

# IRS CI Background and Current Initiatives

*By Josh O. Ungerman*

Josh O. Ungerman examines the Internal Revenue Service Criminal Investigation Initiatives.

## Introduction

Over the years, Internal Revenue Service Criminal Investigation (“IRS CI”) has been known as a training ground for the finest financial investigators in the federal government. Today, IRS CI is operating with approximately 2,600 Special Agents working over a wide variety of subject matter areas. IRS CI is continuing to realign its focus to include a large percentage of resources on legal source income cases.

## Background

The legacy of IRS CI dates back to 1919 when the Intelligence Unit of the Treasury Department was established. The agents in the Intelligence Units were referred to as “T Men.” The gangster Al Capone, Public Enemy No. 1 in the United States, was finally brought down by the Intelligence Unit of the Treasury. Next, the Intelligence Unit focused its “T Men” on current government officials. At one point in history, over two-thirds of federal prisoners were in jail based on the work of the “T Men.” In his Fiscal 2012 Annual Business Report,<sup>1</sup> Chief IRS CI Richard Weber boasted:

Since our inception in 1919, almost 100 years ago, we often have been the last line of defense in bringing down America’s criminal

elite. Criminal Investigation agents, analysts, and professional staff have a strong sense of purpose, dedication, and passion for following the money and pursuing those who want to terrorize and destroy this country, victimize others, and steal taxpayer dollars.

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Our legacy is one of perseverance and taking on complex, sensitive investigations that many others simply did not have the financial sleuthing ability to complete.

## Current Initiatives of IRS CI

### Offshore Tax Evasion

IRS CI remains diligent in its efforts to prosecute as many noncomplying U.S. taxpayers with intentionally unreported offshore accounts and income as possible. IRS CI has never waived in this task nor backed down from the complexities of many offshore banking and financial arrangements.

While the IRS continues its path of criminal prosecutions with respect to noncompliant U.S. taxpayers with offshore activities, IRS CI remains the gateway for the IRS’s Offshore Voluntary Disclosure Program “OVDP” which offers qualifying cooperating and timely taxpayers the ability to apply for a voluntary disclosure with the IRS.<sup>2</sup>

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IRS CI's job in identifying and prosecuting non-compliant U.S. taxpayers with offshore activities is becoming easier through the Department of Justice's successful issuing of John Doe Summons on both U.S. branches of banks with an offshore presence and correspondent banks. Recently, in the FirstCaribbean International Bank (FCIB) matter, FCIB's use of a correspondent account Wells Fargo, N.A. provided a link for a federal judge in San Francisco to authorize the IRS to serve a John Doe Summons on Wells Fargo seeking information regarding U.S. taxpayers with accounts at FCIB.<sup>3</sup>

The authorization of the John Doe Summons on Wells Fargo as a result of its correspondent banking relationship with the FirstCaribbean International Bank will likely drive many FCIB depositors into the IRS Offshore Voluntary Disclosure Program.

On April 9, 2013, Justice Department Tax Division Assistant Attorney General Kathryn Keneally stated in a news briefing that to the extent that there are people still out there with unreported offshore bank accounts, they should stop waiting and come forward.

### **Tax Related Identity Theft**

IRS CI is experiencing a changing landscape of crime with the advent of so many identity thieves who are using stolen identities to obtain fraudulent income tax refunds. However, the IRS is continuing to follow the money in order to shut down identity theft tax fraud. The IRS has established four scheme development centers in eight cities relating to identity theft income tax refund fraud. The IRS has also established an identity theft clearinghouse.<sup>4</sup>

In her April 9, 2013, news briefing, Assistant Attorney General Kathryn Keneally also reported that the Justice Department is making every effort to make it harder to engage in identity theft without getting caught and to ensure that there will be severe punishment when people do get caught.

### **Terrorist Financing**

IRS CI financial expertise is being utilized to follow the money in terrorists financing cases. It is of interest that these cases are not necessarily tax crimes. The IRS has developed a counter-terrorist lead development center.<sup>5</sup>

### **Public Corruption**

When IRS CI began in 1919, after taking down Al Capone, they turned their focus toward corrupt public officials. The IRS remains actively involved in working

public corruption cases. This is especially true with other governmental agencies.<sup>6</sup>

### **Suspicious Activity Reports (SAR)**

The IRS has become very adept at using SARs to initiate criminal investigations. The IRS currently is utilizing 94 SAR teams and over 50 dedicated IRS CI led task forces.<sup>7</sup> The SAR teams review SARs daily.

### **Money Laundering and Forfeiture**

In addition to investigating money laundering and implementing asset forfeiture techniques in illegal source income investigations, IRS CI has shifted these tools to legal source after tax scenarios as the factual basis for structuring an asset forfeiture in many current investigations.<sup>8</sup>

Our Bank Secrecy Act (BSA) teams are doing amazing work—reviewing hundreds of thousands of Suspicious Activity Reports (SARs), finding good cases, investigating them and forfeiting millions of dollars in illegal proceeds.<sup>9</sup>

### **Annual Sweeps Week (Week of April 15)**

The IRS is gears up each January with over 800 enforcement actions for a culmination regarding a big public statement of enforcement actions occurring during the week of April 15.<sup>10</sup>

### **Sequestration**

On April 9, 2013, Justice Department Tax Division Assistant Attorney General Kathryn Keneally stated in a news briefing that "[N]obody should think that now is the time to engage in tax fraud because of sequestration. We are very much here. We are very much committed to enforcement."

## **Fiscal Year 2012 IRS CI Annual Business Report**

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### **Highlights**

IRS CI initiated 5,125 cases in fiscal year 2012.<sup>11</sup> IRS CI increased investigation completions in fiscal year 2012 up to 4,937 which represents a five percent increase over fiscal year 2011.<sup>12</sup> IRS CI increased prosecution recommendations from fiscal year 2011 to fiscal year 2012 by 8.5 percent with a total of 3,701 prosecution recommendations.<sup>13</sup> The largest

percentage increases from fiscal year 2011 to fiscal year 2012 were the convictions, which total 2,634.<sup>14</sup> Finally, a slight increase in conviction rate resulted in a 93-percent conviction rate for fiscal year 2012.<sup>15</sup>

## Fraud Referral Program

IRS CI has placed a high degree of emphasis on the Fraud Referral Program recognizing that a good source of investigations comes from the Civil IRS Divisions in the form of fraud referrals. IRS CI is working fraud referrals through the Small Business/Self-Employed, Wage and Investment, and Large Business International Divisions of the IRS.<sup>16</sup> IRS CI has committed to timely evaluate each fraud referral from these three civil divisions of the IRS.<sup>17</sup>

## Legal Source

### Tax Crimes

**General Tax Fraud.** The IRS CI Fiscal 2013 Annual Business Report describes general tax fraud investigations as the backbone of CI's enforcement program. The report focuses on taxpayers ranging from wage earners all the way up to corporate executives who do not pay their fair share of taxes through "willful non-compliance." The schemes described in the report include:

- deliberately under-reporting or omitting income ("skimming");
- maintaining two sets of books;
- entering false entries in books and records,
- claiming personal expenses as business expenses;
- claiming false deductions or credits against taxes; and
- hiding or transferring assets to avoid payment to the IRS.

**Refund Fraud Program-Return Preparer Program.** IRS CI is looking for the orchestrated preparation and filing of false income tax returns by dishonest preparers. The schemes IRS CI are encountering include:

- inflated personal expenses;
- inflated business expenses;
- false deductions;
- excessive exemptions; and
- unallowable tax credits.

Of note is that the Annual Business Report acknowledges that the return preparers' clients may not have knowledge of the falsity of the returns in issue.

**Refund Fraud Program—Questionable Refund Program.** The report describes this category of schemes as involving individuals filing false tax returns using taxpayer identification numbers of other individuals.

Interestingly, the Annual Business Report acknowledges that sometimes the information of an individual that is used for a false return can be unknowingly usurped.

**Identity Theft.** The IRS CI Annual Business Report discusses identity theft at length. Among the topics discussed are the identity theft clearinghouse, stolen identity refund fraud, and the Victim Waiver Pilot Program.

**Abusive Tax Schemes.** The IRS CI Annual Business Report identifies the focus of CI on promoters and their clients who willfully participate in both domestic and/or offshore tax schemes. The IRS CI Annual Business Report identifies that the participants use and create structures such as trusts, foreign corporations and partnerships for the purpose of making it appear that a true owner of assets and income is:

- trustee;
- nominee;
- nonresident alien; or
- foreign entity, when in fact a true ownership and control remains with a U.S. taxpayer.

**Nonfiler Investigations.** The IRS CI Annual Business Report describes nonfilers as "individuals who simply refuse to comply with the law." IRS CI is very concerned that the active nonfiling undermines public confidence and the IRS' ability to administer tax laws fairly and effectively. High income nonfiler cases should continue to grow.

**Employment Tax.** The IRS CI Annual Business Report describes the following employment tax evasion schemes:

- "Pyramiding"
- Employee leasing
- Paying employees in cash
- Filing false payroll tax returns
- Failing to file payroll tax returns

The Annual Business Report notes that some business owners intentionally fail to remit taxes which are withheld from their employees' paychecks.

## Illegal Source

### Financial Crimes

The IRS CI Annual Business Report identifies illegal financial crimes that include financial institution fraud, public corruption, corporate fraud, gaming, insurance fraud, healthcare fraud and bankruptcy fraud.

## International Operations

A major theme of the International Operations section of the IRS CI Annual Business Report is international

collaboration. International collaboration is described as vital to IRS CI's efforts to combat offshore tax evasion and fraud. IRS CI Special Agents and Attachés are "strategically" stationed in ten foreign countries. Additionally, current overseas offices are in:

1. Beijing, China;
2. Bogota, Columbia;
3. Bridgeton, Barbados;
4. Frankfurt, Germany;
5. Hong Kong, China;
6. London, England;
7. Mexico City, Mexico;
8. Ottawa, Canada;
9. Panama City, Panama; and
10. Sydney, Australia.

IRS CI has established the International League Development Center which is specifically tasked with conducting research on potential international criminal investigations. Furthermore, IRS CI has personnel assigned to Interpol in Washington, D.C. who assist in joint investigations in the apprehension of international fugitives. Finally, Simultaneous Criminal Investigation Program Agreements provide IRS CI with the ability to share financial information on criminal tax suspects along with associated parties and promoters who are based in both the foreign jurisdiction and the United States. IRS CI currently has SCIP agreements:

- Mexico;
- Italy;
- France;
- Canada;
- South Korea; and
- Japan.

### Money Laundering and Bank Secrecy Act (BSA)

Interestingly, the IRS CI Annual Business Report describes the laundering of criminally derived pro-

ceeds as a major challenge facing IRS CI. The IRS CI Annual Business Report admits that in "most" money laundering cases, the money involved is earned from an illegal enterprise and the goal is to give the money the appearance of coming from a legitimate source. The IRS CI Annual Business Report does not address the increase in the segment of the BSA structuring case solely involving legal source after tax funds.

#### ENDNOTES

- <sup>1</sup> IRS CI Fiscal Year 2012 National Operations Annual Business Report – Chief's Message – Richard Webber, at 2, available at [www.irs.gov/pub/foia/ig/ci/REPORT-fy2012-ci-annual-report-05-09-2013.pdf](http://www.irs.gov/pub/foia/ig/ci/REPORT-fy2012-ci-annual-report-05-09-2013.pdf). IRS Voluntary Disclosure Program Frequently Asked Questions and Answers (June 26, 2012), at #23.
- <sup>2</sup> IRS Voluntary Disclosure Program Frequently Asked Questions and Answers (June 26, 2012), at #23.
- <sup>3</sup> DOJ Press Release, Court Authorizes Service of John Doe Summons Seeking the Identities of U.S. Taxpayers with Offshore Accounts at Canadian Imperial Bank of Commerce's First Caribbean International Bank (Apr. 30, 2013).
- <sup>4</sup> IRS Criminal Investigation Targets Identity Theft Refund Fraud FS-2013-4 (Feb. 2013).
- <sup>5</sup> IRS Criminal Investigation Responds to Terrorism (Mar. 8, 2013).
- <sup>6</sup> IRS Public Corruption Investigations – Criminal Investigations (CI) (Oct. 17, 2012).
- <sup>7</sup> IRS CI Fiscal Year 2012 National Operations Annual Business Report – Money Laundering and Bank Secrecy Act (BSA), at 21.
- <sup>8</sup> For example, in a currency structuring investigation where the funds are deemed to be from a legal source and after-tax income, the IRS may still assert a forfeiture penalty on the funds at issue and may use the IRS Mitigation Guidelines as guidance of the amount to be forfeited. See e.g. *IRM Exhibit 9.7.7-5*.
- <sup>9</sup> IRS CI Fiscal Year 2012 National Operations Annual Business Reports – Chief's Message – Richard Webber, at 2.
- <sup>10</sup> *Id.* Accomplishments – Overall Fiscal Year 2012 (FY 2012) Investigation Statistics, at 4.
- <sup>11</sup> *Id.*
- <sup>12</sup> *Id.*
- <sup>13</sup> *Id.*
- <sup>14</sup> *Id.*
- <sup>15</sup> *Id.*
- <sup>16</sup> *Id.* Legal Source Tax Crimes – Fraud Referral Program, at 7.
- <sup>17</sup> *Id.*

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