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STATEMENT OF

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GENERAL GOVERNMENT DIVISION

BEFORE THE

SUBCOMMITTEE ON TREASURY, POSTAL

SERVICE, AND GENERAL GOVERNMENT

SENATE COMMITTEE ON APPROPRIATIONS

ON CHANGES NEEDED TO STRENGTHEN

FEDERAL EFFORTS TO COMBAT NARCOTICS TRAFFICKING

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Mr. Chairman and Members of the Subcommittee:

Our testimony today deals with several specific actions needed to strengthen the ability of various Federal agencies, particularly the Drug Enforcement Administration (DEA) and the Internal Revenue Service (IRS), to deal with the narcotics problem.

Incarcerating major traffickers for long periods and causing forfeiture of their financial resources are key elements to successfully reducing the narcotics problem. This requires close interaction and coordination among Federal law enforcement agencies, including DEA and IRS.

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For various reasons, however, neither DEA nor IRS have performed many finance-oriented narcotics investigations.

Knowledge of money flows, along with other information, is essential to identifying and immobilizing narcotics traffickers. Although DEA has the legal authority, under various U.S. code sections, to seek forfeiture of traffickers' illegally derived assets, it does not have the extensive financial expertise needed to perform such investigations. IRS, on the other hand, has the financial expertise and, thus, can play an important role. However, legal obstacles, little overall direction, and changing priorities have hindered these and other agencies from fully using and coordinating their unique skills, jurisdictions, and resources. As a result, the Federal Government lacks a well integrated, balanced, and coordinated approach to the problem and has had only limited success in immobilizing financial resources of high-level traffickers.

To improve Federal efforts to combat narcotics trafficking, the Congress needs to amend the disclosure and summons provisions of the 1976 Tax Reform Act. However, the Tax Reform Act is only one of many impediments affecting Federal efforts. Under existing law, IRS, DEA, and the Justice Department can take certain administrative actions to improve their cooperation and coordination on narcotics matters. Chief among these actions is the need for DEA to make greater use of asset forfeiture authority by focusing more on the financial transactions

connected with the narcotics business.

To begin with, however, I would like to discuss the need for legislative revisions to the 1976 Tax Reform Act.

CONGRESS NEEDS TO AMEND THE DISCLOSURE AND SUMMONS PROVISIONS OF THE 1976 TAX REFORM ACT

In our March 12, 1979, report (GGD-78-110) on the effects of the disclosure and summons provisions of the 1976 act, we pointed out that the disclosure provisions had afforded taxpayers increased privacy over information they provide IRS by placing substantial restrictions on access to such information. At the same time, however, these provisions have had some adverse impact on coordination between IRS and other law enforcement agencies.

In December 1979, the Senate Permanent Subcommittee on Investigations held hearings on the narcotics trafficking problem. It concluded that the disclosure provisions had seriously impeded Federal efforts to deal with the problem and needed to be amended.

In our testimony before the Permanent Subcommittee, we supported the need for a revision to the law but emphasized the importance of striking a proper balance between legitimate privacy concerns and equally legitimate law enforcement information needs. In this regard, we were particularly concerned that present law provides no means for IRS to initiate disclosure of information it obtains from the taxpayer regarding the commission of non-tax crimes.

We therefore recommended that the Congress authorize IRS to disclose such non-tax criminal information by obtaining an ex parte court order.

As a result of the hearings, identical bills (S. 2402 and H.R. 6826), which would significantly revise the disclosure statute, were introduced in the Senate and the House. The Administration is also developing a position on the disclosure issue and plans to submit its own legislative proposal in the near future.

In our March 1979 report and December 1979 testimony, we also pointed out that the third-party summons provisions of the 1976 Tax Reform Act were impeding investigative efforts by causing unreasonable delays in granting IRS access to information it needed to enforce the tax laws. The provisions require IRS to notify affected taxpayers after issuing a summons to a third-party recordkeeper. The taxpayer has 14 days within which to stay compliance by merely notifying the person summoned not to comply. IRS must then initiate court action to enforce the summons. The taxpayer can, but is not required to, intervene in the court proceedings. As a result, many individuals stay compliance to delay ongoing tax investigations.

We recommended that the Congress consider adopting the stay of compliance procedures contained in section 1105 of the Right to Financial Privacy Act of 1978. That act calls

for an individual to be notified when a Government agency seeks access to financial records by means of an administrative summons. However, at the outset, the affected individual must specify to a court, in writing, why he or she objects to the summons, thus removing the incentive to stay compliance for delay purposes only. The Government must then file with the court its written justification for seeking the records. The law further authorizes the court to reach a decision based on the written affidavits.

As a result of the Senate Permanent Subcommittee's December 1979 hearings, a bill (S. 2403) was recently introduced in the Senate which basically adopts the stay of compliance procedures for IRS third-party summonses contained in the Right to Financial Privacy Act.

However, IRS, DEA, and Justice need not await legislative revisions before taking action to enhance their effectiveness in dealing with narcotics traffickers.

ADMINISTRATIVE CHANGES NEEDED TO ENHANCE THE GOVERNMENT'S NARCOTICS INVESTIGATIVE EFFORTS

These agencies can take certain administrative actions under present law which would lead to a more effective, coordinated Federal effort to immobilize the financial resources of narcotics traffickers. The remainder of my testimony deals with these actions.

DEA needs to make more effective use of asset forfeiture authority

First and foremost among administrative actions which these agencies should take involves DEA using asset forfeiture authority more effectively.

IRS has various means by which it can identify and collect taxes owed by narcotics traffickers on their illicit profits. In the last decade, however, DEA has been granted even broader powers to seek the forfeiture of the profit itself, as well as related assets.

Three Federal statutes allow for the forfeiture of traffickers' narcotics-related assets:

--The Continuing Criminal Enterprise statute (21 U.S.C. 848), part of the 1970 Controlled Substances Act, allows for forfeiture of profits obtained by an individual from the criminal enterprise, upon conviction.

--The Racketeer Influenced and Corrupt Organization statute (RICO) (18 U.S.C. 1961-64), part of the Organized Crime Control Act of 1970, allows for forfeiture, upon conviction, of profit, interest, or property acquired in violation of the RICO statute.

--Title 21, section 881 of the U.S. Code allows for civil forfeiture of vehicles, equipment, and other items used to facilitate controlled substance violations. In addition, since November 1978, this statute also provides for civil forfeiture of moneys or other things of value used in exchange for a controlled substance and all proceeds of that exchange.

However, as discussed in our March 1980 report on DEA's Central Tactical (CENTAC) program, despite the enormous amounts of illegally derived funds generated by narcotics trafficking organizations, few of their assets have been

taken under the forfeiture statutes. With your permission, we would like to submit a copy of the report for the record.

The CENTAC program is DEA's premiere effort to develop conspiracy investigations of high-level narcotics traffickers. DEA determines whether an investigation should be done under the program and is responsible for controlling and coordinating such investigations. The targeted organization usually must be at the top of the criminal hierarchy, be susceptible to immobilization through conspiracy investigations, and have a broad span of drug distributing activities.

CENTAC teams are comprised of DEA headquarters and field personnel and, sometimes, staff from IRS, the U.S. Customs Service, and local police forces. From its inception in 1973 through 1979, CENTAC has completed 21 investigations of major trafficking organizations, which are described in our report. Although CENTAC investigative results have been impressive in terms of the number of high-level traffickers arrested and the stiff prison sentences they have received, the investigations have produced little in the way of forfeitures of illicitly derived assets. For example, five CENTAC investigations we reviewed in detail resulted in no asset forfeitures; yet the organizations involved had estimated annual total earnings of $10 to $35 million each.

The Federal Government has to make more effective use of existing forfeiture authority in order to successfully immobilize narcotics traffickers. To accomplish this, DEA

must establish forfeiture as an operational goal and develop the financial investigative expertise necessary to make such cases. Federal prosecutors now lack experience in using the forfeiture statutes and consider their use time consuming. However, if DEA develops the financial expertise and generates more forfeiture cases, Federal prosecutors must be willing to prosecute narcotics traffickers under these statutes.

Decentralization of disclosure authority within IRS would speed handling of disclosure requests

Second, I would like to discuss administrative actions which IRS can take to speed up disclosures it makes in response to court orders and written head of agency requests, as well as the procedures IRS follows in disclosing information it uncovers concerning non-tax crimes.

Under present law, certain Federal agency heads can gain access to information IRS has collected from taxpayers, their records, or their representatives, by obtaining an ex parte Federal district court order. Similarly, certain Federal agency heads can gain access to information IRS has obtained from third parties by submitting a written request to the Secretary of the Treasury specifying the taxpayer's name and address, the tax periods involved, the statutory authority under which the agency head is proceeding, and the specific reason for needing the tax information.

As you can see in chart I before you (and in appendix I to my prepared statement), present IRS procedures require that a Federal agency head forward court orders and written requests for tax information to the Director of IRS' Disclosure Operations Division in Washington, D.C. Upon receipt, each request is assigned for processing to an operations analyst who sends a clearance request to the affected IRS district office. The district disclosure officer, who is responsible for processing the clearance request, initiates the gathering of the information and routes the request to district Examination, Collection, and Criminal Investigation Division personnel for review. Once the clearance information is received from the three Divisions, the district disclosure officer forwards it to the operations analyst in Washington, D.C., who prepares a draft authorization or declination letter. The Section Chief, Branch Chief, and Division Director, review the letter sequentially with the Division Director making the final decision. If the Division Director authorizes disclosure, an authorization letter is forwarded to the district disclosure officer, who is then free to disclose the requested information, assuming the district can locate that information.

We recently checked IRS' response time on court ordered disclosures and written tax information requests. Four IRS district offices--Jacksonville, Los Angeles, Manhattan, and Philadelphia--responded to court orders in an average of 80, 61, 77, and 50 calendar days, respectively. The same

offices responded to written tax information requests in an average of 85, 68, 88, and 81 days, respectively. The average processing time for written requests is usually longer than for court-ordered disclosures because Justice Department attorneys often seek court ordered disclosure of tax returns while also requesting third-party tax information on an individual taxpayer.

In our view, district offices could respond faster to court orders and requests if IRS would decentralize its disclosure procedures under existing law. As depicted in chart II before you (and in appendix II to my prepared statement), Federal agency heads would forward court orders and written requests for tax information directly to the appropriate IRS district office. Once the district disclosure officer obtained clearance from district Examination, Collection, and Criminal Investigation Division personnel, the District Director, in consultation with the disclosure officer, could authorize disclosure where appropriate. If the disclosure is authorized, the information, if and when collected, could be disclosed immediately. However, we recommend that IRS national headquarters make the final determination when a District Director believes that compliance with a court order or disclosure request might endanger a confidential informant or impair a tax investigation.

Next, I would like to discuss IRS' centralized process for disclosing information it uncovers about non-tax crimes. As you can see in chart III before you (and in appendix III

to my prepared statement), an IRS employee who discovers an indication of a non-tax crime forwards that information, through appropriate channels, to IRS' Disclosure Operations Division in Washington, D.C. A Division operations analyst reviews the information to determine whether it can be disclosed. Then the Section Chief, Branch Chief, and Division Director review the analyst's decision sequentially with the Division Director making the final determination as to whether the information can legally be disclosed. If the Division Director determines that the information was obtained from a third party, it is forwarded to the appropriate Federal agency head. Otherwise, it is retained in IRS' files.

Once again, we propose that IRS decentralize the authority to disclose information about non-tax crimes which it obtains from third parties. This could speed up the process, which takes 43 days on the average now, and encourage IRS employees to seek permission to make such disclosures. According to various IRS officials, the current process discourages employees from seeking permission to disclose information on non-tax crimes. They stated that IRS field employees perceive that information they forward to the national office for disclosure is just "filed." The facts do not support that perception. However, a decentralized disclosure process, such as the one depicted in chart IV before you (and in appendix IV to my prepared statement), could encourage additional disclosures of non-tax crime information already authorized by existing law.

IRS is currently studying its administrative process for initiating disclosure or responding to disclosure requests. We understand that the study will result in some streamlining. Basically, IRS should not incur any additional costs in decentralizing or streamlining its processes. IRS already has a disclosure officer in each district who, with minimal additional training, could assume the responsibilities presently carried out by headquarter's officials. This, in turn, would lessen the burden on IRS' national office, thus reducing administrative and personnel costs.

DEA and IRS need to improve joint investigative efforts against narcotics traffickers

The third administrative action I would like to discuss relates to improvements DEA and IRS can make in their joint investigative efforts against narcotics traffickers.

In accordance with a 1976 DEA/IRS agreement, DEA provides IRS with names and background information on high-level drug traffickers referred to as DEA class I violators. Although IRS gives high priority to evaluating those leads for their criminal and civil tax potential, that process has produced few tangible results. Criminal tax cases are complex in nature and therefore usually take several years to investigate and prosecute. By the time IRS develops a tax case on a class I violator, the violator often has been incarcerated for drug-related or other offenses. In such instances, the Justice Department generally

will not prosecute the tax charges because of its dual prosecution policy, which I will discuss shortly.

During the 3 years ended June 30, 1979, IRS' evaluation of 792 DEA-provided leads resulted in 114 new criminal investigations. Fifty class I violators were already being investigated by IRS when it received the DEA information. Only 11 class I violators had been convicted on criminal tax charges as of December 1979.

In February 1980, to improve DEA/IRS joint efforts, DEA agreed to provide IRS the names and background information on class I and class II violators, and other selected targets who derive substantial income from narcotics activities. Although this agreement should improve the program to some extent, it does not address the timeliness problem. To be effective, IRS needs to learn the identities of DEA investigative targets as early as possible.

Justice's dual prosecution policy limits IRS efforts against narcotics traffickers

A fourth area in which administrative action is needed is Justice's dual prosecution policy.

Justice's policy provides that all offenses arising out of a single transaction, such as drug trafficking and evading taxes on the ensuing profits, should be tried together. The policy has particular impact in the

narcotics area because violators often are arrested and convicted on a narcotics charge before IRS can fully develop the related tax case for prosecution. In such instances, Justice will usually decline to prosecute the person for violations of the tax laws. Thus, IRS would have wasted scarce investigative resources. Moreover, the dual prosecution policy also affects the extent to which IRS intitiates criminal tax investigations of narcotics traffickers since its district Criminal Investigation Division chiefs understandably are reluctant to invest scarce resources in cases which are not likely to be prosecuted.

As an alternative strategy to remedy this problem, Justice needs to develop a more flexible dual prosecution policy. Presently, Justice gives special consideration only to class I violators who receive prison sentences of less than 5 years on non-tax charges. However, in a case where Justice and DEA have not pursued asset forfeiture under the controlled substance laws and the trafficker's illicitly derived assets remain intact, flexibility to consider a subsequent prosecution for a tax violation might be desirable. We believe a policy that takes factors like these into account will place IRS in a better position to evaluate whether the criminal tax consequences of a narcotics case should be pursued.

IRS needs to streamline its grand jury approval process

The fifth area in which administrative action is needed is the cumbersome grand jury approval process, which I would now like to discuss.

The grand jury is a powerful investigative body which, from IRS' standpoint, can be particularly valuable in the narcotics area. A special agent assigned to a grand jury investigation seldom has to deal with disclosure, summons, or dual prosecution problems. However, it takes IRS a long time to approve an agent's participation in a grand jury.

Since passage of the Tax Reform Act of 1976, IRS and other law enforcement agencies have used the grand jury increasingly as a tool for joint investigation and prosecution because it has several advantages over the normal administrative process. Members of grand jury investigative teams representing IRS and other agencies can fully and rapidly interchange information to a degree not otherwise possible under normal administrative procedures. Also, tax evasion charges and other criminal charges can be developed simultanenously, thus avoiding the dual prosecution problem. A grand jury also has the benefit of subpoena power, which is not subject to the multiple restrictions and requirements imposed on IRS summonses.

As depicted in chart V before you (and in appendix V to my prepared statement), IRS' current procedures for approving participation in grand jury investigations are cumbersome and time-consuming. The process begins at the district level with

receipt and evaluation of a Government attorney's grand jury request by an IRS special agent. The attorney's request then is forwarded--through the Director of the district's Criminal Investigation Division, the District Director, and the Regional Commissioner--to the appropriate Regional Counsel for approval. If approved by the Regional Counsel, the request goes directly to the Justice Department's Tax Division for review. With Tax Division approval, a U.S. attorney or strike force attorney can initiate an investigation or integrate IRS agents into a grand jury investigation already in process.

We recently obtained limited statistics from IRS on the timeliness of the grand jury approval process. In IRS' Manhattan district and North Atlantic regional offices, an average of 131 calendar days were needed to process seven recent grand jury investigations approved as of February 29, 1980. On the average, the Regional Counsel used 61 of the 131 days. Similar overall statistics were not available from IRS' Philadelphia district and its Mid-Atlantic region. However, since 1977, the region alone required an average of 59 days to process grand jury requests, 52 of which were used by the Regional Counsel. Also, according to the Assistant Regional Commissioner for Criminal Investigations in the Mid-Atlantic region, the Regional Counsel takes from 1 to 4 months to review grand jury authorizations. Thus, the primary consumer of processing time seems to be the Regional Counsel.

Regional Counsel attorneys must perform a complex and painstaking analysis to determine whether a grand jury is necessary and appropriate. The attorneys seek to ensure that (1) the administrative process cannot develop the relevant facts within a reasonable period of time, (2) coordination of a tax investigation would be more efficient, and (3) the case has significant deterrent potential. While this analysis is necessary, too few attorneys presently are authorized to perform grand jury analyses in the Regional Counsel's office. For example, only two attorneys in the North Atlantic Regional Counsel's office have the authority to analyze grand jury requests. Therefore, they must review all grand jury requests emanating from 10 IRS district offices while carrying out their other responsibilities.

IRS is presently considering a revision to the grand jury review and approval process. The revision would delete the Regional Commissioner's review and substitute the District Counsel review for the existing Regional Counsel review.

IRS needs to use jeopardy and termination assessments more effectively

The last administrative action relates to IRS using its jeopardy and termination assessment powers more effectively.

The Internal Revenue Code provides that when the IRS determines that the collection of a tax may be in jeopardy, it may immediately assess and collect the tax--through

seizure of property, if necessary. If the date for filing a return and paying income tax has not passed, a termination assessment may be made of the tax liability before the end of the tax year. If the due date for filing a return and paying the tax has passed, filing and payment is generally done purusant to a jeopardy assessment.

Between 1972 and 1974, IRS systematically used jeopardy and termination assessments against individuals suspected of, or arrested for, a drug law violation as part of its Narcotics Traffickers Program. In May 1974, however, due to alleged abuses of its assessment powers, IRS modified its criteria for using jeopardy and termination assessments against narcotics traffickers to assure that they were used only in cases with substantial and documentable tax violations. Then, in 1976, the Congress amended the law to afford taxpayers subjected to such assessments quicker judicial remedy than had previously been available. Also, in January 1977, the Supreme Court ruled that a valid search warrant was needed to seize a taxpayer's possessions on the taxpayer's private premises.

The change in law, together with IRS' revised criteria and the 1977 Supreme Court decision, led to a sharp decline in the use of these powerful tools. Total jeopardy assessments, after rising from 298 in fiscal year 1972 to 526 in fiscal year 1974, rapidly declined to 69 by the end of fiscal

year 1979. Similarly, IRS made 5,311 total termination assessments during fiscal years 1972 to 1974, but it made only 756 during the next 5 years.

Although there was definite evidence that IRS had abused its assessment powers during the early and mid-1970s, the statistics indicate that IRS may have abandoned use of these powerful civil tax tools even in situations where it could legitimately and effectively use them.

We believe that IRS can make more effective use of its assessment powers and should increase their use under proper circumstances, subject to the legal and administrative safeguards I mentioned earlier. That this can be done has recently been demonstrated by IRS' Jacksonville district.

Recognizing the serious nature of the narcotics problem, the Jacksonville district has initiated major efforts against narcotics traffickers in recent years. In fiscal year 1979, for example, the district developed 1,730 tax fraud allegations on traffickers and evaluated 173 of those allegations in detail for criminal tax potential. Another 268 of the 1,730 allegations led to audits. Moreover, the district made 15 jeopardy assessments and 53 termination assessments. These civil tax actions enabled IRS to assess traffickers over $21 million in back taxes and penalties. In contrast, IRS' Manhattan district office made only 3 jeopardy and 3 termination assessment, involving a total of about $1 million, during fiscal year 1979.

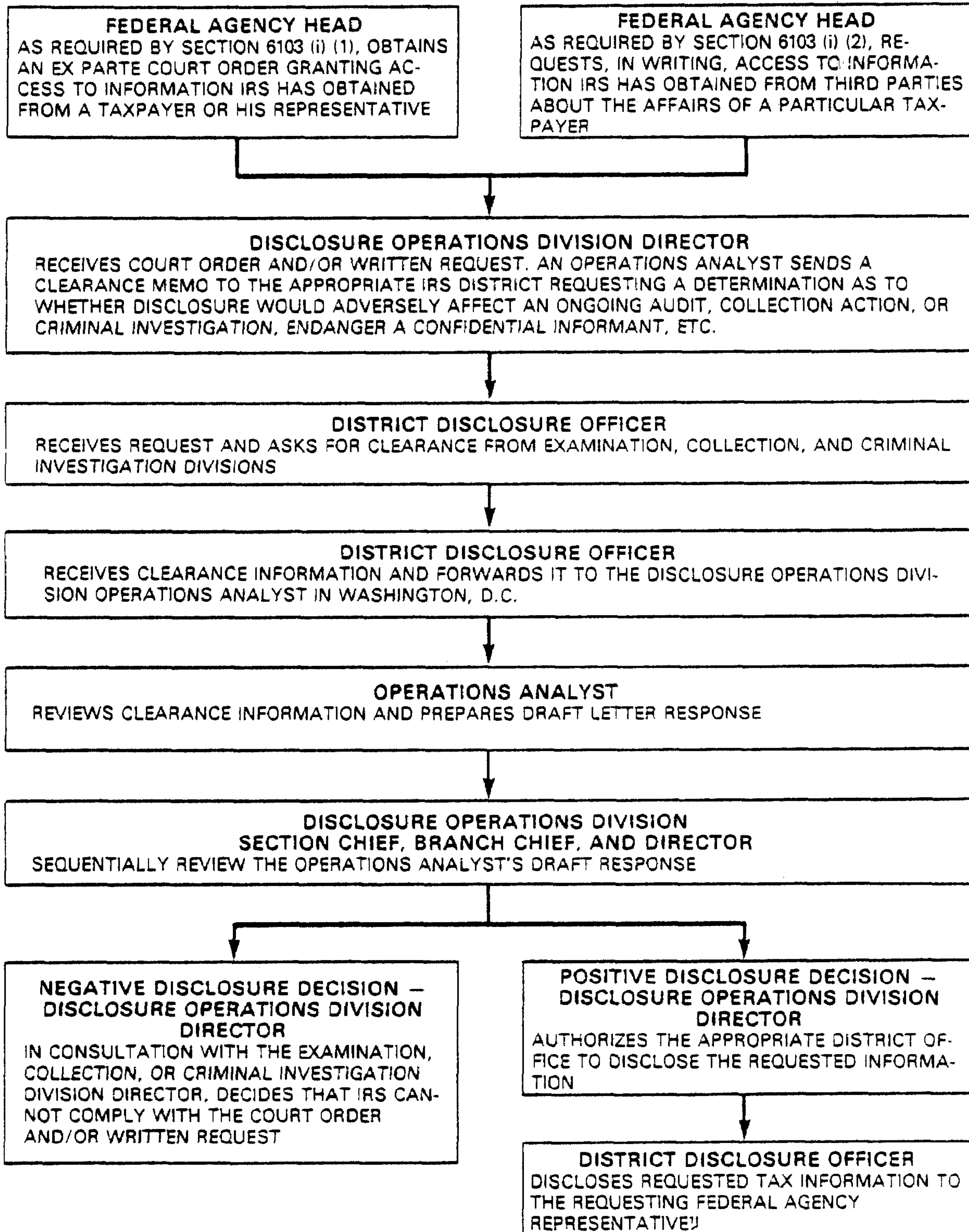
SUMMARY

In summary, a key way for the Federal Government to abate the flourishing narcotics trafficking business is to direct its coordinated efforts at immobilizing the financial resources which support that business. Yet, the Government has had only limited success in this regard because legal and administrative constraints have prevented IRS, DEA, and other agencies from effectively using and coordinating their unique skills, jurisdictions, and resources. Federal narcotics efforts could be improved if the Congress amends the disclosure and summons provisions of the 1976 Tax Reform Act. However, this alone will not resolve the problem. Federal agencies involved in narcotics enforcement need to take certain administrative actions. Most important among these is the need for DEA to make greater use of its asset forfeiture authority to curtail the financial resources of narcotics traffickers.

This concludes my prepared statement. We would be pleased to respond to any questions.

I

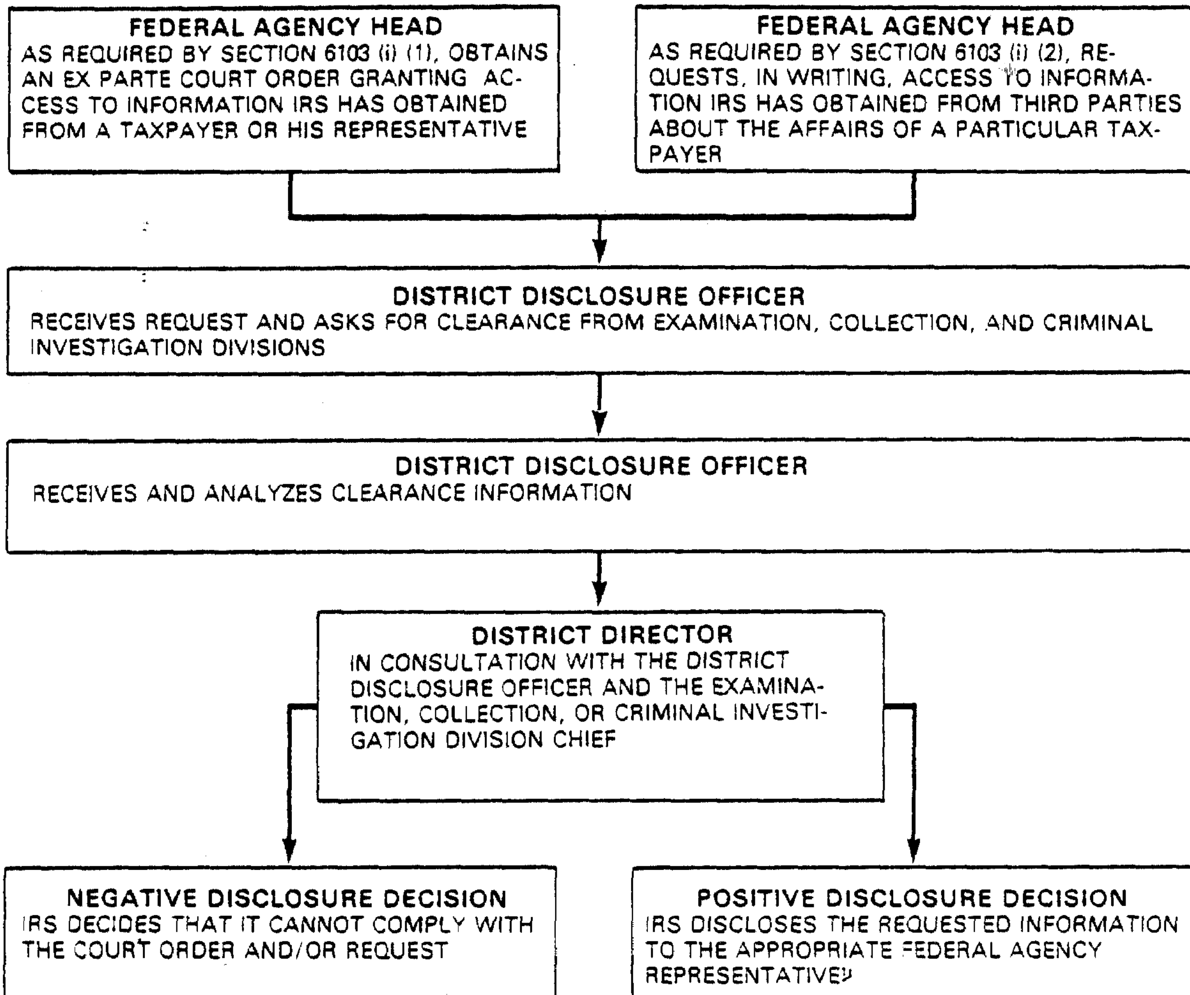
IRS ADMINISTRATIVE PROCESS FOR DISCLOSING INFORMATION UNDER I.R.C. 6103 i (1) AND (i) 2



[a]ALTHOUGH AUTHORIZED TO DISCLOSURE INFORMATION AT THIS POINT, DISCLOSURE MAY NOT BE FEASIBLE FROM AN ADMINISTRATIVE STANDPOINT. WHILE THE DISTRICT HAS BEEN GATHERING THE REQUESTED INFORMATION SINCE RECEIVING THE CLEARANCE REQUEST, THE INFORMATION GATHERING TASK CAN TAKE WEEKS OR MONTHS.

II

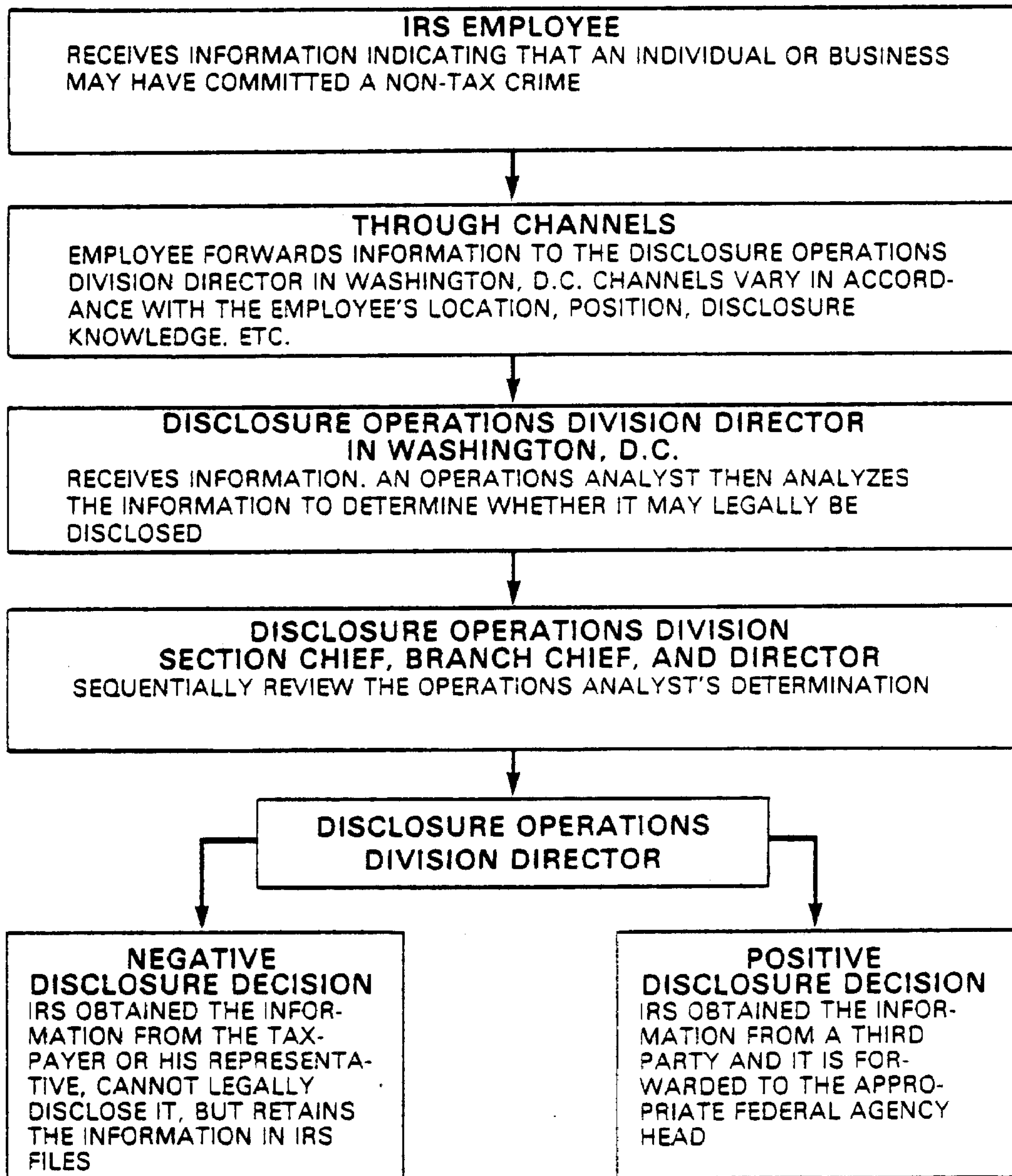
GAO'S PROPOSED REVISION TO THE IRS ADMINISTRATIVE PROCESS FOR DISCLOSING INFORMATION UNDER I.R.C. 6103 i (1) AND (i) 2



[a] WHILE THE DISCLOSURE OFFICER CAN DISCLOSE INFORMATION AT THIS POINT, THE AFFECTED IRS DIVISION MIGHT NEED WEEKS OR MONTHS TO GATHER ALL THE REQUESTED INFORMATION.

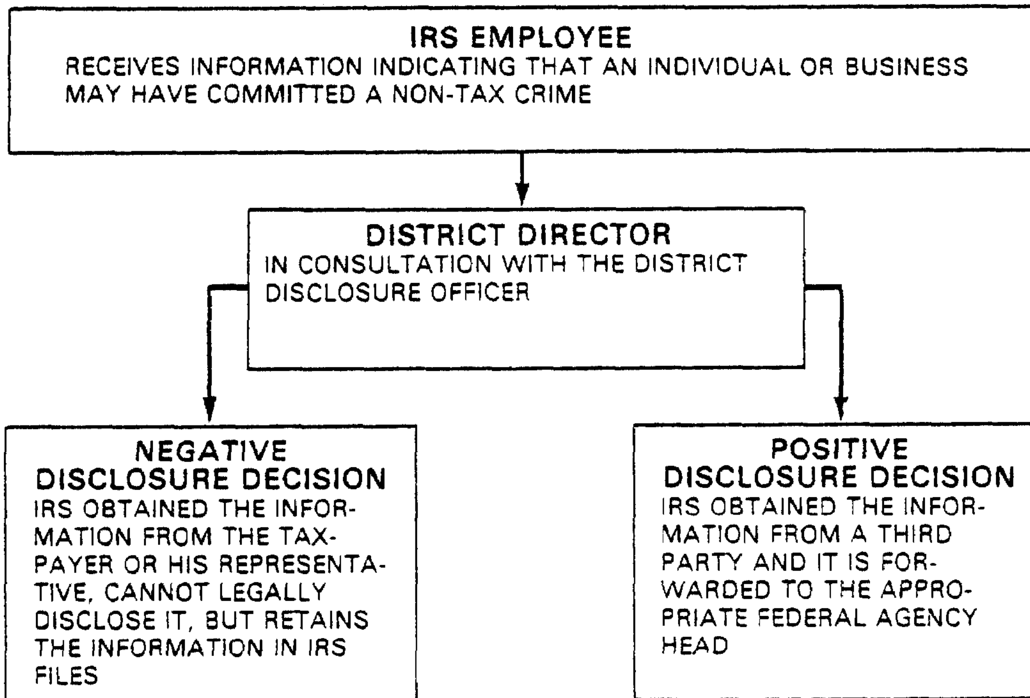
III

IRS ADMINISTRATIVE PROCESS FOR DISCLOSING INFORMATION UNDER I.R.C. 6103 (i) (3)



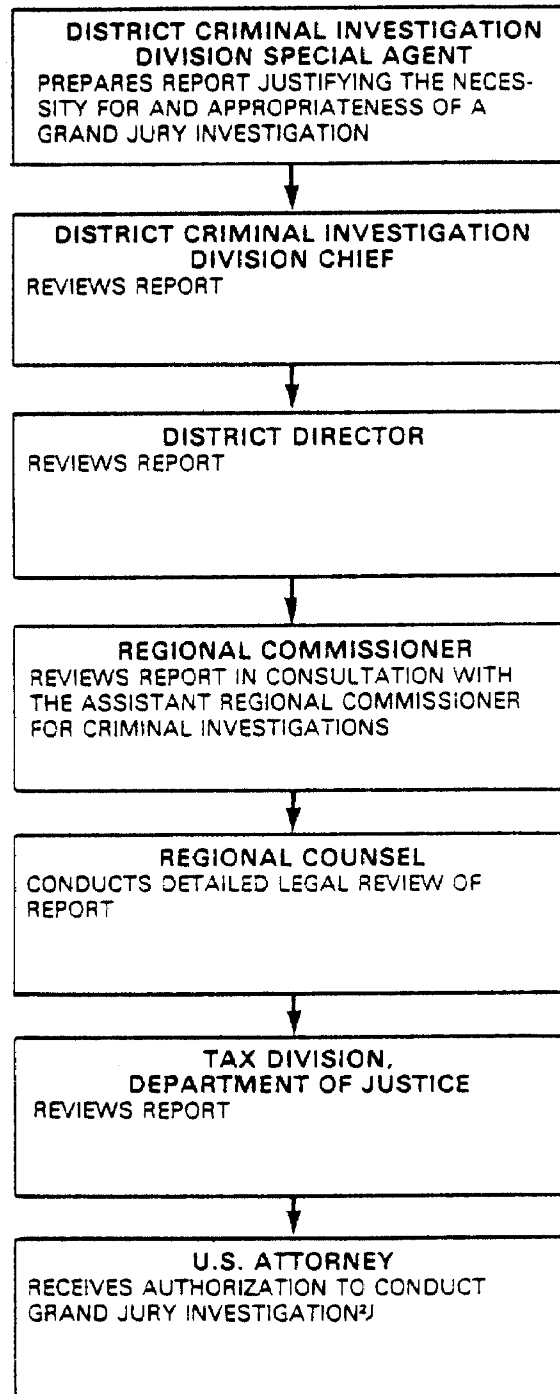
IV

GAO'S PROPOSED REVISION TO THE IRS ADMINISTRATIVE PROCESS FOR DISCLOSING INFORMATION UNDER I.R.C. 6103 (i) (3)



V

ADMINISTRATIVE APPROVAL PROCESS FOR A TYPICAL IRS GRAND JURY INVESTIGATION[1]



[1]EACH REVIEWER IS AUTHORIZED TO APPROVE OR DENY GRAND JURY AUTHORIZATION. DENIALS ARE NOT FORWARDED TO SUBSEQUENT REVIEWERS.

[2]IRS ALSO RECEIVES NOTIFICATION THAT THE TAX DIVISION HAS APPROVED THE GRAND JURY INVESTIGATION.