



January 2020

INDIVIDUAL RETIREMENT ACCOUNTS

IRS Could Better Inform Taxpayers about and Detect Noncompliance Related to Unconventional Assets

GAO Highlights

Highlights of [GAO-20-210](#), a report to the Ranking Member, Committee on Finance, U.S. Senate

Why GAO Did This Study

Unconventional IRA investments—such as real estate, certain precious metals, private equity, and virtual currency—can introduce risks to account owners who assume greater responsibility for navigating the complex rules that govern tax-favored retirement savings. IRS enforces tax rules relating to IRAs and can assess additional taxes.

GAO was asked to examine the challenges associated with enforcing rules governing IRAs invested in unconventional assets. This report examines (1) the extent to which IRS offers guidance to help taxpayers understand the rules governing unconventional IRA assets; and (2) the challenges IRS faces in enforcing those rules. GAO identified and analyzed IRS information to help taxpayers understand four compliance areas. GAO reviewed IRS analysis of nonmarket IRA assets reported by IRA custodians, and IRS audit procedures and training materials; and interviewed relevant IRS officials to identify enforcement challenges.

What GAO Recommends

GAO is recommending that IRS (1) assess options for updating its IRA publications to provide more information for taxpayers with unconventional assets, (2) evaluate the feasibility of requiring disclosure for high-risk IRA asset types associated with abusive tax schemes, and (3) develop auditor resources (such as training materials or job aids) that explain how IRAs with unconventional assets can generate unrelated business income tax. IRS generally agreed with GAO's recommendations.

View [GAO-20-210](#). For more information, contact James R. McTigue, Jr. at (202) 512-9110 or mctiguej@gao.gov, or Charles A. Jeszeck at (202) 512-7215 or jeszeck@gao.gov.

January 2020

INDIVIDUAL RETIREMENT ACCOUNTS

IRS Could Better Inform Taxpayers about and Detect Noncompliance Related to Unconventional Assets

What GAO Found

The Internal Revenue Service's (IRS) Publications 590-A and 590-B serve as a general handbook for millions of taxpayers with individual retirement accounts (IRA). However, the two-part publication provides limited information for IRA owners with unconventional assets surrounding complex tax rules in four compliance areas: (1) barred investments, (2) prohibited transactions, (3) unrelated business income, and (4) fair market value. GAO found other limited information about these topics on IRS's website. With only about 2 percent of IRAs invested in unconventional assets, adding more pages to Publications 590-A and 590-B may not be practical. By assessing options for informing IRA owners investing in unconventional assets, such as directing them to web pages with specialized information and technical regulations, IRS could better help them comply.

Noncompliance involving unconventional IRA assets is difficult to detect and time consuming for IRS to pursue. Whereas IRS relies on automated enforcement for IRAs invested in conventional assets held by custodians and trustees, enforcement for IRAs invested in unconventional assets or under IRA owner control requires labor-intensive audits of individual taxpayers. Using newly compiled information, IRS identified about 2 million IRAs that held certain types of hard-to-value assets as of 2016; however, about 20 percent of the forms were missing fair market value amounts for these assets (see fig.).

Numbers of IRAs Reporting Certain Types of Unconventional Assets and Reporting Their Value (Tax Year 2016)

Data element from IRS Form 5498	Number of forms reporting (in millions)
Certain types of unconventional nonmarket assets	2.0
Fair market value of specified assets	1.6

Source: GAO analysis of IRS data. | GAO-20-210

IRS officials said this type of reporting alone may be inadequate for audit selection and identifying potentially abusive IRAs. When IRS lacks sufficient data to detect abusive transactions, IRS can require taxpayers to self-report certain transactions that have been used by other taxpayers to avoid taxes. Additional taxpayer or custodian disclosure of potentially abusive IRA transactions coupled with IRS analysis of reported details may help IRS to select IRA owner tax returns to audit.

Fragmented responsibility among IRS divisions creates challenges for examiners who need to share expertise and collaborate on IRA enforcement. The division responsible for tax-exempt entities trains its examiners on how to determine if an employee retirement plan has engaged in business activities subject to taxation. However, examiners in the division that audits complex individual tax returns, including those involving IRAs, do not receive such training. Training for those examiners could help improve collaboration on IRA enforcement.

Contents

Letter		1
	Background	3
	Primary IRS Publication Could Better Help IRA Owners with Unconventional Assets Understand Complex Rules	8
	Insufficient Data and Fragmented Expertise across IRS Organizational Units Complicate Enforcement of IRA Rules Involving Unconventional Assets	12
	Conclusions	21
	Recommendations for Executive Action	22
	Agency Comments	23
Appendix I	Status of GAO Recommendations	25
Appendix II	IRS Information for IRA Owners Investing in Unconventional Assets	28
Appendix III	Comments from the Internal Revenue Service	32
Appendix IV	GAO Contacts and Staff Acknowledgments	35
Tables		
	Table 1: Overview of IRS Organizational Units Responsible for IRA Enforcement	7
	Table 2: Summary of the Information Provided in Selected IRS Resources on Four Compliance Topics for IRA Owners with Unconventional Assets	10
	Table 3: Numbers of IRAs Reporting Certain Types of Unconventional Assets and Reporting Their Value (Tax Year 2016)	15
	Table 4: Status of Our Recommendations Related to Individual Retirement Account Rules Enforcement	25

Abbreviations

DOL	Department of Labor
ERISA	Employee Retirement Income Security Act of 1974
FMV	fair market value
FAQ	frequently asked questions
IRA	individual retirement account
IRS	Internal Revenue Service
LB&I	Large Business and International
SB/SE	Small Business/Self-Employed
TE/GE	Tax-Exempt and Government Entities
Treasury	Department of the Treasury
W&I	Wage and Investment

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.



January 27, 2020

The Honorable Ron Wyden
Ranking Member
Committee on Finance
United States Senate

Dear Senator Wyden:

Individual retirement accounts (IRA) are a key vehicle for individuals to save for retirement or roll over savings from employer-provided retirement plans, such as a 401(k) plan. For tax year 2016 (the most recent statistical data available), an estimated 59 million taxpayers had IRAs with a total estimated fair market value (FMV) of \$8 trillion.¹ IRA owners are able to invest their IRA savings in a wide variety of asset types. Many IRA owners choose to invest in publicly traded assets, such as stocks, bonds, and mutual funds, through a bank or qualified firm that acts as a trustee or custodian of those investments. Some IRA owners seek out alternative investment opportunities in less conventional or nonpublicly traded assets such as real estate, certain precious metals, private equity, and virtual currency. We previously found that IRA owners who have accumulated unusually large IRA balances likely have invested in unconventional assets like nonpublicly traded shares of stock and partnership interests.²

As we also previously found, unconventional IRA investments can introduce new risks to account owners who assume greater responsibility for navigating the complex rules that govern tax-favored retirement investments.³ Difficulty in valuing nonpublicly traded investments can heighten the risk of noncompliance. We have also found that noncompliance associated with nonpublicly traded IRA assets has been difficult for Internal Revenue Service (IRS) to detect and time consuming

¹IRS, Statistics of Income Division, *Individual Retirement Arrangements Study*, April 2019. A taxpayer may own multiple IRAs.

²GAO, *Individual Retirement Accounts: IRS Could Bolster Enforcement on Multi-Million Dollar Accounts, but More Direction from Congress is Needed*, [GAO-15-16](#) (Washington, D.C.: Oct. 20, 2014).

³GAO, *Retirement Security: Improved Guidance Could Help Account Owners Understand the Risks of Investing in Unconventional Assets*, [GAO-17-102](#) (Washington, D.C.: Dec. 8, 2016).

to pursue.⁴ Overall, IRS audits of individual tax returns have declined in recent years.⁵

You asked us to examine the challenges associated with enforcing rules governing IRAs invested in unconventional assets. This report examines: (1) the extent to which IRS offers guidance to help taxpayers understand the rules governing unconventional IRA assets and (2) the challenges IRS faces in enforcing IRA rules for unconventional assets. In June 2019, we issued a separate report on IRS and Department of Labor (DOL) collaboration on shared oversight of prohibited transaction rules for IRAs and the DOL process for granting exemptions for prohibited IRA transactions.⁶ These reports are part of a larger body of work on retirement security—a key issue we have identified facing the nation.⁷

To determine the extent to which IRS offers published guidance to help taxpayers understand rules governing unconventional IRA assets, we identified and analyzed publicly available IRS information on four compliance areas where complex rules are likely to apply: (1) barred investments, (2) prohibited transactions, (3) unrelated business income, and (4) fair market value (FMV). Information sources reviewed include federal laws and regulations and guidance published in the Internal Revenue Bulletin such as revenue rulings and revenue procedures. We also reviewed IRS publications, forms and instructions, as well as information on IRS.gov, including frequently asked questions (FAQ).

To identify challenges IRS faces in enforcing rules for IRAs invested in unconventional assets, we built on the analyses of IRA rules developed for the first objective by reviewing relevant sections of the Internal Revenue Manual, IRS audit procedures, and internal training materials covering IRA rules to determine how IRS detects when violations of the

⁴See [GAO-15-16](#).

⁵We generally use the term audit, instead of review or examination, for the purposes of this report. For data about recent declines in the number of IRS audits, see GAO, *Tax-Law Enforcement: IRS Could Better Leverage Existing Data to Identify Abusive Schemes Involving Tax-Exempt Entities*, [GAO-19-491](#) (Washington, D.C.: Sept. 5, 2019).

⁶GAO, *Individual Retirement Accounts: Formalizing Labor's and IRS's Collaborative Efforts Could Strengthen Oversight of Prohibited Transactions*, [GAO-19-495](#) (Washington, D.C.: June 7, 2019).

⁷See https://www.gao.gov/key_issues/retirement_security.

rules occur, resolves noncompliance, and develops strategies to promote IRA owner compliance.

We interviewed IRS officials from the Small Business/Self Employed (SB/SE) division, and the Tax-Exempt and Government Entities (TE/GE) division's Exempt Organizations and Employee Plans groups to identify enforcement challenges and how these units communicate and coordinate in handling IRA issues. We also discussed with SB/SE and TE/GE officials the status of implementing our prior recommendations related to IRAs with unconventional assets.⁸ We reviewed documentation and analysis of nonpublicly traded IRA assets from an IRS team studying IRA noncompliance. We reviewed the IRS data tabulations and interviewed staff responsible for compiling the data. Based on our review and interviews with IRS officials, we determined the data reported on IRAs with unconventional assets were sufficiently reliable for purposes of this report.

We conducted this performance audit from December 2016 to January 2020 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Created as part of the Employee Retirement Income Security Act of 1974, as amended (ERISA), traditional IRAs provide tax advantages to help individuals—including small business owners, independent contractors, and other workers not covered by employer-sponsored retirement plans—save for retirement.⁹ Employees who have employer-sponsored retirement plans, such as a 401(k), can also roll over these assets into an IRA when they retire or change jobs.

Since the enactment of ERISA, different types of IRAs with different features for individuals and small businesses have been created. The two IRA types with federal income tax benefits for individuals are traditional

⁸Appendix I summarizes recommendations from our prior reports related to IRAs with unconventional assets and actions that have been taken or are planned to address them.

⁹See Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered section of 26 and 29 U.S.C.).

IRAs (which allow eligible individuals to make tax-deductible contributions and accumulate tax-deferred investment earnings) and Roth IRAs (which allow eligible individuals to make after-tax contributions and accumulate investment earnings tax free).¹⁰

IRA owners are able to invest their IRA savings in a wide variety of asset types. IRA owners generally make tax-favored contributions to their accounts to purchase assets from investment options offered through banks or other IRS-qualified firms acting as custodians of the IRA assets.¹¹ Most IRA custodians limit holdings in IRA accounts to firm-approved stocks, bonds, mutual funds, and CDs.

Some custodians offer so-called “self-directed IRAs” that allow investments in a broader set of unconventional assets—such as real estate, certain precious metals, private equity, and virtual currency—than is permitted by most IRA custodians. As we previously reported, custodial agreements for these accounts often require IRA account owners to be responsible for directing their investments, and to oversee the selection, management, monitoring, and retention of all investments in the account.¹² The account owners bear the consequences of any mistakes made in managing their accounts, such as being noncompliant with IRA rules.

Through our prior work, we identified the following four areas where complex rules are likely to apply to IRA owners investing in unconventional assets:

- **Barred investments.** Investments in life insurance contracts and collectibles, such as artwork and antiques, are prohibited. Although

¹⁰Two other types of IRAs are intended to encourage savings sponsored through small employers. A Simplified Employee Pension (SEP) IRA was created in 1978, and was designed with fewer requirements than traditional employer pension plans to encourage small employers to offer pension plans to their workers. A Savings Incentive Match Plan for Employees (SIMPLE) IRA was created in 1996 to help employers with 100 or fewer employees more easily provide a retirement savings plan to their employees through employer and employee contributions.

¹¹All IRA accounts are held for investors by custodians or trustees. An IRA custodian or trustee must be a bank, a federally insured credit union, a savings and loan association, or an entity approved by IRS to act as trustee or custodian. Throughout this report, we generally use the term “custodians” to refer to both trustees and custodians.

¹²See [GAO-17-102](#) for more on different types of unconventional IRA investments and how these IRAs are managed.

precious metals are generally prohibited collectibles, certain types of coins and bullion are permitted provided that they meet specific purity and custody requirements.

- **Prohibited transactions.** IRA owners are not permitted to engage in prohibited transactions that personally benefit the owner or other disqualified persons in a way other than as a vehicle to save for retirement. Examples of such prohibited transactions include IRA owners selling their own property to an IRA, or taking a salary from an IRA-funded business. IRA owners who believe that an otherwise prohibited transaction should be permitted, may apply to the Department of Labor (DOL) to request an exemption for a specific transaction.¹³
- **Unrelated business income.** Earnings and profits made in tax-deferred savings vehicles like IRAs generally are reinvested in the account without generating current federal tax liability, but investments in certain unconventional assets can generate ongoing tax liability for IRA owners.¹⁴ Any IRA that earns \$1,000 or more of gross income from an unrelated business must file Form 990-T *Exempt Organization Business Income Tax Return* with IRS and pay related taxes.
- **Fair market value (FMV).** When IRA owners invest in less conventional and nonpublicly traded assets, custodians may find it challenging to properly report the FMV of those assets. Starting with tax year 2015, IRS began requiring IRA custodians to report selected information on unconventional assets in their clients' accounts. For some hard-to-value unconventional assets, IRA owners may need to supply custodians with independent appraisals or other evidence to substantiate an asset's current FMV.

¹³IRS and DOL each have responsibilities for overseeing prohibited transactions relating to IRAs. DOL has primary responsibility for interpretive guidance and exclusive authority to grant exemptions from the prohibited transaction rules for retirement plans and IRAs. Whereas IRS and DOL share oversight responsibilities for employer-sponsored retirement plans such as 401(k) plans, IRS is responsible for enforcing tax laws relating to IRAs and, among other things, assessing additional taxes for early distributions for IRA owners who engage in prohibited transactions. See [GAO-19-495](#).

¹⁴Unrelated business taxable income is gross income generated from an ongoing trade or business (less allowable deductions) that is not related to the exempt or tax-deferred entity, such as an IRA. Examples include using an IRA to invest in an active business or using debt to finance a portion of an asset's purchase. See [GAO-17-102](#) for more about how certain IRA investments can trigger unrelated business income tax liability.

Failure to abide by the rules governing IRAs with unconventional assets can have significant consequences for IRA owners. For example, if an IRA owner engages in a prohibited transaction that has not been exempted by DOL, the IRA will lose its tax-favored status, and the account is treated as distributing all of its assets to the owner at the FMV on the first day of the year in which the prohibited transaction occurred.¹⁵ Noncompliance with IRA rules—if not detected—can also lead to millions of dollars in uncollected tax revenue for the government.

Individuals who invest in certain unconventional assets using Roth IRAs can avoid taxation on investment gains. For example, founders of companies (or key initial investors) who use IRAs to invest in nonpublicly traded shares of their newly formed companies can realize many millions of dollars in tax-favored gains on their investment if the company is successful.¹⁶

IRS is responsible for enforcing IRA tax laws, including rules that apply when IRA owners invest in unconventional assets. Within IRS, four business operating divisions have responsibilities for enforcing compliance with IRA rules. Table 1 provides an overview of each division's IRA enforcement activities.

¹⁵See 26 U.S.C. § 408(e)(2)(B). The IRA owner may also be subject to additional income taxes because of an early distribution from an IRA. See 26 U.S.C. § 72(t). The prohibited transaction may also be subject to excise taxes. If a disqualified person other than the IRA owner engages in a prohibited transaction, that person may be liable for a 15 percent excise tax on the amount of the prohibited transaction and a 100 percent additional tax if the transaction is not corrected in a timely manner. 26 U.S.C. § 4975(a). If the IRA ceases to be an IRA as a result of the prohibited transaction, the IRA owner or beneficiary is not subject to the excise tax. See 26 U.S.C. § 4975(c)(3).

¹⁶See [GAO-15-16](#). We previously found that with no total limit on IRA accumulations, the government forgoes millions in tax revenue.

Table 1: Overview of IRS Organizational Units Responsible for IRA Enforcement

IRS unit	Responsibility for IRA enforcement
Wage and Investment (W&I)	Operates automated enforcement programs that check taxpayer reporting of IRA transactions against information provided by third-parties such as IRA custodians.
Small Business/Self-Employed (SB/SE)	Enforces traditional and Roth IRA rules through field audits of more complex individual tax returns.
Tax-Exempt and Government Entities (TE/GE)	Has jurisdiction over tax-exempt employee retirement plans (including employer-sponsored IRAs). Approves non-bank IRA trustees and custodians and periodically investigates them.
Large Business and International (LB&I)	Can penalize financial institutions that are IRA trustees and custodians for inaccurate reporting. Provides in-house expertise from IRS's Engineering Department (part of LB&I) on hard-to-value assets including assets held in IRAs.

Source: GAO analysis of IRS information. | GAO-20-210

Third-party reporting by IRA custodians provides information that taxpayers can use in preparing their tax returns and that IRS can use to identify noncompliant taxpayers and help close the tax gap.¹⁷ In 2015, IRS began requiring custodians to report new information to help identify IRAs with hard-to-value unconventional assets. IRS Form 5498 *IRA Contribution Information* has a new box 15a for custodians to report the portion of the IRA FMV attributable to nonmarket assets as well as a box 15b with codes describing the type of nonmarket assets.¹⁸ Custodians are to report similar information on IRS Form 1099-R identifying distributions of IRA assets that do not have a readily available FMV.

¹⁷The tax gap is the difference between tax amounts that taxpayers should pay and what they annually pay voluntarily and on time. See GAO, *Tax Gap: IRS Needs Specific Goals and Strategies for Improving Compliance*, GAO-18-39 (Washington, D.C.: Oct. 31, 2017).

¹⁸Box 15b on the form provides eight codes for identifying the types of unconventional assets: (A) stock or other ownership interest in a corporation that is not readily tradable on an established securities market; (B) short- or long-term debt obligation that is not traded on an established securities market; (C) ownership interest in a limited liability company or similar entity (unless the interest is traded on an established securities market); (D) real estate; (E) ownership interest in a partnership, trust, or similar entity (unless the interest is traded on an established securities market); (F) option contract or similar product that is not offered for trade on an established option exchange; (G) other asset that does not have a readily available fair market value; and (H) more than two types of assets (listed in A through G) are held in this IRA. Precious metals is not one of the specified categories of hard-to-value IRA assets that custodians can select on the Form 5498.

Primary IRS Publication Could Better Help IRA Owners with Unconventional Assets Understand Complex Rules

The first article in the Taxpayer Bill of Rights is the right to be informed which means that taxpayers have the right to know what they need to do to comply with tax laws.¹⁹ IRS’s Publication 1, *Your Rights as a Taxpayer*, further states that taxpayers are entitled to clear explanations of the laws and IRS procedures in all forms, instructions, publications, notices, and correspondence.²⁰

To help taxpayers and their advisors better understand tax rules, such as those governing IRAs with unconventional assets, IRS produces several types of resources. Taxpayers (or their advisors and paid tax preparers) with complicated returns or transactions may require detailed and technical resources, such as guidance published in a weekly IRS publication called the Internal Revenue Bulletin (IRB).²¹ Tax regulations—issued by the Department of the Treasury (Treasury)—are published in the IRB together with technical IRS guidance such as revenue rulings and revenue procedures. IRS has stated that only guidance published in the IRB contains IRS’s authoritative interpretation of the law.²²

IRS also produces resources that are less technical and intended to be more easily understood by most taxpayers. IRS issues hundreds of publications on a variety of tax topics, and many are updated annually. IRS also produces a variety of information on its website (IRS.gov) such as online tools, instructions, and FAQs.

IRS’s Publication 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*, and Publication 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*, serve as a general IRA handbook for

¹⁹In discharging the duties of the Commissioner of IRS, the Commissioner is to ensure that IRS employees are familiar with and act in accord with taxpayer rights as afforded by the Internal Revenue Code, including the right to be informed. 26 U.S.C. § 7803(a)(3)(A).

²⁰IRS, *Your Rights as a Taxpayer, Publication 1* (September 2017). This publication further explains 10 rights for taxpayers and the processes for examination, appeal, collection, and refunds.

²¹See 26 C.F.R. § 601.601(d)(2)(ii)(a). The Internal Revenue Bulletin (IRB) is the “authoritative instrument” for publishing official IRS rulings and procedures, and tax regulations; it is available free online at: <https://www.irs.gov/irb>. Tax regulations are also published in the *Federal Register*.

²²For more information about IRS’s different types of guidance and levels of legal authority, see GAO, *Regulatory Guidance Processes: Treasury and OMB Need to Reevaluate Long-standing Exemptions of Tax Regulations and Guidance*, GAO-16-720, (Washington, D.C.: Sept. 6, 2016).

IRA owners and a logical starting point for all IRA owners with tax questions, including those with unconventional assets.²³ At more than 120 pages combined, Publications 590-A and 590-B comprise one of IRS's longest publications on retirement related topics. Publications 590-A and 590-B provide some limited information on the four compliance topics that we identified through prior work as likely to affect IRA owners with unconventional assets. However, the two-part publication lacks additional information that IRA owners with unconventional assets need to comply.

Publications 590-A and 590-B recommend that taxpayers research IRS's website (IRS.gov) for additional information. We found some additional information on IRS's website about three of the four compliance topics. This information was typically in the form of FAQs in a section of IRS's website about retirement plans (<https://www.irs.gov/retirement-plans>).

Table 2 summarizes: what information for IRA owners with unconventional assets can be found in Publications 590-A and 590-B; what other IRS sources provide relevant information; and what information was not readily available on the IRS website for the four compliance areas likely to affect IRA owners with unconventional assets. Appendix II describes in more detail the information available and the information lacking in Publications 590-A and 590-B and other IRS sources.

²³Beginning for tax year 2014, IRS split Publication 590 into two parts. Publication 590-A covers contributions to traditional and Roth IRAs as well as the rules for rollover and conversion contributions. Publication 590-B covers distributions from traditional and Roth IRAs as well as the rules for required minimum distributions and IRA beneficiaries. At the time of our review, the latest Publications 590-A and 590-B were those for tax year 2018.

Table 2: Summary of the Information Provided in Selected IRS Resources on Four Compliance Topics for IRA Owners with Unconventional Assets

Topic	IRS information for taxpayers
Barred investments	<p>Publications 590-A and 590-B explain what types of collectibles are not permitted, and the consequences of investing in them, and that certain types of coins and bullion are permitted. Publications 590-A and 590-B do not explain the storage requirements for bullion nor do the publications mention that investments in life insurance contracts are not permitted.</p> <p>Two FAQs web pages contain additional information about bullion custody requirements, and the prohibition on investments in life insurance contracts.^a</p>
Prohibited transactions	<p>Publications 590-A and 590-B define prohibited transactions and provide examples; explain the consequences of engaging in a prohibited transaction; and caution that investing in nonpublicly traded assets or assets that an IRA owner controls directly increases the risk of engaging in a prohibited transaction. Publications 590-A and 590-B do not provide information about applying to the Department of Labor (DOL) for an exemption to the prohibited transaction rules.</p> <p>A web page titled, "Retirement Plan Investments FAQs," states that plan sponsors can apply to DOL for an exemption.^b Neither of the Publications 590 nor the IRS web page provide direct links for IRA owners to DOL information such as a publication that explains the DOL exemption process.</p>
Unrelated business income	<p>Publications 590-A and 590-B explain how an IRA can be subject to tax on unrelated business income and explain IRA trustee requirements to file a Form 990-T. Publications 590-A and 590-B direct taxpayers to Publication 598, <i>Tax on Unrelated Business Income of Exempt Organizations</i>, for more information.</p> <p>Publication 598 describes tax-exempt organization activities by that would be considered an unrelated business. Publication 598 does not have examples specific to IRA investments.</p>
Fair market value (FMV)	<p>Publications 590-A and 590-B instruct taxpayers to enter the fair market value (FMV) of the IRA from custodian forms when using the publication's worksheets. Publications 590-A and 590-B and instructions for custodian forms do not provide information about how to accurately determine the FMV of hard-to-value unconventional assets.</p> <p>A web page titled "Valuation of Plan Assets at Fair Market Value" provides some additional information on FMV methods, but it is directed at employer-provided retirement benefits like traditional pensions and 401(k) plans.^c</p>

Source: GAO analysis of IRS information. | GAO-20-210

^aIRS, "IRAs FAQs – Investments," <https://www.irs.gov/retirement-plans/retirement-plans-faqs-regarding-iras-investments>; and "Retirement Plan Investments FAQs" <https://www.irs.gov/retirement-plans/retirement-plan-investments-faqs>.

^bIRS, "Retirement Plan Investments FAQs," <https://www.irs.gov/retirement-plans/retirement-plan-investments-faqs>.

^cIRS, "Valuation of Plan Assets at Fair Market Value," <https://www.irs.gov/retirement-plans/valuation-of-plan-assets-at-fair-market-value>.

Given the complexity of the four compliance topics we identified as well as the relatively few numbers of taxpayers affected and the already large publication size, it may not be feasible to provide complete information on these topics within Publications 590-A and 590-B. IRS publications (like 590-A and 590-B) are intended to explain the law in plain language for taxpayers and their advisors. They generally summarize and translate into layperson's terms more complex and technical information from authoritative sources like the Internal Revenue Code and more

authoritative guidance like tax regulations, revenue procedures, and revenue rulings.

IRS analysis indicates that perhaps only about 2 percent of IRAs have invested in hard-to-value unconventional assets.²⁴ However, even small numbers of taxpayers with particular circumstances have the right to know what they need to do to comply with tax laws. IRA owners with unconventional assets who turn to Publications 590-A and 590-B are unlikely to fully understand how certain IRA investment decisions can increase their risks for noncompliance. Misunderstanding the rules governing IRAs could result in increased tax liability for taxpayers making unintentional errors and jeopardize their retirement savings.

Given the serious consequences that could result for a taxpayer found to be noncompliant, IRS's current publications are not clearly providing information for IRA owners with unconventional assets. Adding information to Publications 590-A and 590-B would be one solution that IRS could explore, but we recognize that it may not be practical for IRS to add substantially more information to Publications 590-A and 590-B for a relatively small percentage of IRA owners. Alternatives to adding more pages to Publications 590-A and 590-B could include directing readers with questions about rules affecting unconventional IRA assets to other IRS resources, such as IRS web pages or tax regulations that contain more technical and specialized information. As shown in table 2 above, we found some additional information on IRS web pages that would be helpful to IRA owners with unconventional assets. Adding language in Publication 590-A or 590-B directing taxpayers to specific web page URL addresses for additional information could help taxpayers more easily locate this information.²⁵ For more technical or specialized information, IRS could direct readers of Publications 590-A and 590-B to the relevant

²⁴According to IRS analysis of 124 million Forms 5498 filed in 2017 (for tax year 2016), about 2 million forms indicated that the IRA contained one or multiple types of hard-to-value unconventional assets.

²⁵The last chapter of some IRS publications—"How To Get Tax Help"—directs readers to specific sections of IRS's web page, rather than directing readers to just IRS.gov in general. IRS Publication 17 *Your Federal Income Tax* also contains many hyperlinks to more detailed parts of IRS.gov as well as to individual Revenue Procedures.

sections of the Internal Revenue Code and related tax regulations.²⁶ This additional information could help IRA owners better understand and navigate the potential compliance challenges associated with certain types of unconventional assets.

Insufficient Data and
Fragmented
Expertise across IRS
Organizational Units
Complicate
Enforcement of IRA
Rules Involving
Unconventional
Assets

IRS Cross-Divisional Team
Identified Risks of IRA
Noncompliance Based on
Different Asset Types

In October 2017, the Deputy Commissioner for Service and Enforcement commissioned a cross-divisional team comprised of representatives from all four IRS operating divisions to identify, assess, and mitigate risks of IRA noncompliance. In its February 2018 interim presentation, the IRS cross-divisional team categorized potential noncompliance risks over an IRA life cycle into two mitigation strategies, which are summarized below.²⁷

1. Noncompliance risks for most contribution and distribution IRA rules can be mitigated systemically through automated enforcement. For example, IRS can detect excess IRA contribution deductions and unreported IRA distributions by matching information from taxpayer

²⁶For prohibited transactions, DOL has primary responsibility for interpretive guidance and information that could be useful for developing educational outreach to IRA owners. In June 2019 (see [GAO-19-495](#)), we recommended DOL and IRS establish a formal means to collaborate on oversight of prohibited IRA transaction exemptions. In October 2019, IRS officials told us providing additional information about prohibited transactions for IRA owners could be a collaboration opportunity.

²⁷Stages of an IRA life cycle include, but are not limited to, setting up the account, investing the funds, and distributing funds to the IRA owner or beneficiaries. Noncompliance with IRA rules can be unintentional or intentional.

returns with information reported by custodians. For the large population of IRA owners investing in conventional assets held by custodians, IRS relies on automated enforcement.

2. Noncompliance risks associated with the small population of IRAs with hard-to-value unconventional assets or under direct control of the IRA owner are generally mitigated through case-by-case audits. For example, noncompliance with the complex rules governing prohibited transactions and unrelated business income is generally not reflected on individual tax returns. Some custodians rely on IRA owners to provide asset value information and may not have complete and accurate data to report to IRS.²⁸ Undervaluing IRA assets hampers automated enforcement, for example, to detect excess contributions and taxable distributions.

Noncompliance involving IRAs with unconventional assets is generally detected through labor-intensive audits of individual taxpayers. IRS's SB/SE division uses field audits to pursue complex individual tax return cases, including those that could involve IRAs with unconventional assets.²⁹ In February 2018, an IRS cross-divisional team that studied the risks of IRA noncompliance reported that, from fiscal years 2012 to 2016, IRS audited about 26,000 tax returns with IRA issues.

IRS officials provided us examples of SB/SE job aides and training materials designed to help examiners recognize different types of noncompliance associated with IRAs invested in unconventional assets. For example, the job aides provide instructions on prohibited transactions, barred collectibles, and FMV issues involving IRAs. When interviewing taxpayers, examiners are instructed to ask a series of questions covering subjects such as:

- what kind of advice the taxpayer received from promoters or custodians of self-directed IRAs,
- whether the taxpayer had direct involvement in purchasing unconventional assets through a control feature known as "checkbook access,"

²⁸As we reported in 2015, custodians may not always be able to get accurate asset information about IRAs if the IRA owner has day-to-day investment control, which could lead to unreliable Form 5498 reporting of asset types and FMV. See [GAO-15-16](#).

²⁹See [GAO-15-16](#) for more information about, and an illustration of, the SB/SE field examination process.

-
- whether the taxpayer has a limited liability company (LLC) tied to the IRA, and
 - how the taxpayer determined the FMV of unconventional assets.

IRS officials told us that enforcing rules associated with IRAs investing in unconventional assets can be particularly challenging for investments involving LLCs or special partnership arrangements. An IRA owner may establish an LLC that is owned by the IRA.³⁰ Once the LLC is set up, a business checking account is linked to the IRA funds and the account owner is named the manager of the LLC with control over the checkbook. This allows IRA owners to purchase assets directly from investment sponsors without having to wait for custodians to execute a purchase or sale.

The LLC may be used to invest in businesses that could generate unrelated business income. According to IRS officials, prohibited transactions may also be more likely to occur when custodians allow “checkbook” access to IRAs, in part because the marketing of this IRA structure is appealing to individuals who want less oversight of their IRA transactions and are more likely to intentionally engage in self-dealing transactions.

IRS examination officials told us that the 3-year statute of limitations for assessing taxes owed remains an obstacle in pursuing noncompliance that may span the many years of an IRA investment.³¹ For example, abuses involving prohibited transactions frequently are not reflected on any filed tax return and may be difficult to detect within the general 3-year statute of limitations period. IRS agreed with our October 2014 recommendation for the Commissioner to work in consultation with the Department of the Treasury (Treasury) on a legislative proposal to

³⁰A single-member LLC is generally treated as an entity disregarded from its owner for federal income tax purposes. A multi-member LLC is generally treated as a partnership for federal income tax purposes, unless it elects to be treated as a corporation.

³¹Generally, IRS has 3 years from the date a return is filed (whether the return is filed on time or not) to make an assessment of tax liability. See 26 U.S.C. § 6501(a). The statute of limitations is extended in certain situations. For example, if a taxpayer submits a false or fraudulent tax return or otherwise engages in a willful attempt to evade a tax, the tax may be assessed at any time after the return is filed. See 26 U.S.C. § 6501(c)(1), (2). Also, IRS and the taxpayer may agree to extend the statute of limitations for assessment. See 26 U.S.C. § 6501(c)(4). Other extensions are authorized when the taxpayer fails to file a tax return, omits a certain amount of gross income from the return, or fails to report a listed transaction. See 26 U.S.C. § 6501(c)(3), (10) & (e)(1).

expand the statute of limitations on IRA noncompliance. IRS said Treasury is aware of IRS' support for changing the limitation period for IRA noncompliance. Treasury reviews and presents the administration's tax proposals and has not released a legislative proposal as of October 2019.

Data Collection Has Improved, but Opportunities Exist to Further Strengthen Identification of Potentially Abusive IRAs

With electronically compiled data for tax year 2016 filed in 2017, IRS was positioned for the first time to quantify the number of IRAs with specified types of hard-to-value assets. IRS officials said that even with the new custodian reporting, the broad IRA asset type data alone may be inadequate for improving audit selection criteria and identifying potentially abusive IRAs in a timely manner. In February 2018, using the newly available data, an IRS cross-divisional team identified that about 2 million IRAs included one or more types of hard-to-value assets for tax year 2016. However, custodians reported an FMV dollar amount for hard-to-value assets for only 1.6 million of those IRAs, as shown in table 3. The combined FMV was approximately \$137 billion.³²

Table 3: Numbers of IRAs Reporting Certain Types of Unconventional Assets and Reporting Their Value (Tax Year 2016)

Data element from IRS Form 5498	Number of forms reporting (in millions)
Certain types of unconventional nonmarket assets	2.0
Fair market value (FMV) of specified assets	1.6

Source: GAO analysis of IRS data. | GAO-20-210

Note: IRS requires IRA custodians to identify via Form 5498, *IRA Contribution Information*, IRAs with certain types of nonmarket assets and report the fair market value (FMV) associated with of those nonmarket assets. The latest IRS tabulations of Form 5498 data on unconventional nonmarket assets available for review was for tax year 2016.

As shown in table 3, about 400,000 (about 20 percent) of the Form 5498s reporting that the IRA held investments in one or more of the specified unconventional categories were missing the 2016 FMV dollar amount for those assets. The cross-divisional team identified that undervaluation risk affects custodian reporting. IRS officials said that the team did not review

³²For IRAs with a reported FMV greater than \$5 million in tax year 2016 (about 9,000 IRAs), IRS identified that about 25 percent of the total reported value was held in hard-to-value unconventional assets. In [GAO-15-16](#), we found that taxpayers with IRA values greater than \$5 million had likely accumulated these larger IRA balances by investing in unconventional assets unavailable to most investors.

the custodian reporting patterns as part of its initial analysis of the 2016 Form 5498 data. Forthcoming tax regulations on IRAs may help to improve custodian reporting of FMVs on Form 5498.³³ IRS officials told us that the new IRA regulations would address FMV for certain categories of hard-to-value unconventional assets. IRS officials also told us that it would be premature to publish new guidance for IRA owners and custodians on the FMV of unconventional assets until the new regulations are issued.

The tax year 2016 Form 5498 information indicated about 141,000 IRAs invested in LLCs—an asset type which IRS has determined presents greater noncompliance risk.³⁴ Prior to the newly available asset type data, SB/SE conducted an interim Compliance Initiative Project (CIP) using external state government information to identify businesses, including LLCs and partnerships, owned by IRAs as a way to select IRA owners for audit.³⁵ Completed in October 2019, the interim compliance research revealed that audits detecting prohibited transactions can result in substantial tax adjustments.

In September 2018, SB/SE approved a new CIP using the asset type data from Form 5498s for tax year 2017 to select a sample of traditional and Roth IRAs that had an ownership in an LLC or real estate. The latest compliance research field work began in February 2019 and is to be completed in January 2021. IRS officials told us they plan to use this research in combination with the interim research results to improve criteria for selecting tax returns with IRAs at greater risk of noncompliance for audit.

³³In [GAO-17-102](#) we recommended that IRS provide guidance to IRA owners and custodians on how to determine and document fair market value for hard-to-value assets. IRS agreed with the recommendation. If IRS fully implements actions to provide guidance and reporting instructions, we believe that it will ameliorate some of the data anomalies. In its October 2019 update of planned tax regulations, Treasury's Office of Tax Policy and IRS listed the planned IRA regulations as forthcoming. Department of the Treasury, Office of Tax Policy and Internal Revenue Service, *2019-2020 Priority Guidance Plan* (released Oct. 8, 2019).

³⁴On about 141,000 of the Form 5498s, custodians entered Code C for "Ownership interest in a limited liability company or similar entity (unless the interest is traded on an established securities market)." On about another 22,000 of the Form 5498s, custodians entered Code C plus one other code for another type of specified investment category.

³⁵IRS Compliance Initiative Projects are compliance actions or activities involving the collection of data on specific groups or segments of taxpayers and contact with those taxpayers.

To detect abusive transactions, IRS can require taxpayers to self-report certain transactions that have been used by other taxpayers to avoid taxes. Transactions become “reportable” (meaning a taxpayer must report it to IRS) when IRS designates them as a “listed transaction” or “transactions of interest.”³⁶

- **Listed Transaction.** A listed transaction is reportable when it is the same or substantially similar to one of the types of transactions that IRS has determined to be an avoidance transaction.³⁷ In 2004, IRS determined that Roth IRA “stuffing” is an abusive tax avoidance transaction that taxpayers must report to IRS as a listed transaction.³⁸ “Stuffing” involves shifting value through transactions that disguise Roth IRA contributions exceeding annual IRA limits, such as selling receivables at less than FMV to a Roth IRA, or other transactions between a closely-held business in which the Roth IRA invests and another closely-held business of the Roth IRA owner.
- **Transaction of Interest.** A transaction of interest is one that IRS and Treasury believe to have the potential for tax avoidance or evasion, but which lacks enough information for IRS and Treasury to determine whether the transaction should be identified as a tax avoidance transaction. As of December 2019, IRS has not identified or classified any IRA asset types or investment transactions as reportable transactions of interest.

Taxpayers are required to disclose all types of reportable transactions on Form 8886, *Reportable Transaction Disclosure Statement*. Similarly, advisers helping taxpayers conduct reportable transactions are required to file Form 8918, *Material Advisor Disclosure Statement*.³⁹

Results from the ongoing IRS compliance research may yield insights about existing and emerging abusive schemes involving IRAs. This

³⁶See [GAO-19-491](#) for more information on these and other types of reportable transactions.

³⁷IRS provides a detailed list of the 36 recognized listed transactions on its website. See <https://www.irs.gov/businesses/corporations/listed-transactions>.

³⁸Internal Revenue Service, “Abusive Roth IRA Transactions,” *Internal Revenue Bulletin No. 2004-4*, Notice 2004-8 (Jan. 26, 2004).

³⁹Tax exempt entities like IRAs are required to file Form 8886-T, *Disclosure by Tax Exempt Entity Regarding Prohibited Tax Shelter Transaction*, when the entity is party to listed and confidential transactions and knows the identity of any other party in the transaction.

information could be useful for evaluating the feasibility of requiring greater disclosure by IRA owners and their custodians and advisors. For example, IRS could consider requiring reporting of known abusive IRA arrangements and prohibited transactions as listed transactions. Also, IRS could explore disclosure of high-risk IRA asset types susceptible to gross valuation misstatements, such as LLCs, as transactions of interest.⁴⁰ We recently found that IRS's Research, Analysis and Statistics office had developed the capability to analyze the narrative fields of tax forms.⁴¹ Additional disclosure of potentially abusive IRA transactions coupled with greater use of tax form's narrative fields may help IRS to select IRA owner tax returns for more detailed review. The cases identified by such detailed review would help IRS better allocate limited audit resources.

Enforcing IRA Rules for Unconventional Assets Draws on Expertise and Roles of Multiple IRS Organizational Units

Responsibility for addressing IRA noncompliance detected through case-by-case audits is fragmented among multiple IRS organizational units. This fragmentation creates challenges for IRS examiners from different units that may need to share expertise and collaborate on enforcement of complex rules applicable to IRAs that invest in unconventional assets.⁴² In February 2018, the IRS cross-divisional team concluded that no one IRS operating division alone can effectively identify and penalize IRA

⁴⁰The fact that a transaction must be reported does not mean IRS will disallow the tax benefit, but IRS uses the reports to assess compliance.

⁴¹See [GAO-19-491](#). We found that the narrative analytical tool was not being used operationally to review the Form 8886 or any other disclosure report. Our analysis showed that the tool has the potential to help IRS better search disclosure reports for additional information about transactions involving tax-exempt entity involvement in abusive tax schemes. In September 2019, we recommended that IRS should use existing data analytic tools to further mine Form 8886 data for possible audit leads. IRS agreed with the recommendation.

⁴²In our body of work on duplication, overlap, and fragmentation within agencies and across the federal government, we use the term fragmentation when referring to those circumstances in which more than one federal agency (or more than one organization within an agency) is involved in the same broad area of national need and opportunities exist to improve service delivery. Fragmentation may have positive and negative effects. Negative aspects of fragmentation can be addressed through improving coordination and collaboration within and across agencies. See GAO, *Fragmentation, Overlap, and Duplication: An Evaluation and Management Guide*, [GAO-15-49SP](#) (Washington, D.C.: Apr. 14, 2015).

noncompliance regarding unrelated business income and undervaluation of unconventional assets.⁴³

Unrelated business income. SB/SE and TE/GE officials told us that detecting unrelated business income unreported by an IRA can also require the involvement of multiple IRS divisions. IRS responsibility and expertise in detecting noncompliance with the rules for unrelated business income resides in IRS's TE/GE division. TE/GE is responsible for enforcing the unrelated business income taxation rules across tax-exempt organizations. Its Exempt Organizations group audits Form 990-T filed by tax-exempt charities and its examiners are required to check if tax-exempt charities have reported unrelated business income.⁴⁴ Examiners in TE/GE's Employee Plans group have been trained on how to determine if a tax-exempt employee retirement plan has engaged in activities that constitute unrelated trade or business.⁴⁵

SB/SE has primary responsibility for auditing individuals owning IRAs, and its examiners are to verify that all returns within the taxpayer's sphere of influence are filed.⁴⁶ IRS officials told us that when SB/SE examiners discover potential unrelated business income issues when reviewing an individual taxpayer's IRAs, those examiners can seek assistance from TE/GE examiners via an internal Specialist Referral System used to refer cases to other divisions.⁴⁷

⁴³The cross-divisional team also identified prohibited transactions as a crosscutting compliance challenge. See [GAO-19-495](#) for more information about how IRS and the Department of Labor coordinate on shared oversight of prohibited transactions for IRAs.

⁴⁴Internal Revenue Manual 4.75.12.

⁴⁵Internal Revenue Manual 4.71.10 provides guidance for identifying unrelated business income and procedures for examining Form 990-T for TE/GE Employee Plan examiners. According to TE/GE training materials we reviewed, the receipts of an unrelated trade or business may be buried in with other items of an entity's income and, as a result, TE/GE examiners must conduct in-depth reviews of an entity's books and records to discover the unrelated trade or business.

⁴⁶Internal Revenue Manual 4.10.5.2.1. This examination guidance applies to both SB/SE and LB&I.

⁴⁷Internal Revenue Manual 4.10.5.2.3.

Although IRS officials described to us how SB/SE examiners, at their own initiative, can seek out expertise on unrelated business income, the topic is not addressed in SB/SE examiner training materials and job aids on auditing IRAs with unconventional assets. SB/SE officials provided us training slides used to teach examiners how to recognize excess contributions, prohibited transactions, barred collectibles, and valuation issues involving IRAs. While the slides instruct examiners to contact a Senior Program Analyst or Counsel for assistance with complicated issues or cases, there is no information educating SB/SE examiners about unrelated business income or informing examiners that specialized knowledge about this topic resides in the TE/GE division. Without resources, such as training materials or job aids, that provide such information, SB/SE examiners carrying out the ongoing compliance initiative project are not positioned to surface unrelated business income tax issues for referral to TE/GE. Given that IRS plans to use those research results to refine its audit selection criteria, IRS is missing an opportunity to learn more about IRA noncompliance with unrelated business income taxation.

Undervaluation of unconventional assets. In February 2018, the cross-divisional IRA team cited undervaluation of unconventional assets as another compliance risk that involves the expertise and enforcement responses from multiple IRS units.⁴⁸ If SB/SE examiners determine in auditing an IRA owner that the IRA custodian had inaccurately reported IRA asset values, other IRS divisions can take action against the custodian. LB&I can penalize a large financial institution custodian, although the cross-divisional IRA team reported the \$50 penalty for filing an incorrect Form 5498 poses little deterrent effect.⁴⁹ For the approximately 75 non-bank IRA trustees approved by IRS, TE/GE

⁴⁸As we reported in 2015, IRA account owners may try to evade annual contribution limits or reduce required minimum distributions by undervaluing unconventional assets like real estate or private equity. To detect noncompliance SB/SE examiners might need to obtain appraisals from outside experts. See [GAO-15-16](#).

⁴⁹The \$50 penalty for filing incomplete, incorrect, or late information also applies to certain other third-party information returns. 26 U.S.C. § 6693.

can revoke a non-bank's trustee status for violating any fiduciary, accounting, or financial requirements.⁵⁰

The cross-divisional IRA team explored an approach for joint examination to more effectively identify and penalize noncompliance associated with prohibited transactions, unreported unrelated business income, and undervaluation of IRA assets. Based on knowledge from prior examinations, the team identified a small subset of non-bank trustees publicly marketing alternative investments that held IRAs more than \$5 million in reported FMV as of tax year 2016.

As of February 2018, the team reported that it had been premature for the separate divisions to commit examination resources. As of October 2019, IRS officials said they plan to reconvene the cross-divisional IRA team after the ongoing SB/SE compliance initiative project is complete in 2021. IRS officials said the plan is for the team to use the compliance research results to refine audit selection. Also, the team could continue work on establishing a joint examination approach for IRA noncompliance associated with hard-to-value unconventional assets.

Conclusions

IRA owners that invest in unconventional assets—such as real estate, certain precious metals, virtual currency, or private equity—assume greater responsibility for navigating complex rules that govern tax-favored retirement investments. To understand these rules, taxpayers are likely to consult IRS Publications 590-A and 590-B. While this two-part publication provides some information on compliance issues likely to affect IRA owners with unconventional assets, the information in the publication as well as on IRS web pages is limited. By assessing options for making such information clearer, IRS could better inform taxpayers and help them comply. This is particularly important because misunderstanding the rules governing IRAs can result in increased tax liability for these taxpayers and jeopardize their retirement savings.

Noncompliance associated with nonpublicly traded IRA assets has been difficult for IRS to detect and time consuming to pursue. In contrast to

⁵⁰TE/GE issues private letter rulings approving non-bank trustees and periodically investigates them. Non-bank trustees may include major financial institutions, state or non-profit retirement entities, and small investment companies. A list of IRS-approved non-bank trustees is available at: <https://www.irs.gov/retirement-plans/approved-nonbank-trustees-and-custodians>.

automated enforcement for IRAs with conventional investments, noncompliance involving IRAs with unconventional assets is generally detected on a case-by-case basis through labor-intensive audits of individual taxpayers. In recent years, IRS has begun collect information from IRA custodians that IRS can use to quantify the dollar amounts of specified types of hard-to-value assets held by IRAs.

However, the broad IRA asset type data alone may not be sufficient for audit selection and identifying potentially abusive IRAs in a timely manner. When IRS lacks sufficient data to detect abusive transactions, IRS can require taxpayers to self-report certain transactions that have been used by other taxpayers to avoid taxes. Additional disclosure of certain IRA transactions coupled with mining the narrative fields of tax forms could help IRS to efficiently identify potentially abusive IRA activity and better allocate limited audit resources.

Fragmented responsibility among IRS operating divisions creates additional challenges for IRA enforcement. The division responsible for tax-exempt entities trains its examiners on how to determine if an employee retirement plan has unrelated business activities subject to taxation. Yet, examiners in the division that audits complex individual tax returns, including those involving IRAs, do not receive similar training. Training for those examiners on unrelated business income tax issues, and how examiners can refer those cases to other divisions for assistance, could help improve collaboration on IRA enforcement.

Recommendations for Executive Action

We are making the following three recommendations to IRS:

The Commissioner of Internal Revenue should assess options for updating Publications 590-A and 590-B to either include more information or direct taxpayers to other resources for IRA owners with investments in unconventional assets. Such information could include: storage requirements for IRA investments in certain precious metals; valuation methods for hard-to-value IRA assets; the Department of Labor's process for granting exemptions to IRA prohibited transactions rules; and IRA investments with the potential to create unrelated business income tax liabilities. (Recommendation 1)

The Commissioner of Internal Revenue, building on forthcoming compliance research using new IRA asset data, should evaluate the feasibility of requiring disclosure for high-risk IRA asset types associated with abusive schemes as transactions of interest. (Recommendation 2)

The Commissioner of Internal Revenue should develop resources (such as training materials or job aids) for Small Business/Self-Employed examiners conducting IRA owner audits that explain how IRAs with unconventional assets can generate unrelated business income tax liability, and how examiners can refer cases to unrelated business income experts in IRS for assistance. (Recommendation 3)

Agency Comments

We provided a draft of this report to the Treasury and IRS for review and comment.

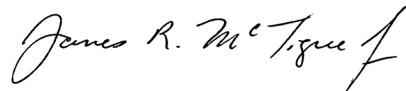
In its comments, reproduced in appendix III, IRS generally agreed with our recommendations. For recommendation 1, IRS said it will review its educational publications and web pages for appropriate updates within the scope of the tax code. For recommendation 2, IRS said that it will determine whether there are abusive schemes associated with certain IRA asset types, and if the data indicate such a correlation, it will evaluate the feasibility of requiring disclosure of such arrangements as transactions of interest. For recommendation 3, IRS said it will review and update resources for examiners conducting IRA owner audits, including guidance on how to address unrelated business income tax (UBIT). It will incorporate guidance for agents on how to refer such cases to UBIT experts when assistance is needed. IRS also said that it will renew its efforts at ensuring collaboration with relevant subject matter experts.

IRS in consultation with Treasury also provided technical comments which we incorporated as appropriate.

As agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the Secretary of the Treasury, the Commissioner of Internal Revenue, the Secretary of Labor, and other interested parties. In addition, the report will be available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact James R. McTigue, Jr. at (202) 512-9110 or Charles A. Jeszeck at (202) 512-7215. You may also reach us by email at jeszeckc@gao.gov or mctiguej@gao.gov. Contact points for our Office of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff making key contributions to this report are listed in appendix IV.

Sincerely yours,



James R. McTigue, Jr.
Director, Tax Issues
Strategic Issues



Charles A. Jeszeck
Director, Education, Workforce,
and Income Security

Appendix I: Status of GAO Recommendations

Table 4: Status of Our Recommendations Related to Individual Retirement Account Rules Enforcement

Recommendation	Implementation status
<p><i>GAO-15-16: Individual Retirement Accounts: IRS Could Bolster Enforcement on Multimillion Dollar Accounts, but More Direction from Congress is Needed (October 2014).</i></p>	
<p>1. Matter for Congressional Consideration: To promote retirement savings without creating permanent tax-favored accounts for a small segment of the population, Congress should consider revisiting the use of individual retirement accounts (IRA) to accumulate large balances and consider ways to improve the equity of the existing tax expenditure on IRAs. Options could include limits on (1) the types of assets permitted in IRAs, (2) the minimum valuation for an asset purchased by an IRA, or (3) the amount of assets that can be accumulated in IRAs and employer-sponsored plans that get preferential tax treatment.</p>	<p>Not implemented. As of October 2019, no legislation enacted. In its October 2014 report, we found that individuals with limited, occupationally related opportunities could engage in sophisticated investment strategies and accumulate considerable tax-preferred wealth in IRAs and subsequently suggested to Congress legislative options. The Senate Finance Committee held a hearing on a range of IRA policy issues in September 2014 for which we provided a statement for the record that covered preliminary data on IRA balances (GAO-14-878T). Without legislation, the intended broad-based tax benefits of IRAs are likely to continue to be skewed toward a select group of individuals.</p>
<p>2. To improve the Internal Revenue Service's (IRS's) ability to detect and pursue noncompliance associated with undervalued assets sheltered in IRAs and prohibited transactions, the Commissioner of Internal Revenue should approve plans to fully compile and digitize the new data from electronic and paper-filed Form 5498s to ensure the efficient use of the information on nonpublicly traded IRA assets.</p>	<p>Implemented. As of March 2017, IRS had begun transcribing paper-filed Form 5498 submissions and compiling information from electronically filed Form 5498 submissions beginning with tax year 2016 data filed in calendar year 2017. For tax year 2015, the first year the new IRA asset reporting was required, IRS did not fund electronic compilation. Once comprehensive digitized information from Form 5498 is available on databases that examiners and examination researchers can access, IRS will be able to conduct enforcement on IRA rules more efficiently and accurately.</p>
<p>3. To improve IRS's ability to detect and pursue noncompliance associated with undervalued assets sheltered in IRAs and prohibited transactions, the Commissioner of Internal Revenue should conduct research using the new Form 5498 data to identify IRAs holding nonpublic asset types, such as profits interests in private equity firms and hedge funds, and use that information for an IRS-wide strategy to target enforcement efforts.</p>	<p>Implemented. In February 2018, IRS completed its first analysis of new information about the amounts and types of nonpublic IRA assets from Form 5498 for tax year 2016 filed in 2017. IRS used the asset type data for tax year 2017 filed in 2018 to streamline the process of identifying those IRAs with hard-to-value nonpublic assets at risk for noncompliance. In September 2018, the IRS Small Business/Self Employed (SB/SE) division approved a new compliance research project examining a sample of IRAs holding certain nonpublic asset types. The compliance research field work began in February 2019 and is to be completed in January 2021. IRS convened a cross-divisional team to identify, assess, and mitigate the risks of IRA noncompliance. As of October 2019, IRS officials said that the team will use the compliance research results to refine audit selection and continue work on establishing a joint examination approach for IRA valuation issues.</p>
<p>4. To improve IRS's ability to detect and pursue noncompliance associated with undervalued assets sheltered in IRAs and prohibited transactions, the Commissioner of Internal Revenue should work in consultation with the Department of the Treasury on a legislative proposal to expand the statute of limitations on IRA noncompliance to help IRS pursue valuation-related misreporting and prohibited transactions that may have originated outside the current statute's 3-year window.</p>	<p>Not implemented. IRS agreed with our October 2014 recommendation on IRAs with large balances and said it had discussed the recommendation with Treasury's Office of Tax Policy and Benefits Tax Counsel. Consequently, IRS said Treasury is aware of IRS's willingness to support legislative efforts in this area. Ultimately, Treasury reviews all tax legislative proposals and presents the administration's tax proposals for congressional consideration. However, Treasury had not released a legislative proposal as of October 2019. Because IRA schemes can occur over many years and the effects of noncompliance may start small but grow, IRS efforts to identify and enforce against possible IRA noncompliance are weakened without expanding the statute in regard to IRAs.</p>

Recommendation	Implementation status
<p>5. To help taxpayers better understand compliance risks associated with certain IRA choices and improve compliance, the Commissioner of Internal Revenue should, building on research data on IRAs holding nonpublic assets, identify options to provide outreach targeting taxpayers with nonpublic IRA assets and their custodians, such as reminder notices that engaging in prohibited transactions can result in loss of the IRA's tax-favored status.</p>	<p>Partially implemented. IRS has taken action to provide general outreach and as of December 2019 has ongoing compliance research that could inform additional opportunities to target outreach to taxpayers with nonmarketable IRA assets at greater risk of noncompliance. In June 2016, IRS published information on IRS.gov outlining the new information to be reported for nonmarketable IRA assets and included a general caution that IRAs with nonmarketable investments or assets under direct taxpayer control may be subject to a heightened risk of committing prohibited transactions. This caution is similar to those that IRS added to its publications about IRA contributions and distributions. It is a step toward helping taxpayers better understand which investments pose greater risks.</p> <p>In February 2018, IRS completed its first analysis of new information about the amounts and types of nonpublic IRA assets from Form 5498 for tax year 2016 that was filed in 2017. In October 2019, IRS also completed an interim compliance research project examining a sample of tax returns to determine whether the beneficiary of the IRA caused his or her IRA to engage in a prohibited transaction. As of December 2019, IRS was conducting a new compliance research project examining IRAs holding certain nonpublic asset types. The compliance research began in February 2019 and is to be completed in January 2021. Unless IRS augments outreach based on reliable data about nonpublicly traded IRA investments, taxpayers at greater risk may not be able to ensure compliance with rules on prohibited transactions.</p>
<p>6. To help taxpayers better understand compliance risks associated with certain IRA choices and improve compliance, the Commissioner of Internal Revenue should add an explicit caution in Publication 590 <i>Individual Retirement Arrangements (IRAs)</i> for taxpayers about the potential risk of committing a prohibited transaction when investing in nonpublicly traded assets or directly controlling IRA assets.</p>	<p>Implemented. In response to our recommendation, in January 2015 IRS added an explicit caution to taxpayers of the potential risk of committing a prohibited transaction when investing in non-publicly traded assets or in directly controlling IRA assets within both the new Publication 590-A, which focuses on IRA contributions, and the 590-B, which focuses on IRA distributions.</p>
<p>GAO-17-102: Retirement Security: Improved Guidance Could Help Account Owners Understand the Risks of Investing in Unconventional Assets (December 2016)</p>	
<p>1. To assist IRA owners in addressing challenges associated with investing their retirement savings in unconventional assets, the Commissioner of Internal Revenue should provide guidance to IRA owners on the potential for IRA transactions involving certain unconventional assets to generate unrelated business taxable income subject to taxation in the current tax year and subsequent years. For example, IRS could consider adding an explicit caution in Publication 590 <i>Individual Retirement Arrangements (IRAs)</i> and include a link in Publication 590 to Publication 598 <i>Tax on Unrelated Business Income of Exempt Organizations</i> to provide examples demonstrating how certain unconventional assets in IRAs can generate unrelated business income tax for account owners.</p>	<p>Implemented. In February 2018, IRS updated both Publication 590-A and Publication 590-B with language informing IRA owners that an IRA can be subject to taxes on unrelated business income if it carries on an unrelated trade or business.</p>

Recommendation	Implementation status
<p>2. To assist IRA owners in addressing challenges associated with investing their retirement savings in unconventional assets, the Commissioner of IRS should provide guidance to IRA owners and custodians on how to determine and document fair market value (FMV) for certain categories of hard-to-value unconventional assets. For example, IRS could consider updating Form 5498 instructions to custodians on how to document FMV for hard-to-value assets (e.g., last-known FMV based on independent appraisal, acquisition price) and provide guidance directed at account owners that provides examples of how to ascertain FMV for different types of unconventional assets.</p>	<p>Not implemented. IRS agreed with our recommendation on IRA valuation guidance and stated that it would discuss this issue with the Department of the Treasury. Treasury plans to issue regulations on IRAs. IRS officials told us that these new regulations would address FMV for certain categories of hard-to-value unconventional assets. In its October 2019 update of planned regulations, Treasury’s Office of Tax Policy and IRS listed the IRA regulations. IRS officials told us that it would be premature to modify instructions to custodians on how to determine and document FMV for hard-to-value assets until the new regulations are issued.</p>
<p>3. To assist IRA owners in addressing challenges associated with investing their retirement savings in unconventional assets, the Commissioner of IRS should clarify the content of the model custodial agreement to distinguish what has been reviewed and approved by IRS and what has not. For example, IRS could consider: (1) restricting custodians from stating that the form has been “preapproved by the IRS” on the form; (2) adding language to specify which articles have been preapproved by the IRS and which have not; and (3) limiting custodians from adding provisions to the model form other than those preapproved by the IRS.</p>	<p>Implemented. In April 2017, IRS revised custodial agreement Forms 5305, <i>Traditional Individual Retirement Trust Account</i> and 5305-A, <i>Traditional Individual Retirement Custodial Account</i> to include language consistent with our recommendation to clarify that only the first seven articles of the forms are approved by IRS.</p>
<p>GAO-19-495: Individual Retirement Accounts: Formalizing Labor’s and IRS’s Collaborative Efforts Could Strengthen Oversight of Prohibited Transactions (June 2019)</p>	
<p>1. The Secretary of Labor should document internal policies and procedures for managing the IRA prohibited transaction exemption process.</p>	<p>Not implemented. The Department of Labor (DOL) agreed with this recommendation and, as of August 2019, planned to create an internal procedure manual formalizing the Office of Exemption Determinations’ administrative case processing procedures to help in passing along institutional knowledge.</p>
<p>2. The Secretary of Labor, in consultation with the Commissioner of Internal Revenue, should establish a formal means, such as a memorandum of understanding or other mechanism, to support and guide DOL’s and IRS’s collaborative efforts to oversee IRA prohibited transaction exemptions.</p>	<p>Not implemented. DOL agreed with this recommendation and plans to periodically discuss all IRA exemption cases with IRS. As of August 2019, DOL planned to document its IRS communication process in its forthcoming internal procedure manual.</p>
<p>3. The Commissioner of Internal Revenue, in consultation with the Secretary of Labor, should establish a formal means, such as a memorandum of understanding or other mechanism, to support and guide DOL’s and IRS’s collaborative efforts to oversee IRA prohibited transaction exemptions.</p>	<p>Not implemented. IRS agreed with this recommendation and said it is committed to discussing an appropriate mechanism, including periodic meetings, to formalize collaboration on IRA prohibited transaction exemptions. IRS planned to consider expanding its formal collaboration with DOL as part of the next periodic update of the existing employee plan memorandum of understanding. As of October 2019, IRS officials said providing additional information about prohibited transaction rules for IRA owners, as recommended in GAO-15-16, could be a collaboration opportunity.</p>

Source: GAO. | GAO-20-210

Appendix II: IRS Information for IRA Owners Investing in Unconventional Assets

This appendix describes: what information for individual retirement account (IRA) owners with unconventional assets can be found in Publications 590-A and 590-B, what other Internal Revenue Service (IRS) sources provide relevant information, and what information was not readily available on the IRS website for the four compliance areas we identified through prior work as likely to affect IRA owners with unconventional assets.¹ The information below does not include the Internal Revenue Code or detailed and technical resources published in the weekly Internal Revenue Bulletin, such as tax regulations, revenue rulings, and revenue procedures.

Barred investments

Publications 590-A and 590-B explain what types of IRA investments are barred, such as collectibles, but the publication does not have additional information that could be useful to IRA owners with allowable investments in coins and bullion. The publications define collectibles as including artworks, rugs, antiques, metals, gems, stamps, coins, alcoholic beverages, and certain other tangible personal property.² The publications explain that if a traditional IRA invests in collectibles, the amount invested is considered distributed, and that the IRA owner could be subject to an additional tax on early distributions. Publications 590-A and 590-B further explain that an exception exists for IRA investments in certain types of coins and bullion. However, the two-part publication does not indicate that certain types of bullion must be stored by a bank or an IRS-approved non-bank trustee.³ The two-part publication also does not mention that IRA investments in life insurance contracts are not permitted.⁴

¹Beginning for tax year 2014, IRS split Publication 590 into two parts. Publication 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*, covers contributions to traditional and Roth IRAs as well as the rules for rollover and conversion contributions. Publication 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*, covers distributions from traditional and Roth IRAs as well as the rules for required minimum distributions and IRA beneficiaries. At the time of our review, the latest Publications 590-A and 590-B were those for tax year 2018.

²Publications 590-A and 590-B do not provide additional information about the last type of collectible—"certain other tangible personal property." Other tangible personal property refers to personal property specified by the Secretary of the Treasury. See 26 U.S.C. §408(m)(2).

³See 26 U.S.C. Section 408(m)(3).

⁴See 26 U.S.C. Section 408(a)(3).

Two IRS web pages listing frequently asked questions (FAQs) about retirement plans contain additional information about bullion storage requirements and IRA investments in life insurance contracts.⁵ Both web pages state that investing IRA funds in life insurance contracts and collectibles are prohibited, and they also note the exception for certain precious metals. One of the web pages further explains that allowable bullion must be stored with a bank or an IRS-approved non-bank trustee.⁶

Prohibited transactions

Publications 590-A and 590-B define prohibited transactions in general terms, list examples, and explain the consequences of engaging in a prohibited transaction. The two-part publication also cautions that the risk of engaging in a prohibited transaction in connection with an IRA account may be increased when an IRA owner invests in nonpublicly traded assets or assets that an IRA owner directly controls. However, the publication does not provide any information about applying for an exception to the prohibited transaction rules.

We found some limited information about exemptions to the prohibited transaction rules on an IRS web page entitled “Retirement Plan Investments FAQs.”⁷ The web page explains that the Department of Labor (DOL) has granted class exemptions for certain types of investments under specific conditions, and that a plan sponsor may apply to DOL to obtain an administrative exemption for a particular proposed transaction that would otherwise be prohibited. However, the web page

⁵IRS, “IRAs FAQs—Investments,” <https://www.irs.gov/retirement-plans/retirement-plans-faqs-regarding-iras-investments>. Accessed September 11, 2019. IRS, “Retirement Plan Investments FAQs” <https://www.irs.gov/retirement-plans/retirement-plan-investments-faqs>. Accessed December 3, 2019.

⁶That web page—“IRAs FAQs—Investments,” <https://www.irs.gov/retirement-plans/retirement-plans-faqs-regarding-iras-investments>, also explains that the requirement applies to indirect acquisition of bullion, such as having an IRA-owned limited liability company buy the bullion.

⁷IRS, “Retirement Plan Investments FAQs,” <https://www.irs.gov/retirement-plans/retirement-plan-investments-faqs>. Accessed December 3, 2019. We found two other web pages under the IRS.gov category of Retirement Plan Topics, but neither web page provides information about the Department of Labor exemption process: <https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-prohibited-transactions>, and <https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-tax-on-prohibited-transactions>. Accessed November 21, 2019.

does not provide any links to DOL information such as a DOL publication that explains the prohibited transactions exemption process.⁸

Unrelated business income

In February 2018, IRS updated Publications 590-A and 590-B to include information about IRAs with unrelated business income. Publications 590-A and 590-B now explain that an IRA is subject to tax on unrelated business income if the IRA carries on an unrelated trade or business. Publications 590-A and 590-B state that the IRA trustee is required to file a Form 990-T if an IRA has \$1,000 or more of unrelated trade or business gross income. For more information, Publications 590-A and 590-B direct taxpayers to consult Publication 598, *Tax on Unrelated Business Income of Exempt Organizations*.⁹

Publication 598 lists IRAs as one of many exempt entities subject to taxes on unrelated business income, and the requirement to file Form 990-T for gross income of \$1,000 or more. Publication 598 describes dozens of activities by tax-exempt organizations that would be considered an unrelated business; but the publication does not include any examples specific to IRA investments that could also be considered unrelated business activities and subject to taxes. Our search did not find additional information on IRS.gov relating to IRAs and unrelated business income taxes.

Fair market value (FMV)

Publications 590-A and 590-B do not provide guidance about how to accurately determine the FMV of hard-to-value unconventional assets. IRS requires custodians to report (on Form 5498) an IRA's FMV at year's end as well as some additional information for IRAs with unconventional assets. The instructions for completing Form 5498 explain that IRA custodians are responsible for ensuring that "all IRA assets (including those not traded on established markets or not having a readily determinable market value) are valued annually at their FMV." However, neither the form's instructions nor Publications 590-A and 590-B provide guidance or tips on how to determine the FMV of non-publicly traded or other hard-to-value assets.¹⁰ As we previously reported, some

⁸DOL, *Exemption Procedures Under Federal Pension Law*. Available at <https://www.dol.gov/sites/dolgov/files/EBSA/about-ebsa/our-activities/resource-center/publications/exemption-procedures-under-federal-pension-law.pdf>. Accessed April 8, 2019.

⁹IRS, Publication 598, *Tax on Unrelated Business Income of Exempt Organizations*, Feb. 26, 2019.

¹⁰IRS, *2019 Instructions for Forms 1099-R and 5498*, Dec. 18, 2018.

unconventional assets may require a third-party appraisal to determine their FMV.¹¹

One IRS web page titled, “Valuation of Plan Assets at Fair Market Value,” provides some additional FMV information but it is intended more for the valuing assets in employer-provided retirement benefits like traditional pensions and 401(k) plans.¹² The web page states that an accurate assessment of the FMV of retirement plan assets is essential for complying with Internal Revenue Code requirements and avoiding prohibited transactions. The web page also states that for defined contribution plans like a 401(k) plan, investments must be valued at least once per year in accordance with a consistent and uniform method. For traditional pensions (defined benefit plans), tax regulations define FMV for purposes of valuing plan assets as “the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.”¹³

The Department of the Treasury (Treasury) plans to issue regulations on IRAs. IRS officials told us that these new regulations would address FMV for certain categories of hard-to-value unconventional assets. IRS officials also told us that it would be premature to publish new guidance for IRA owners and custodians on the FMV of unconventional assets until the new regulations are issued. In their October 2019 update of planned guidance projects, Treasury’s Office of Tax Policy and IRS listed planned IRA regulations.¹⁴

¹¹See [GAO-17-102](#).

¹²IRS, “Valuation of Plan Assets at Fair Market Value,” <https://www.irs.gov/retirement-plans/valuation-of-plan-assets-at-fair-market-value>. Accessed December 3, 2019.

¹³See 26 C.F.R. § 1.412(c)(2)-1(c).

¹⁴Department of the Treasury, Office of Tax Policy and Internal Revenue Service, *2019-2020 Priority Guidance Plan* (released Oct. 8, 2019). See page 12, item 2. Regulations under §§ 219, 408, 408A, and 4973 regarding IRAs. The *Fall 2019 Unified Agenda of Regulatory and Deregulatory Actions* (published by the Office of Management and Budget’s Office of Information and Regulatory Affairs) also lists regulations providing guidance relating to IRAs as expected in June 2020.

Appendix III: Comments from the Internal Revenue Service



DEPUTY COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

January 14, 2020

Mr. James R. McTigue, Jr.
Director, Tax Issues, Strategic Issues
Mr. Charles A. Jeszeck
Director, Education, Workforce & Income Security
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Messrs. McTigue & Jeszeck:

Thank you for the opportunity to review the draft report of the Government Accountability Office entitled "Individual Retirement Accounts: IRS Could Better Inform Taxpayers About and Detect Noncompliance Related to Unconventional Assets" (GAO-20-210, Job Code 101303).

The Internal Revenue Service (IRS) continually strives to educate taxpayers and detect noncompliance. In this vein, we direct the efforts of multiple divisions toward Individual Retirement Account (IRA) compliance, relating to unconventional assets as well as other potential risk areas.

The draft report contains three recommendations. First, GAO recommends disseminating information about unconventional assets to taxpayers who own IRAs. As the report acknowledges, the IRS already publishes educational booklets on IRAs, as well as web pages, which we can review with an eye toward any update appropriate within the scope of the tax code.

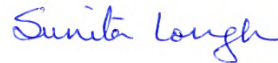
Second, the report recommends an evaluation of the feasibility of listing, as transactions of interest, IRA investments in certain high-risk asset types that are associated with abusive schemes. We plan to do so, based on the data derived from our Compliance Initiative Project started in 2018. As a general rule, a notice requiring the reporting of a transaction as a transaction of interest is drafted by the IRS Office of Chief Counsel for publication by the authority of the Department of the Treasury. To issue such a notice, the IRS would need to describe the transaction in a manner that ensures sufficient information is gathered to analyze and identify abusive transactions, but also would need to describe the transaction with enough specificity to avoid an overly broad description resulting in unnecessary burdens on taxpayers.

2

Third, GAO recommends the development of instructional materials on unrelated business income tax for IRA examiners in the IRS Small Business/Self-Employed division. The IRS is actively engaged in advancing the skills of our staff, and we will renew our efforts at ensuring collaboration with relevant subject-matter experts.

The IRS remains committed to the continuous improvement of tax compliance, and we appreciate the interest in this important topic. If you have questions, please contact me, or a member of your staff may contact Catherine L. Jones, Acting Director, Employee Plans, at (202) 317-8700.

Sincerely,



Sunita Lough
Deputy Commissioner for
Services and Enforcement

Enclosure

Enclosure

Recommendation 1

The Commissioner of Internal Revenue should assess options for updating Publications 590-A and 590-B to either include more information or direct taxpayers to other resources for IRA owners with investments in unconventional assets. Such information could include: storage requirements for IRA investments in certain precious metals; valuation methods for hard-to-value IRA assets; the Department of Labor's process for granting exemptions to IRA prohibited transactions rules; and IRA investments with the potential to create unrelated business income tax liabilities.

Comment

We agree to review our educational publications and web pages for appropriate updates within the scope of the tax code. This includes providing a website link in Publications 590-A and 590-B with the Department of Labor procedures for granting prohibited transaction exemptions.

Recommendation 2

The Commissioner of Internal Revenue, building on forthcoming compliance research using new IRA asset data, should evaluate the feasibility of requiring disclosure for high-risk IRA asset types associated with abusive schemes as transactions of interest.

Comment

We agree and will use data from the Compliance Initiative Project started in 2018 to determine whether there are abusive schemes associated with certain asset types. If the data indicate there is such a correlation, then we will evaluate the feasibility of requiring disclosure of such arrangements as transactions of interest. We will share the results of the evaluation with IRS stakeholders including the IRA cross-divisional team.

Recommendation 3

The Commissioner of Internal Revenue should develop resources (such as training materials or job aids) for Small Business/Self-Employed (SB/SE) examiners conducting IRA owner audits that explain how IRAs with unconventional assets can generate unrelated business income tax liability, and how examiners can refer cases to unrelated business income experts in IRS for assistance.

Comment

We agree and will review and update resources for SB/SE examiners conducting IRA owner audits, to include guidance on how to address unrelated business income tax (UBIT). We will also incorporate guidance for completing referrals to UBIT experts when assistance is needed.

Appendix IV: GAO Contacts and Staff Acknowledgments

GAO Contacts

James R. McTigue, Jr., Director, Tax Issues, Strategic Issues, (202) 512-9110 or mctiguej@gao.gov

Charles A. Jeszeck, Director, Education, Workforce, and Income Security Issues, (202) 512-7215 or jeszeckc@gao.gov

Staff Acknowledgments

In addition to the contacts named above, MaryLynn Sergent and David Lehrer (Assistant Directors), Ted Burik, Susan Chin, Steven Flint, Emily Gruenwald, Mark Kehoe, Jungjin Park, and David Reed made key contributions to this report. James Bennett, Amy Bowser, Jacqueline Chapin, Edward J. Nannenhorn, Andrew J. Stephens, Walter Vance, and Adam Wendel also provided support.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through our website. Each weekday afternoon, GAO posts on its [website](#) newly released reports, testimony, and correspondence. You can also [subscribe](#) to GAO's email updates to receive notification of newly posted products.

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, <https://www.gao.gov/ordering.htm>.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on [Facebook](#), [Flickr](#), [Twitter](#), and [YouTube](#).
Subscribe to our [RSS Feeds](#) or [Email Updates](#). Listen to our [Podcasts](#).
Visit GAO on the web at <https://www.gao.gov>.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact FraudNet:

Website: <https://www.gao.gov/fraudnet/fraudnet.htm>

Automated answering system: (800) 424-5454 or (202) 512-7700

Congressional Relations

Orice Williams Brown, Managing Director, WilliamsO@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800 U.S. Government Accountability Office, 441 G Street NW, Room 7149 Washington, DC 20548

Strategic Planning and External Liaison

James-Christian Blockwood, Managing Director, spel@gao.gov, (202) 512-4707 U.S. Government Accountability Office, 441 G Street NW, Room 7814, Washington, DC 20548

