October 21, 1997
The Honorable Bill Archer
Chairman
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C.

Ways and Means Committee Hearings --
Restructuring of the Internal Revenue Service --
Employee Benefits and Exempt Organizations

Dear Mr. Chairman:

On September 17, 1997, I appeared before the Committee on Ways and Means on behalf of the Section of Taxation of the American Bar Association. As requested by the Committee, our testimony was limited to certain issues raised in the Report of the National Commission on Restructuring the Internal Revenue Service ("Report") and H.R. 2292. In our testimony, we spoke to issues relating to Executive Branch governance and Congressional oversight of the Internal Revenue Service ("Service"), as well as certain recommendations regarding efforts to simplify future tax legislation. We indicated that, at the appropriate time, we would appreciate the opportunity to present our views on other issues addressed in the Commission's Report.

Since we understand the Committee may meet later this month to draft legislation relating to the restructuring of the Service, we think it is appropriate to supplement our earlier testimony at this time. Our supplement relates to the employee plans and exempt organizations (EP/EO) functions within the Service.

In its Report, the Commission made recommendations with respect to the EP/EO functions. H.R. 2292 would amend the Internal Revenue Code to strengthen the provisions in existing law which contain a special authorization for funding those functions. The Commission makes this recommendation notwithstanding its general predisposition to simplify tax administration by limiting the "non-core" functions assigned to the Service. The Report concludes that, insofar as employee plans and exempt organizations are concerned, the Service has demonstrated its ability to carry out its regulatory activities effectively. The Report, therefore, recommends that the Congress should support the allocation of sufficient resources to ensure the Service's continued ability to achieve this objective. Indeed, the Report states that "the Employee Plans and Exempt Organizations operation is recognized as one of the most innovative and efficient functions within the IRS."

With respect to funding the EP/EO functions, H.R. 2292 would retain existing law, which provides for an authorization of appropriations equal to the Section 4940 excise tax on investment income (assuming a 2 percent excise tax rate), plus the greater of the same amount or $30 million. H.R. 2292 would strengthen these provisions by specifying that this authorized appropriation may be used solely to carry out the Service's EP/EO functions. The bill also provides an additional funding source: all user fees collected by the Employee Plans and Exempt Organizations Division would be dedicated to carry out EP/EO functions.

On September 16, 1997, the Staff of the Joint Committee on Taxation ("Joint Committee") issued JCX-44-97, "Description and Analysis of Proposals Relating to the Recommendations of the National
Commission on Restructuring the Internal Revenue Service on Executive Branch Governance and Congressional Oversight. The Joint Committee document contains a description and discussion of the provisions in H.R. 2292 and the Report relating to the structure and funding of the Employee Plans and Exempt Organizations Division, and reviews in detail both the size of the employee plans and exempt organizations sectors and the decline in Service personnel dedicated to enforcement of the tax laws applicable to those sectors. The Joint Committee document provides a thorough and well-documented frame of reference for Congressional consideration of the EP/EO funding issue.

The Section of Taxation has two large and active committees -- Exempt Organizations and Employee Benefits -- the membership of which have extensive experience with the Service's administration of the Internal Revenue Code provisions pertaining to employee plans and exempt organizations. Our committees strongly support the conclusions of the Report regarding the Service's performance with respect to the regulation of EP/EO and the need to provide adequate funding to accomplish this purpose. Indeed, our Committees have concerns that, without such funding, the Service's ability to regulate and enforce the tax laws applicable to the employee plans and exempt organizations sectors will be in serious jeopardy.

With respect to the manner of achieving adequate funding of the Service's EP/EO activities, our committees have some concern about the formulaic budget authorization mechanism contained in existing law and endorsed by H.R. 2292. While H.R. 2292 evidences an intent to provide a mechanism for adequate funding of these functions within the Service, that mechanism is not self-executing and would require specific appropriations, as does existing law. To date, there have been no such appropriations, and there is little reason to expect that the provision in H.R. 2292 would, standing alone, be any more effective in achieving the intended objective. In addition to the historical ineffectiveness of the provision, the Joint Committee document referred to above points out that the dedication of a particular revenue source to fund the EP/EO functions could lead to fluctuations in funding which would make organizational planning difficult.

In our view, as a practical matter, the provision of adequate funding for the Service's EP/EO activities requires collaboration and cooperation among the Service, the Treasury Department, and the tax writing and appropriations committees of the Congress. We believe this probably can best be achieved within the traditional budget authorization and appropriations process.

In our September 17 testimony, we recommended that Congress establish the position of Undersecretary of the Treasury charged with the responsibility, among other things, of coordinating the activities of the Treasury Department which involve tax administration and tax policy. One of the responsibilities of the Undersecretary, as we see it, would be to evaluate the resource requirements in the various functions of the Service and to influence the final budget allocations on behalf of the Administration. Based upon the information and data contained in the Report and the Joint Committee document, the Undersecretary would be in the best position to achieve the necessary resource allocations to the Employee Plans and Exempt Organizations Division. This is exactly the kind of issue which prompted our recommendation for establishing a high-level position within the Treasury Department responsible for overall coordination of tax administrative and policy matters. The Undersecretary also would be in a position to provide information, and be accountable, to the tax writing and appropriations committees of the Congress on this subject. These committees, we hope, then would be able to ensure the availability of adequate funding for the EP/EO functions within the context of the Service's overall budget.

We appreciate your willingness to allow us to submit this supplemental statement, and we request that it be made a part of the September 17 hearing record. We would be pleased to meet with you, other members of the Ways and Means Committee or your staff to further discuss this matter.
Sincerely,

Phillip L. Mann
Chair
Section of Taxation

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