

Remarks of Steven T. Miller
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Internal Revenue Service
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Thank you all for being here this morning. Let me first express my appreciation for the work of the organization that has brought us here, Independent Sector. They are a valued partner.

I want to focus my remarks this morning on three general topics.

- First, I would like to touch on where we are today and how we got there: my assessment of the current environment.
- Second, given the environment, I want to cover the activities of the Service.
- Finally, I want to focus on where I see the Service headed. As part of this, and as time permits, I would like to talk about our role in governance and transparency.

Before I start, though, let me note a couple of things that people tend to forget about the IRS. First, we believe – I believe – that a vigorous, vibrant tax-exempt sector is vital to America, and indeed to the world. The public relies on your good works each and every day. The second thing to remember about the IRS: Our job is not to overburden you with eccentric, nit-picking, nonsensical rules. Rather, it is to design a compliance and service structure that will enable you to do your jobs as efficiently and effectively as you can.

That said, we do need to ensure the public and other stakeholders have a sufficient line of sight into your activities so they know what their contributions and our foregone taxes are paying for.

The bottom line is this: We at the Service understand that virtually all tax-exempt organizations do want, and do strive, to be tax compliant. So with that preface, let's begin today's discussion. Let's talk about the current environment and what has led us to this place.

If what I say about the tax-exempt sector is true – that it is generally compliant – why is the current environment unsettled? Why all the ruckus? There is a ruckus because troubling themes have emerged in the tax-exempt sector. Some of these themes have been present for a long while. Others are newer. But whether long-standing or new, until fairly recently, these themes were generally unopposed by meaningful regulatory oversight.

What are these troubling themes? Let me identify several of them:

- First, nominally charitable pursuits have been twisted to capitalize on gaps in the marketplace and then used to make a profit rather than to serve a public purpose. While there are others, I can use as examples here most credit counseling organizations, and many down-payment assistance organizations.
- Second, there exist some bad actors out there: for example, schemes in which a donor claims a deduction but maintains control over the contributed assets, often using them for personal benefit. Here we have the more abusive type 3 supporting organizations and donor advised funds. We also have what appears to be a disturbing trend, the acceptance by charities of unusual non-cash assets that are of questionable utility to the charity.
- Third, in some organizations, we see a sense of entitlement by donors and those in charge, arising from a lack of accountability. You have read the papers and know the stories here. This illustrates the problem of organizational insiders who are not accountable to their board of directors, to the public or to the IRS.
- The last example – although there are others – concerns the blurring of lines between the for-profits and non-profits. This shows up across whole sectors – health care is one example, but not the only one. It also appears where non-profit organizations undertake commercial activities that mimic those carried on by the tax-paying for-profit organizations. Here we have restaurants and gift shops, gyms, etc. Now, obviously, some of these are more problematic than others. But as these themes continue to emerge – as the press publishes articles and the Congress holds hearings – some really troubling things have appeared.

That in, a nutshell, is the environment in which you find yourselves. It is an increasingly skeptical environment – an environment that is not as willing as before to extend the benefit of the doubt. Moreover, it is an environment in which some are questioning whether the public benefits that tax-exempt organizations are providing are commensurate with the organizations' resources and the tax subsidies they receive. In addition, increased transparency has led to some absolutely legitimate questions about certain practices and what they cost the public.

Let's go now to my second topic: What is the Service up to, given this environment?

The first thing to be said is that we did indeed take notice. We see the problems and understand the environment and, in response, have significantly enhanced our compliance efforts. At the same time, we have started to act on the principle that effective tax-exempt organizations benefit from transparency, and from engaged boards.

Our renewed emphasis on compliance is illustrated by the increasing number of examinations that we conduct. We have further enhanced our work by establishing new offices and new ways of doing business. An example is the Exempt Organizations

Compliance Unit (EOCU). Through the EOCU, we look at more issues, touch more organizations, and establish a more comprehensive compliance presence.

We are using all these tools to pursue problems and to look at areas where we have questions or concerns: credit counseling, down-payment assistance, assessing the community benefit test for hospitals, executive compensation, improper campaign intervention, to name just a few. And this important work continues. We are proceeding with work on charitable organizations that issue tax-favored bonds, and this year a key initiative will be the rollout of a large-scale project involving colleges and universities.

That is my discussion of our renewed emphasis on compliance. But what of our emphasis on transparency, good governance and accountability?

I was pleased to see that the panel on the non-profit sector has just released its take on governance and ethical practice. It is a great effort. We support and applaud the panel's efforts. We too have been at work in this area.

Key to our effort is our redesign of the Form 990. I don't think anyone is surprised that we decided to revise the form. We needed to start over.

We began by asking what the form should accomplish. Promoting tax compliance is always a core concern. But there are others. One of these is enhancing transparency. We wanted a form that provides the public and the Service with a realistic picture of the organization. A final concern was to accomplish the first two goals while minimizing the burden on the filing organization.

At the same time, we recognize that there may be an increase in the effort required by organizations with complicated compensation arrangements, related entity structures, and activities that raise compliance concerns.

Taking all those concerns into account, we came up with the redesigned Form 990, released for comment in June. The new Form 990 consists, as you know, of a 10 page core form, and a series of 15 schedules. The new form features a summary page that presents the organization's identifying information and a snapshot of the organization's key information. One portion of the form requires governance information, including the composition of the board, and information about other governance, financial statement, and public disclosure practices. The schedules focus on distinct areas of interest to the public and the IRS.

We received a great number of comments which have taught us a number of lessons. One gratifying point that has emerged is that the sector clearly supports the need for a new 990. A second point is that people accept the idea that the IRS has a role to play in the area of governance. No one suggests we walk away. A third point – very interesting to us – was that when we presented some questions that had always been on the old 990 in a different way, a lot of people reacted as if we had created brand new requests. The lesson: some people were not perfect in completing the 990.

The fourth point concerns flaws in the way the 990 requests and presents financial information. Data we ask for on the 990 cannot easily be compared to financial data in standard financial reports that organizations prepare and use in the ordinary course of business. This is a cause of confusion. We need to work on this.

Fifth, we very much want to design the 990 in a way that will enable an ordinary reader to make a meaningful apples-to-apples comparison of two different organizations. This is turning out to be more difficult to accomplish than we ever imagined.

Besides learning lessons from the comments, we are using them to make some decisions:

- The so-called efficiency ratios will drop off the summary page;
- We will move the program service explanations up to the front;
- We will substantially re-format some of the more burdensome schedules;
- And we are considering what targeted transition relief we should provide.

By way of targeted transition, we are considering several options. For example, should we make certain of the schedules optional for the first year or two? The best example here is the bond schedule. Similarly, should we allow a broader band of organizations to file the Form 990EZ for a period before requiring them to file the new Form 990? Based on what we have learned, we continue to believe implementation for the 2008 tax year (the 2009 filing seasons) is achievable.

I believe that, going forward, we must continue to press for transparency and good governance practices. So the question becomes, what role should the IRS play?

I think the answer is that we need to continue to promote transparency and good governance. At a minimum we must educate. The concept of the IRS educating organizations on standards of good governance should be familiar. We have been doing it for a long time. Our Determination agents are trained to ask governance-related questions as they review applications. Further, our Examination agents currently assess exempt organizations' internal controls at the start of an exam to help determine how deep they have to go.

Let's move to the third topic: Where I see the IRS headed. As we look toward the future, should we abandon, modify or expand some of our current practices?

The short answer is that I think we are doing well. We are generally focused on the right things. Historically, our program has rested on three legs: Customer Education and Outreach; Determinations, and Examinations. All are vital and we are making strides with respect to each.

Do we need to go beyond education? A question I would put before you this morning is whether it would benefit the public and the tax-exempt sector to require organizations to

adopt and follow recognized principles of good governance? And a related question: Who should police this area – you or the Service?

As I raise these questions, it is important to note that we are not trying to oversee all non-profit governance matters. We view our role as having boundaries consistent with objectives that relate to tax compliance and transparency. Business judgment and many internal governance issues properly belong to the states and to tax-exempt organizations themselves. So, while we have a role to play, part of our challenge and responsibility is to determine what that role is and limit ourselves to it.

Let me wrap up. Today the tax-exempt community is under a microscope. Problems that a few years ago might have gone unnoticed now get picked up and widely broadcast. The result is that while compliance within the tax-exempt community may actually be good, it doesn't always look so good to the public, or to Congress. A slow but steady drumbeat of bad newspaper articles can hurt a reputation. Unfortunately, the IRS, by itself, cannot rescue the community from this predicament. We cannot restore your reputation.

Let me quote from a document I have just read:

“We know that government action cannot – and should not – replace strong, effective governance of independent organizations and constant vigilance by our own community.”

I could not agree more – that quotation is from last week's transmittal letter of the panel's Principles of Good Governance and its wonderful 33 principles.

I believe the Independent Sector and the panel have provided excellent leadership and the 33 principles give you the tools to protect your reputation.

To the extent that you do not use those tools, the answer to what is next for the Service could change, or Congress may step in. Failure to self-regulate now may result in a lost opportunity for you to do so later.

Thanks