



IRS TAX EXEMPT BONDS



FY2012

TAX EXEMPT BONDS

WORK PLAN

Planning Guidelines

Executive Summary

Tax Exempt Bonds

FY2012 Implementing Guidelines

The work plan provides program guidance and direction to all TEB employees.

TEB Operating Priorities support the IRS's 2009-2013 Strategic Plan. The IRS Strategic Plan outlines two goals and a strategic foundation that guide the future direction of the agency.

- Improve service to make voluntary compliance easier;
- Enforce the law to ensure everyone meets their obligation to pay taxes; and
- Invest for high performance.

In support of these goals, TEB has committed to the following Operating Priorities:

- Maintain increased enforcement actions against high-risk cases and abusive tax schemes;
- Detect and deter abusive tax shelters through education and examination strategies;
- Address the use of derivatives and other financial products to divert rebatable arbitrage;
- Expand TEB's compliance presence in the tax-exempt bond and tax credit bond market through increased use of compliance check initiatives and correspondence examinations;
- Refine TEB's examination case processing procedures and practices;
- Encourage greater participation in TEB's voluntary compliance programs; and
- Enhance information gathering through refining existing returns and the correlating instructions.

Section I provides the specific program priorities and goals/objectives for the Customer Education & Outreach function.

Section II provides the specific program priorities and goals/objectives for TEB Compliance Services.

Operating Priorities

Field Operations (FO) will continue its focus on identifying abusive tax-exempt bond transactions and their promoters. It is expected that, similar to FY2011, TEB will direct

substantial resources toward examining arbitrage motivated and/or abusive transactions with a continuing emphasis on addressing abuses involving swaps and other derivative contracts. FO will continue to utilize the IRC section 6700 tax promoter penalty to target the promoters of abusive transactions and the lack of diligence by market professionals. TEB will make referrals of professionals to the Office of Professional Responsibility (OPR), Criminal Investigation (CI) and other agencies when appropriate. TEB will also dedicate substantial resources to providing training and other technical assistance to other IRS offices and government agencies.

TEB will continue discrete arbitrage compliance programs and projects coordinated by the TEB Arbitrage Team. This work will be completed in FO and will include focused examinations of bond issues determined by the Arbitrage Team to have a greater likelihood of arbitrage noncompliance, such as pooled financing bonds and advance refunding bonds, as well as requests for recovery of overpayment of rebate. Additionally, CPM will continue to conduct examinations of Form 8038-Ts to determine rebate compliance, penalty determination examinations for late filed rebate payments.

TEB's Direct Pay Bonds Compliance Team will continue coordinating TEB's enforcement, voluntary compliance, and educational programs relating to direct pay bonds as well as the IRS's forms, processing, and pre-payment compliance review systems to ensure the effective administration of this high profile market segment. The Team will continue to analyze compliance risks and evaluate referral information as well as coordinate issues identified in examination and voluntary compliance cases. The Team will also identify and develop potential compliance initiatives and educational programs for direct pay bonds.

Compliance and Program Management (CPM) will continue the use of risk assessment projects as part of its redesigned classification program. TEB will update its IRM to reflect the new classification program this fiscal year.

CPM will continue with its primary responsibility of negotiating and executing voluntary closing agreements pursuant to the Tax Exempt Bonds Voluntary Closing Agreement Program (TEB VCAP). CPM will continue implementation of additional streamlined voluntary compliance programs. These programs will set forth standardized terms for resolving common violations related to tax-exempt bonds and tax credit bonds.

A high priority of TEB is to communicate effectively with the diverse membership of the municipal bond community. TEB will continue to develop partnerships with state and local government officials, regulatory agencies, industry and national professional associations, as well as their state and local affiliates and members within each of our customer segments.

TEB will continue to train its workforce to ensure that employees have the skills necessary to execute TEB's operating priorities. TEB intends to continue to expand its specialty training programs to allow employees to focus on specialized areas of tax-exempt financing. In FY 2012 TEB will complete the publication of its revised formal

training program which will include training related to the new types of tax credit bonds including Build America Bonds. TEB will continue its use of the employee survey to identify opportunities for improvements in employee satisfaction.

TEB's Financial Restructuring Compliance Team will continue to identify potential tax compliance risks related to tax-exempt bonds and tax credit bonds resulting from actions taken by issuers or other parties in response to their financial hardship or general market liquidity constraints. The Team will also continue to develop potential enhancements to TEB's compliance and educational programs in order to balance protecting the Federal government's interests with the needs of such those government entities facing financial hardship or general market liquidity constraints.

FY 2011 Accomplishments

TEB leadership continues to be grateful for the support and business results of its highly skilled workforce. In FY2011, TEB delivered its planned business results. TEB also continued to be at the forefront of directly addressing serious abuses in the municipal financing industry. TEB continues to provide invaluable assistance to other IRS functions and external agencies involved in ongoing investigations.

In FY2011, TEB continued to meet or exceed its performance goals related to examination and compliance check closures and closures of voluntary closing agreement requests. Examination cycle time and hours per examination case also remained below the performance measure. TEB also strengthened its relationship with various members of its customer segment in FY2011 by holding its first webinar entitled, "Getting It Right: Form Filing and Compliance Issues for Direct Pay Bonds" and hosting a teleconference with external stakeholders discussing the recent revisions to Closing Agreement and Voluntary Compliance Agreement Program IRMs.

As reflected in TEB's employee participation in Survey 2011, TEB's participation in the overall employee engagement process remains high. TEB leadership is appreciative of the satisfaction TEB employees take in their work.

SECTION I

Customer Education and Outreach

Overview of Customer Education and Outreach

TEB will focus on providing the participants in the municipal bond industry with quality service. TEB will assist participants in understanding their tax responsibilities by conducting tailored educational programs. TEB will also monitor noncompliance trends for the purpose of designing proactive education and outreach products for use by TEB customers.

Each TEB unit will plan to fully support opportunities for education and outreach to customers in the various bond industry segments with a focus on assistance to professionals who provide tax advice or monitor post-issuance use or arbitrage compliance. TEB personnel will participate in workshops, seminars, and meetings sponsored by bond industry groups and associations to effectively leverage limited TEB resources. TEB also plans to host a webinar during the fiscal year that will focus on various tax filing and compliance issues relating to arbitrage requirements or qualified 501(c)(3) bonds. These outreach efforts will focus on educating customers with respect to the federal tax requirements that must be met throughout the life cycle of municipal bonds in order to maintain the tax-exempt status of interest income of the bonds.

Compliance and Program Management

The TEB CPM staff is responsible for:

- Improving and expanding TEB's voluntary compliance programs;
- Enhancing education and outreach programs with external stakeholders;
- Developing and issuing, as needed, specialized educational materials and publications;
- Expanding the TEB Internet and Intranet sites and otherwise leveraging technology to meet customer needs;
- Identifying and assisting in the implementation of special projects;
- Developing and evaluating the results of market segment surveys and questionnaires, compliance check initiatives, examination project initiatives and discrete arbitrage initiatives to determine compliance levels and to identify emerging trends and issues;
- Issuing determination letters in response to applications for allocations of volume cap;
- Classifying returns related to general examination program activity;
- Creating or revising Form 8038 series returns and other tax-exempt bond and tax credit bond related returns;
- Coordinating with Customer Account Services (CAS) return filings, taxpayer inquiries, and revisions to Form 8038 series returns;
- Providing assistance, when requested, to the Director's staff and FO on administrative and technical matters;
- Coordinating legislative proposals with internal and external offices and agencies with a primary goal of increasing overall community compliance levels; and
- Working with the Office of Chief Counsel and the Department of Treasury on published guidance projects, with a primary goal of improving tax administration.

Field Operations

TEB FO will continue to assist CPM in the development and delivery of targeted outreach programs by participating in seminars/meetings and partnering with outside stakeholders. FO will continue its State Government Relations Project, which establishes channels of communication between TEB and the States regarding matters of mutual interest in promoting voluntary compliance. TEB has developed a comprehensive communications strategy with respect to all State governments and has made permanent assignments to agents to bolster the building of personal relationships. FO will also assist CPM in identifying areas of abuse and noncompliance warranting the development of market segment initiatives and arbitrage initiatives.

Focus Group

FO and CPM employees will continue to participate in the TEB Focus Group. The TEB Focus Group facilitates quality examinations and ensures that examinations are conducted in a timely and efficient manner and result in consistent treatment of issues raised nationwide. The Focus Group includes agent and manager representatives from the FO groups, CPM representatives, and representatives from Counsel.

SECTION II

Compliance Services

Overview of Compliance Services

TEB will focus on identifying and correcting noncompliance, ensuring consistency and fairness in application of law, and resolving issues at the lowest possible level using appropriate resolution mechanisms.

TEB Field Operations is responsible for:

- Conducting examinations using standardized procedures and audit guidelines;
- Processing requests for refund of arbitrage payments;
- Measuring the compliance levels of market segments by conducting project initiatives and identifying emerging trends;
- Applying IRC section 6700 promoter penalties, where appropriate;
- Conducting pre-payment and post-payment compliance activity with respect to the direct pay bonds payment process;
- Coordinating with other business operating divisions to apply tax to bondholders and conduit borrowers, when appropriate;
- Identifying best practices and recommending changes in procedures; and

- Coordinating with, and referring appropriate cases to, other IRS functions, including OPR and CI.

TEB Compliance and Program Management staff is responsible for:

- Issuing compliance check questionnaires with respect to Qualified School Construction Bonds;
- Coordinating referral information with the TEB Referral Committee;
- Working VCAP submissions;
- Working willful neglect determinations on late-filed returns;
- Classifying returns and closing examination cases on AIMS;
- Conducting mandatory review (technical advice requests, etc.);
- Maintaining and updating the third party contact database;
- Assisting field personnel in the identification and development of complex and emerging technical issues;
- Administering TEB's quality review of closed examination cases; and
- Operating the TEB Bondholder Unit for the purpose of identifying bondholders of tax-exempt bonds and tax credit bonds, when appropriate.

For FY 2012, the principal activity of the program will be to continue to participate in ongoing investigations of arbitrage motivated and/or abusive transactions. It is anticipated that examination FTE will continue to be applied to arbitrage motivated and/or abusive transactions. Training activities will continue to be conducted, as necessary, to ensure consistent and uniform issue development and resolution.

In FY 2012, TEB will continue to focus on abusive and arbitrage-driven transactions involving long investment periods or large investment amounts, including requests for recovery of overpayment of rebate, examinations of Form 8038-Ts to determine rebate compliance, penalty determination examinations for late filed rebate payments, as well as examinations of bond issues determined by the Arbitrage Team to have a greater likelihood of arbitrage noncompliance. This work will be completed in both the CPM and FO programs. The issuance of bonds for the primary purpose of diverting rebatable arbitrage remains TEB's highest compliance risk and enforcement focus. Managers will assign these transactions priority status and ensure all appropriate penalties and sanctions are applied.

In FY 2012, TEB will initiate examination projects focused on specific types of bonds. Such work will include student loan bonds, pooled bond financings, independent multi-functional special district (IMFSDI) financings, and advance refunding bonds. This work will be completed in the FO program.

TEB will continue the use of market segment risk assessment examinations as part of its new classification program. During FY 2012, TEB expects to complete projects relating to working capital financings, small governmental lease financings, and various types of governmental and charitable financings involving management contracts, research agreements, naming rights, and other public-private partnership arrangements. This work will be completed in the CPM program

TEB's Direct Pay Bonds Compliance Team will continue coordinating TEB's enforcement, voluntary compliance, and educational programs as well as the IRS's forms, processing, and pre-payment compliance review systems to ensure the effective administration of this high profile market segment. The Team will continue to analyze compliance risks and evaluate referral information as well as coordinate issues identified in examination and voluntary compliance cases. The Team will also continue to identify and develop potential compliance initiatives and educational programs for direct pay bonds.

TEB's State Government Relationships Team will continue its efforts to establish ongoing lines of communication between TEB and State officials responsible for the issuance and compliance monitoring of state and local bonds. FO will continue these efforts in order to discuss compliance trends and educational needs.

TEB's Financial Restructuring Compliance Team will continue to identify potential tax compliance risks related to tax-exempt bonds and tax credit bonds resulting from actions taken by issuers or other parties in response to their financial hardship or general market liquidity constraints. The Team will also continue to develop potential enhancements to TEB's compliance and educational programs in order to balance protecting the Federal government's interests with the needs of such distressed government entities.

CPM will perform compliance reviews on late filed bond returns forwarded by the Ogden Service Center. CPM will make determinations regarding whether the failure to file timely is due to willful neglect by following the procedures set forth in Rev. Proc. 2002-48, 2002-37 I.R.B. 531, or Rev. Proc. 2005-40, 2005-28 I.R.B. 83. CPM will, when necessary, contact the issuer for an explanation. CPM will classify for examination cases involving non-responsive issuers.

FY2012 Audit Procedures

The audit techniques for conducting examination activities are field, office, and correspondence. Generally, the managers in FO are responsible for determining which audit technique is appropriate for a case based on the potential issues involved, the scope of the examination, and the most effective way to gather required information.

Managers will determine when the collection of bondholder names becomes a priority during an ongoing examination of a bond return. Managers should consult with the manager responsible for operation of the Bondholder Unit, when appropriate. As soon as a proposed determination of taxability is made, the Bondholder Unit will initiate efforts to identify bondholder names and open bondholder examinations. The Bondholder Unit will also be responsible for acquiring statute extensions, issuing deficiency notices, and making discrepancy adjustments while bondholder cases remain under TEB jurisdiction.

FO managers will coordinate with other business operating divisions all potential adjustments to the borrower's tax return, including adjustments under IRC sections 150(b) and 168(g). FO managers should coordinate early in the examination process in order to preserve potential adjustments for expiring tax years.

Examination Categories

For FY2012, TEB resources will be allocated to the following areas:

- Abusive Arbitrage-motivated Transactions
- Pooled Financing Bonds
- Tax and Revenue Anticipation Notes and other working capital financings
- Tax Promoter Penalties (Section 6700)
- Tax Increment Bonds
- Advance Refunding Bonds
- IMFSDI Financings
- Student Loan Bonds
- 501(c)(3) Bonds
- Governmental Bonds
- Other specialty bonds and tax-credit bonds

These examination areas and other examination categories will be separately identified for technical time and inventory tracking reporting purposes through particular Activity Codes for the type of return and specific Project Codes.

Research Program

The TEB market segmentation is a systematic method to define the universe by conducting examinations of a sample of returns on a nationwide or geographic basis and reflecting results/conclusions from the samples in a profile of the applicable market segment. The objective of TEB market segmentation is to continually build information and knowledge through conducting research on the compliance levels of various types of bond issuances. These research projects assist in the targeting of direct compliance activities to areas of actual or suspected noncompliance.

Annually, the Director, TEB will conduct meetings with all of TEB's managers to develop the subsequent fiscal year market segment project initiatives. The Director will also consider the findings from completed examination and compliance check initiatives as well as voluntary compliance initiatives when identifying the market segments that will be reviewed.

Voluntary Resolution Programs

CPM will work documents submitted as part of the Tax Exempt Bond Voluntary Closing Agreement Program (VCAP) (Notice 2008-31) and other voluntary resolution programs

(e.g., Rev. Proc. 97-15, 1997-1 C.B. 635, and IRM 7.2.3). CPM will work with other responsible offices to develop and expand its voluntary compliance programs and procedures.

Compliance Support Function

The CPM staff provides administrative and research support to FO. This support includes AIMS activities, referral analysis and research, and third-party contact data. The CPM staff also will research available database information to provide field agents supporting documentation and information regarding examinations.

ATTACHMENT I

Workload Selection

TEB will continue to refine the workload selection criteria utilized in prior years. Workload selection will be monitored to ensure that key areas identified through examination and compliance check project initiatives, market segment risk assessment and focus groups are addressed and that the actions being assigned represent the optimal approach to the identified issue. The Workload Selection Process described in this section will be a primary tool TEB uses to identify and prioritize workload in concert with its Annual Work Plan.

An effective Workload Selection Process should accomplish several key tasks. It should:

1. Generate work that addresses issues pertaining to non-compliance on a national level.
2. Be data driven, to the fullest extent possible.
3. Be consistent with TEB's balanced measures.
4. Ensure fair treatment of each taxpayer.
5. Ensure adequate controls are in place in accordance with Servicewide work assignment and approval requirements.
6. Be flexible enough to accommodate Work Plan adjustments, e.g., new legislation and court decisions.
7. Provide the TEB field group managers the flexibility they need to balance local concerns with national priorities.

The Workload Selection Process for FY2012 incorporates information from several sources. All of these sources are necessary to ensure the Workload Selection Process is data driven, consistent with our balanced measures and reflective of our customers' needs. This approach will also ensure that TEB efficiently uses its enforcement resources. TEB products that have a direct impact on this Workload Selection Process include:

1. TEB Compliance/Project Initiatives
2. FY2012 Annual Workplan
3. TEB Balanced Measures
4. Findings from focus groups, other ad-hoc meetings and other customer communicated items that identify customer needs.

Compliance/ Project Initiatives

There are two primary methodologies used to initiate project initiative. They are:

1. Market Segment Compliance Measurement – This methodology includes the systemic selection of each market segment over a period of time to measure

noncompliance of that segment or type of bond. For example, small issue manufacturing bonds and single family housing bonds would constitute separate market segments.

2. Emerging Issues – This methodology measures noncompliance by identifying cases based on the existence of a potential emerging or identified issues within the TEB return population.

The FY2012 Annual Work Plan will impact the Workload Selection Process in that it will typically quantify the amount of resources that will be expended on any given market segment. For example, the number of examinations is dependent upon the resources devoted to these various segments. Resource allocation decisions are made by the Director of TEB and will be consistent with the overall goals of the business plan.

The Balanced Measures are consistent with the overall outline of the IRS organizational measures:

- Employee Satisfaction
- Customer Satisfaction
- Business – Results – Quality & Quantity

These three measures represent one of the levers of change for the successful modernization of the Internal Revenue Service. The actions undertaken in the Workload Selection Process will be consistent with these measures.

The purpose of this Workload Selection Process is to outline the methodology used to identify and prioritize those returns or customers that warrant an examination. It will also identify and prioritize those customers who may be less compliant on a given national issue. The FY2012 Annual Work Plan quantifies resource expenditures dedicated to the various initiatives.

This Workload Selection Process does not affect the ability of a group manager to request approval of compliance matters based on their knowledge of an issue that they believe requires immediate action. However, such requests must be directed to the Manager, CPM and approved by the Manager, CPM and must be justified as to their importance as well as any negative impact on other work.

Methodology

The Workload Selection Process for FY2012 will generate examination work for the six TEB field groups. Much of the casework will be derived from recommendations and potential compliance issues identified in Compliance/Project Initiatives, Compliance Questionnaires, the Market Segment Risk Assessment (see Attachment VIII) and Referrals (including I.R.C. section 6700 leads).

The following areas will be emphasized in the FY2012 Workload Selection Plan:

Claims

All claims for refund filed through the Ogden Service Center are controlled on AIMS and forwarded for processing. Some claims require taxpayer contact and others can be closed based on the information provided with the claim. The Arbitrage Team Leader will submit closed claim case files to the CPM AIMS unit for closing. If the claim is allowed, CPM will forward the Manual Refund form for the case to Ogden for issuance of the refund. CPM will close the case on AIMS.

Claim cases remain priority cases.

Referrals/Information Items

TEB referrals come from many sources: the media, informants, other Operating Divisions, Appeals, etc. All TEB referrals and information items that are submitted for examination consideration, except certain IRC 6700 cases resulting from a lead, are routed to CPM for review and approval. CPM personnel research information items on IDRS and RICS to provide relevant return filing information for the subject of the referral and information item.

To ensure unbiased selection of cases for examination, referrals must be approved by both the Manager, CPM and the Manager, FO or their representatives (the Referral Committee) before assignment to a field group.

Three forms are prepared for each Referral: a TEB Referral, Information Reports and Information Items Record and a Tax-Exempt Bond Information Item Tracking Sheet. These forms become part of the examination case file. In addition, a copy of each form is retained in a Referral Log in CPM. The group manager completes the form during the case closing and a copy of the form is pulled during the closing of the case in CPM and associated with the copy in the Referral Log. The examination results are notated in the Log. The Logs are housed in CPM and provide a historical reference record of referred bond issues.

Promoter Penalty Cases

IRC section 6700 of the Code imposes a penalty on any “person” who commits certain actions described in the Code section. TEB identifies IRC section 6700 leads by:

- a. Working cooperatively and coordinating, to the extent permitted under IRC section 6103, with counterparts at the Securities and Exchange Commission (SEC); National Association of Securities Dealers (NASD); Municipal Securities Rulemaking board (MSRB); and, Offices of State auditors, etc.
- b. Reviewing, as part of its normal examination activities, the use, expenditure and investment of proceeds of the bond issue and what the various participants knew, or should have known, with regard to such use, expenditure or investment of bond proceeds. In those instances where abusive transactions are found, TEB will use existing databases or John Doe summonses to determine whether there are similar transactions done by the same parties.
- c. Monitoring industry materials and publications to identify new financial techniques and schemes.

TEB operates an IRC section 6700 Committee to evaluate, at the discretion of the Director, recommendations from FO that FO be granted approval to open a promoter penalty case. The Committee is comprised of representatives from Chief Counsel and TEB.

Group managers will assign IRC section 6700 cases priority status and ensure that penalties are applied when appropriate. TEB will use administrative tools, formal guidance and other issue resolution strategies to aggressively combat abusive transactions.