hire 55 new EP agents this year. In addition, we will be building the EP compliance unit. The goal of this unit is to expand our compliance presence with a “soft contact” approach in such areas as pension underfunding and follow-up on voluntary compliance agreements. In the long term, we expect the unit to conduct correspondence examinations and to support our efforts to attack abusive tax schemes.

Thanks to the changes in the determination letter process that Paul Shultz discussed, we have established separate dedicated staffs for the Examinations and Determinations functions. This will give us a stable and increasingly experienced examinations workforce. This, in turn, will have a very real impact on the efficiency, quality, and consistency of the EP Examination Program.

The second area of change I want to discuss with you involves improvements to our infrastructure and the modernization of certain of our work processes. We are modernizing both our information technology systems and the ways we do business.

On the automation side we are working to arm our agents with everything they need to be more productive. This includes improving their ability to communicate with our internal systems when they are in the field and away from the office. It also involves fundamentally rebuilding the computer workstations that our EP agents use when they are out building an examination case.

Coming into this job, I would not have believed that among my greatest challenges would be providing oversight to Information Technology projects – but there you have it. Reduced to its essentials, my job is to ensure that our people get everything they need to succeed. And automation issues are critical to that.

On the business process side, I believe that TE/GE must improve the process we use to select and perform examination work. We need to be able to answer such questions as:

Are we selecting the right case?

Are we starting the examination quickly enough?

Are we getting it done quickly enough?

Are we learning from each contact with a taxpayer?

These are difficult questions, but we are at work on them.

Michael Julianelle talked to you about examination redesign, but let me reiterate some key work.

To improve case selection, we are looking at ways of mining data. We also are looking at starting cases earlier in time.

We are considering focused examinations where we will look at only a few issues – maybe only one. Michael described the ongoing pilot program that is testing this approach.

Automation will play a key role when combined with these new business practices. New systems are being built to capture information about issues under review while the exam is progressing. The results of the exam will be captured, too. We expect this to improve our ability to spot issues and resolve them appropriately, uniformly, and expeditiously. This is the learning part of the program.

The third area in which we are acting to enhance enforcement concerns Form 5500. Improving the utility and timeliness of Form 5500 is a critical initiative for us, as well as for the Department of Labor and the Pension Benefit Guaranty Corporation.

We are currently looking at whether we are putting the right questions on the form, whether we are getting appropriate and timely responses to the questions we do ask, and whether we have the budget to extract and make good analytical use of the responses.

The inadequacies of the Form 5500 have been apparent as the PBGC, the Department of Labor, and the Service try to address pension plan funding deficiencies.

The question is what we should do about the Form 5500 itself. It needs revision, and we need to look for ways to get information quicker, and with full research capability. An obvious way to accomplish this is electronic filing. This might or might not happen, but I think it is worthy of note that the IRS recently began requiring electronic filing for certain

corporations, charities and private foundations. Thus, there is recent precedent for this approach.

The last example of how we are changing to enhance enforcement that I want to address today is professional responsibility.

As I noted in my introduction, one of the Service's four key enforcement objectives is to promote professional responsibility. Now, I share the traditional view that the EP practitioner community does great work to keep plans on the straight and narrow.

The EP professional practitioner community, including the actuarial community, was well ahead of its time in developing and promoting self-audit procedures, whether it was the original voluntary compliance resolution program or the ever-evolving EPCRS.

It is obvious that appropriate practitioner behavior is an indispensable element of our approach toward the regulation of the EP community. And, for that reason, it has been an area of significant IRS focus. The IRS has recently published final regulations in the Circular 230 area.

Circular 230 continues to contain an exclusion from some of the tax shelter opinion rules for pension opinions. But lawyers, CPAs and actuaries who practice before us are still bound to the high standards contained in other parts of Circular 230 that apply to tax advice and practice.

Moreover, there is new vitality and an increased level of vigilance within the Office of Professional Responsibility, the IRS office that has responsibility for enforcing the practice rules. The Office of Professional Responsibility has been re-energized under the leadership of Cono Namorata and it is aggressively pursuing unethical and questionable professional behavior by practitioners.

Just as the Office of Professional Responsibility has been revitalized, so has the Joint Board for the Enrollment of Actuaries. It now has its own executive director and its own dedicated staff. It intends to provide improved service to enrolled actuaries – for example, it is prepared to make this year's renewal process much faster and smoother than it has been in the past. It is also dedicated to enforcing the disciplinary regime that applies to enrolled actuaries. In this regard, the Office intends to conduct 100 randomly selected audits each year to test compliance with CPE rules, and 100 audits to check tax return filing and tax payment compliance.

The Joint Board has also provided our EP managers and employees with briefings on the rules of practice for enrolled actuaries, and on how to make referrals to the Joint Board when violations are discovered.

The continuing challenge for all of us – for you as individual practitioners, and for me as Commissioner of TE/GE – is to ensure that those who do not follow reasonable practices are identified and appropriately sanctioned.

To the extent the bad actors are not sanctioned, or disbarred from practice before the Service, those of you – the overwhelming majority of you – who conduct your practices in an ethical manner, will find yourselves at a competitive disadvantage. And we, at the Service, faced with abuse in the EP area, will have to act broadly and boldly to crack down.

So I ask you for two things. First, if a brown envelope shows up on your desk inviting you or your clients to get involved with a deal that sounds too good to be true, please steer your clients away from it. And after you have done that, please forward the brown envelope and its contents to us. Let us move to level the playing field, and to level it along an ethical plane.

There is one other issue I would like to discuss in the area of professional responsibility. Lawyers, accountants and actuaries are covered by our practice rules, but there are many professionals in the EP community who are responsible for maintaining plans, and ensuring their compliance, but who are not covered by IRS practice rules.

That situation presents the question of whether this gap in the practice regime represents a barrier to compliance and to our ability to enforce the rules. I think that it does.

Our Tax Exempt and Government Entities Advisory Committee, a group of outside experts whom we depend on for stakeholder input, has a project underway that speaks directly to this issue. Should we expand the list of those who may practice before the Service to others, for example to third party administrators? If the answer is yes, then how should the IRS regulate their practice? The advisory committee report is due to us in the spring. If you have thoughts on this subject, the committee has asked me to let you know that comments can be sent to the following address: [tege.act@irs.gov](mailto:tege.act@irs.gov). Or you can send written comments to me, and I will get them to the committee.

Let me wind up. I've spoken about the need for change and the steps we are taking to accomplish that change. In closing, though, I want to come back to what I started with. And that is that there is much that should not change within our Employee Plans function.

TE/GE and EP are unique within the IRS. Our focus is not on revenue generation but on ensuring that our customers have what they need to comply.

We are going to retain that which makes us unique: That we protect the public interest; that we are innovative; and that we continue to value stakeholder education and partnership.

Nothing I have said today should detract from our continued commitment to our longstanding ways of helping you and your clients comply:

- A vigorous determination letter program,
- A robust outreach program, and
- The ability to come to us to correct problems.



How we administer these programs may shift to allow us to bring about needed changes in direction and emphasis, but the programs and all they have provided in the past will remain.

Thank you.