

**Courts Are Not Always Notified When
Criminals Fail to Comply With Their
Sentences to Settle Civil Tax Liabilities**

March 2004

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INSPECTOR GENERAL
for TAX
ADMINISTRATION

March 12, 2004

MEMORANDUM FOR CHIEF, CRIMINAL INVESTIGATION

Gordon C. Milbourn III

FROM: Gordon C. Milbourn III
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Courts Are Not Always Notified When
Criminals Fail to Comply With Their Sentences to Settle Civil Tax
Liabilities (Audit # 200310012)

This report presents the results of our review of the Criminal Investigation (CI) function's controls to identify, report, and monitor subjects' accounts relating to their sentences to settle civil tax liabilities. The overall objective of this review was to determine if the CI function's controls and procedures are effective to ensure convicted criminals comply with the terms of their sentences requiring the settlement of Internal Revenue Service (IRS) civil tax liabilities.

Upon completion of an investigation in which criminal violations of the law have been documented, the CI function forwards the results of the investigation to the Department of Justice for prosecution. The prosecution process may result in the subject of the investigation signing a plea agreement, pleading guilty, or being found guilty as the result of a trial. A sentence is then imposed on the subject and may include conditions relating to the settlement of the subject's civil tax liabilities, such as the filing of tax returns or payment of tax liabilities. The CI function should take whatever steps are necessary to initiate appropriate legal action in any instance in which a subject has failed to comply with the conditions of a sentence relating to the settlement of civil tax liabilities.

In summary, we found that existing procedures within the CI function and Small Business/Self-Employed (SB/SE) Division did not effectively ensure convicted criminals, who did not comply with the conditional terms of their sentences requiring the settlement of their IRS tax liabilities, were reported to the courts for appropriate legal action. The IRS procedures were either unclear or did not assign specific responsibility for monitoring these taxpayers. In addition, our results indicated the CI function's

Management Information System (CIMIS)¹ contains data errors that could affect analyses used for internal management decisions or results presented in ad hoc reports provided to either internal or external stakeholders.

We recommended the Chief, CI, in conjunction with SB/SE Division management, develop clear and concise guidelines to define responsibilities and procedures to ensure the IRS is controlling and monitoring the accounts of criminal subjects whose court sentences required the settlement of their IRS tax liabilities. To improve the monitoring of these cases within the CI function, we recommended the Chief, CI, ensure court documents are verified; provide formal training to first-line managers on the use of the Measures for Managers (MOM) system that identifies the cases; and seek the advice of the respective CI function and SB/SE Division Counsels, in concert with the Office of the Assistant Chief Counsel (Disclosure and Privacy Law), regarding the disclosure of tax returns and tax return information to probation officers. We also recommended the Chief, CI, develop a process to verify and validate the CIMIS data, and assess the clarity of guidance for coding some data fields and revise, as appropriate, to address the errors identified in the CIMIS.

Management's Response: In general, the Chief, CI, believes certain steps can be taken to enhance the coordinating process with the SB/SE Division and the United States Attorney Offices. CI function management agreed to provide training to first-line managers to help them understand and effectively use the MOM system to identify, report, and monitor terms and conditions on tax investigations. The Chief, CI, agreed to coordinate with the SB/SE Division to review and revise as necessary existing procedures and guidance. The Chief, CI, also agreed to develop a process to identify questionable data field entries in the CIMIS and review existing procedures and CIMIS input instructions on identifying, reporting, and monitoring terms and conditions.

Although the Chief, CI, did not agree with Recommendation 1, stating that existing case closing documents instruct the case agent to attach court documents and send them to the appropriate civil functions, CI management stated they would reinforce these existing procedures. The Chief, CI, also did not agree with Recommendation 4, advising that procedures already exist regarding disclosure of tax returns and tax return information to probation officers, and both the CI function and SB/SE Division will reference these procedures in communications issued to field offices. In addition, the Chief, CI, did not agree with our statements that the CIMIS errors have a measurable impact on tax administration because the CI function does not report information from these data fields. Management's complete response to the draft report is included as Appendix V.

Office of Audit Comment: Regarding the case closing procedures, we believe reinforcing the existing procedures, along with the CI function's commitment to provide additional training and revise other procedures as described elsewhere in this report,

¹ The CIMIS is a database that tracks the status and progress of criminal investigations and the time expended by special agents. It is also used as a management tool that provides the basis for decisions of both local and national scope.

should ensure the required terms of probation are properly identified, reported, and monitored. Regarding the disclosure of information, we believe the law may allow for a broader interpretation than that provided in the procedures. Our recommendation was designed to ensure management considered whether the existing guidance covers a broader interpretation and provided clarification or examples if they believed the guidance may not be interpreted consistently. As to the impact of the CIMIS errors on tax administration, we recognized in our report that these data fields are not routinely used in external or internal reports. Nonetheless, fines and criminal deficiency amounts can be an integral part of the impact of investigative cases. Thus, these data fields should be accurate to provide management with reasonable assurance that this information is reliable if used in ad hoc reports for internal management deliberations. While we still believe our recommendations are worthwhile, we do not intend to elevate our disagreement concerning these matters to the Department of the Treasury for resolution.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

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Background

The mission of the Internal Revenue Service's (IRS) Criminal Investigation (CI) function is to serve the American public by investigating potential criminal violations of the Internal Revenue Code (I.R.C.) and related financial crimes in a manner that fosters confidence in the tax system and compliance with the laws.

Upon completion of an investigation in which criminal violations of the law have been documented, the results of the investigation are forwarded to the Department of Justice for prosecution. The prosecution process may result in the subject of the investigation signing a plea agreement, pleading guilty, or being found guilty as the result of a trial. A sentence is then imposed on the subject and may include conditional terms of probation or supervised release relating to the settlement of the subject's civil tax liabilities, such as the filing of tax returns or payment of tax liabilities. If subjects violate a condition of their sentences, the court may resentence them to include a period of imprisonment.

The CI function and Small Business/Self-Employed (SB/SE) Division each have responsibility for monitoring compliance with conditional terms of probation or supervised release. The Technical Services organization in the SB/SE Division should notify the CI function if tax liabilities have not been fully satisfied prior to the expiration of the probationary or supervised release date.

Upon notification, the CI function should take whatever steps are necessary to initiate appropriate legal action. Vigorous enforcement of the criminal provisions of the I.R.C., along with appropriate civil sanctions, contributes to maintaining voluntary compliance and public confidence in the fairness of the tax system.

During Fiscal Years (FY) 2000 through 2002, the CI function closed about 7,000 investigations in which the subject was sentenced for a criminal violation. According to data obtained from the CI function's Management Information System (CIMIS),¹ approximately 1,050 of these

¹ The CIMIS is a database that tracks the status and progress of criminal investigations and the time expended by special agents. It is also used as a management tool that provides the basis for decisions of both local and national scope.

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individuals had conditional terms of their sentences relating to the settlement of their civil tax liabilities (e.g., file future returns, pay tax liabilities, etc.). The data further indicated about 200 of the 1,050 individuals had conditional terms that needed to be satisfied before October 1, 2002.

We conducted this audit between May and October 2003 in the National Headquarters CI function office in Washington, D.C., and the Chicago, Illinois; Cleveland, Ohio; Newark, New Jersey; and Portland, Oregon, CI function field offices. In addition, we contacted SB/SE Division personnel in the Chicago, Illinois; Cincinnati, Ohio; Denver, Colorado; Newark, New Jersey; and Seattle, Washington, offices. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Criminals Who Did Not Comply Were Not Always Reported to the Courts for Additional Legal Action

The IRS' existing procedures are ineffective in ensuring convicted criminals are referred to the courts for additional legal action when they do not comply with the terms of their sentences that require settlement of their civil tax liabilities. This ineffective coordination between the CI function and the SB/SE Division also contributed to the IRS' inability to properly identify and monitor individuals sentenced to probation or supervised release. As a result, these individuals continue to remain noncompliant, which could undermine the effectiveness of the judicial system when considering the alternatives to or the length of incarceration. This could also negatively affect the public's confidence in the fairness of the tax system.

We reviewed all 37 cases closed in 4 CI function field offices during FYs 2000, 2001, and 2002 in which individuals had been sentenced and a probation expiration date prior to October 1, 2002, had been input to the CIMIS. We also reviewed a random selection of 136² of 627 cases closed by the same 4 CI function field offices during the same period in which the individuals had been sentenced

² One case was a duplicate selection. A total of 135 different cases were reviewed.

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and no probation expiration date had been input to the CIMIS.

Table 1 summarizes the conditions or errors we identified during our review of these cases.

Table 1: Case Review Results

Condition or Errors Identified	37 Cases With Probation Expiration Date	135 Cases Without Probation Expiration Date
Conditional Terms Not Imposed	11	Not Applicable
Probation Expiration Date Incorrect	14 of 26	36 of 135 ³
Computer Transaction Code (TC) 910 Not Input ⁴	6 of 26	31 of 36
The CI Function Did Not Notify the SB/SE Division That There Were Conditional Terms	13 of 26	15 of 36
Individuals Did Not Comply With Conditional Terms	18 of 26	9 of 36
Probation Officers ⁵ or Courts Were Not Notified of the Subject's Noncompliance by the CI function or the SB/SE Division	12 of 18	7 of 9

Source: IRS and court records.

Several factors affected the IRS' collective efforts to identify individuals, who should be monitored for compliance with conditional terms of probation or supervised release, and monitor those accounts:

³ For these 36 cases, court records showed that a probation expiration date should have been entered into the CIMIS but was not.

⁴ The CI function uses TC 910 to monitor accounts of taxpayers on probation (relating to the settlement of civil liabilities and fines).

⁵ Probation officers supervise individuals who are placed on probation or supervised release by a sentencing court and should report any violations to the court.

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- The CI function's procedures were ineffective.
- The SB/SE Division's procedures were ineffective.
- The CI function and SB/SE Division did not coordinate efforts effectively.
- Disclosure procedures may have prevented some criminals from being turned in for violating the terms of their sentences.

The CI function's procedures were not effective

When a sentence imposed on a subject includes conditions relating to the settlement of the subject's civil tax liabilities, the CI function enters the probation or supervised release expiration date in the CIMIS. This enables CI function managers to follow up prior to the expiration date to determine if individuals have complied with the conditions imposed. However, the input instructions state this data field is for "tax cases" and "an entry is required if the court specifies that probation of the sentence or supervised release is conditional upon payment or settlement of the civil tax liability." Several managers interviewed stated they considered a "tax case" as one that involved Title 26⁶ violations. However, there are other titles and sections of the United States Code⁷ that could involve or relate to tax violations and are investigated by the CI function.

In addition, CI function personnel can request a computer transaction code (TC 910) be entered on an individual's tax account to facilitate monitoring of the account. Quarterly listings of tax accounts having this transaction code are automatically generated and sent to CI function special agents. These listings provide details of accounts showing whether tax returns have been filed or liabilities have been paid.

However, the CI function did not have any current Internal Revenue Manual (IRM) procedures or guidelines for the following:

⁶ 26 U.S.C. is the I. R. C.

⁷ For example, 18 U.S.C. § 287 (2003), False, Fictitious, or Fraudulent Claims; and 18 U.S.C. § 371 (2003), Conspiracy to Commit Offense or to Defraud the United States.

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- Instructing when a TC 910 should be input to the tax accounts of individuals who have been given conditional terms of probation or supervised release.
- Reviewing the transcripts generated by the input of a TC 910 to an individual's account.
- Obtaining court documents when the case is closed to determine if the settlement of civil tax liabilities is part of the court sentence.
- Notifying the SB/SE Division of individuals with conditional terms of probation or supervised release requiring the settlement of civil tax liabilities.

CI managers and special agents have access to a memorandum template, through the CI function's Document Manager, which can be used to notify the SB/SE Division if an individual has been given conditional terms of probation or supervised release relating to the settlement of tax liabilities. However, there were no procedures for completing the template.

In addition, there was no standard CIMIS-generated report distributed or made available to first-line managers to assist with monitoring probation dates that have not expired.⁸ This information is available on the CI function's Measures for Managers (MOM) system;⁹ however, we were advised there were no formal training or instructions regarding its use.

The SB/SE Division's procedures were not effective

The Technical Services organization within the SB/SE Division is responsible for coordinating all civil enforcement action on individuals who are under criminal investigation and ensuring civil enforcement action is taken to collect revenue where appropriate. It should update the CI function on the status of cases assigned to it, and the responsible SB/SE Division Territory Manager should

⁸ CI function management advised that CIMIS standard Report Seven provides to the Special Agent-in-Charge (SAC) information on unexpired terms of probation and that the SAC has the ability to disseminate this information to the first-line managers.

⁹ The MOM system is a computer application that assists CI function managers with managing group/agent inventory of cases.

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notify the CI function by memorandum if tax liabilities have not been fully satisfied 180 days prior to the expiration of the probationary or supervised release period.

Based on discussions with Technical Services organization personnel and a review of the Integrated Collection System (ICS)¹⁰ case histories, the CI function was notified concerning the status of the cases (either orally or by memorandum) in 6 of 15 cases.¹¹ There was no indication the CI function was notified in 9 of 15 cases. Five of the 9 individuals had not complied with their conditional terms of probation or supervised release to pay their tax liabilities by the expiration date or within 180 days of the expiration.

Further, there was no indication in the ICS case histories that the Technical Services organization personnel were aware of the procedures or were appropriately monitoring the cases and ensuring actions were taken to notify the CI function of the status of the cases.

Coordination between the CI function and SB/SE Division needs improvement

Procedures for the CI function and SB/SE Division did not assign specific responsibilities for monitoring compliance of all types of conditional terms relating to the settlement of civil tax liabilities. The procedures assigning responsibility to the SB/SE Division pertained to only those individuals with outstanding tax liabilities. Conditions imposed by the courts may require additional or other terms, such as the filing of amended or delinquent tax returns or the timely filing of future tax returns.

In addition, the Technical Services organization's procedures provide for notification by the CI function of individuals who are under investigation or who have conditional terms of probation or supervised release by

¹⁰ The ICS is a computer inventory system used by the Collection function. Cases worked by revenue officers are controlled on the system, and case actions are documented electronically.

¹¹ These cases are associated with the sample of 62 cases with a probation expiration date (see Table 1). They are the cases for which Technical Services organization personnel were aware of the conditional terms and the probationary period either expired or was within 180 days of expiring.

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means of a form¹² the CI function uses to request input of its computer transaction codes. However, the CI function had no current procedures or instructions to send this form to the Technical Services organization. We were advised that either there were no formal procedures or instructions, or they were removed from the CI function portion of the IRM several years ago.

Several CI function managers advised us that, prior to the IRS reorganization, some offices had effective local procedures and good working relationships with the Examination and Collection Divisions. However, since the reorganization, coordination has suffered because there have been no procedures clearly outlining responsibilities for monitoring these cases.

Disclosure procedures may need clarification

Limitations on disclosure of tax returns or tax return information to probation officers may have prevented the referral to the courts of individuals who were not complying with the terms of their sentences relating to the settlement of their civil tax liabilities. CI function and SB/SE Division procedures limit information disclosed to those years specified in the conditions of probation issued by the court or, alternatively, to the conviction years and those years for which the individual is placed on probation. We believe it is possible for IRS employees to interpret these procedures, as worded, too narrowly. They could interpret the phrase “years specified in the conditions of probation issued by the court” as meaning that, absent specific years being identified in the probation terms, permissible disclosures are limited to conviction years and those years for which the individual is placed on probation. We believe, however, the disclosure laws¹³ would permit disclosure for all tax years covered by the terms of the probation, even if no tax years are specifically identified in the terms of the probation. For example, if the terms of probation specified that the individual must file all delinquent returns, disclosure could

¹² Criminal Investigation Control Notice (Form 4135). However, CI function management advised that this Form was not designed for civil notification purposes.

¹³ 26 U.S.C. § 6103(h)(4) (2003), Disclosure in Judicial and Administrative Tax Proceedings.

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be made with respect to years for which the individual has not filed income tax returns.

Additional legal action occurred when individuals did not comply and were reported to the courts

As previously mentioned, when the courts receive notification that individuals failed to comply with the conditional terms of their probation or supervised release, they may resentence them. We identified eight individuals that were reported to the courts for additional legal action. The courts imposed additional prison terms in 3 of these cases, ranging from 1 week to 90 days. This illustrates that the monitoring process can have the intended effect if followed. We did not obtain additional records from the courts to determine why they did not impose additional prison terms in the other five cases.

Collectively, the 27 individuals who did not comply with the conditional terms of their probation or supervised release had over \$2.5 million in unpaid assessed taxes, interest, and penalties and 57 unfiled returns at the time their probationary periods expired. Although there may be reasons individuals may not be able to comply with their conditional terms requiring the settlement of their tax liabilities (e.g., inability to pay, bankruptcy proceeding, etc.), the courts should still be advised to determine if additional punitive actions are appropriate.

The CI function's responsibilities should not end with its issuance of a case report and sentencing by the court. We believe the CI function and SB/SE Division, in their roles to ensure fairness in the tax system and voluntary compliance, share the responsibility to ensure individuals satisfy the terms of their court sentences. Promoting and encouraging increased communication, as well as ensuring adequate controls are in place over cases in which the settlement of civil tax liabilities is a condition of the sentence, can help accomplish these goals. If little or no effort is made to ensure individuals comply, not only could this result in a loss of revenue, it could also erode the public's confidence in the tax system if the individual remains noncompliant and no action is taken to deter this behavior.

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Recommendations

The Chief, CI, should:

1. Establish procedures to ensure that, at the time of the case closing, court documents are obtained and verified to determine if the settlement of civil tax liabilities is a part of the sentence.

Management's Response: The Chief, CI, stated that existing case closing documents in the CI function's document manager electronic forms program instruct the case agent to attach the Judgment and Commitment Order to certain forms and memoranda sent to the civil functions for monitoring terms and conditions of probation. The CI function will take steps to reinforce these existing procedures.

Office of Audit Comment: Reinforcing these procedures, along with the CI function's commitment to provide additional training and revise other procedures as described elsewhere in this report, should ensure the required terms of probation are properly identified, reported, and monitored based on the Judgment and Commitment Orders.

2. Establish periodic systemic reports for first-line managers to use to identify and monitor those closed cases requiring the settlement of IRS tax liabilities or provide formal training to first-line managers on the use of the MOM system.

Management's Response: The Chief, CI, agreed to provide training sessions for first-line managers that will include a workshop to help managers understand and effectively use the MOM system's existing custom query and periodic systemic report to identify, report, and monitor terms and conditions of probation on tax investigations.

3. Coordinate with SB/SE Division management to develop clear and concise procedures to define responsibilities and ensure the IRS is controlling and monitoring the accounts of the individuals whose court sentences require the settlement of their civil tax liabilities. These procedures should address the tools needed for monitoring, as well as monitoring other types of conditional terms such as the filing of returns.

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Management's Response: The Chief, CI, agreed with the recommendation. The CI function and SB/SE Division will review and revise as necessary their existing procedures and guidance on reporting and monitoring terms and conditions of probation on tax investigations. The CI function will coordinate its revisions with the SB/SE Division to ensure closed criminal tax investigations containing terms and conditions of probation are properly identified, reported, and monitored.

4. Seek the advice of the respective CI function and SB/SE Division Counsels, in concert with the Office of the Assistant Chief Counsel (Disclosure and Privacy Law), regarding the disclosure of tax returns and tax return information to probation officers in determining noncompliance with conditional terms of probation or supervised release, and revise the appropriate IRM procedures accordingly.

Management's Response: The Chief, CI, advised that procedures already exist within both divisions and are referenced in an IRM section on probation proceedings used by the Disclosure function. Both the CI function and SB/SE Division will reference these IRM sources in any communication issued to field offices on identifying, reporting, and monitoring terms and conditions of probation.

Office of Audit Comment: We continue to believe U.S.C. § 6103(h) may allow for a broader interpretation of what can be disclosed to probation officers. Our concern centers on how the IRM phrase "...limited to those years specified in the conditions..." provided in each division's respective procedures may be interpreted when the conditions imposed by the courts do not specify the tax years to be covered. We believe the disclosure laws would permit disclosure for all tax years covered by the terms of the probation. For example, if the conditions imposed by a court provide for "filing all delinquent or amended returns within 6 months of the sentence date and to timely file all future returns that come due during the period of probation," disclosure could be made with respect to years for which the individual had not filed income tax returns and those tax returns due during the probationary period. Our

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The Criminal Investigation Management Information System Contained Numerous Errors That Resulted, or Could Result, in Inaccurate Information

recommendation was designed to ensure management considered whether the existing guidance covers this broader interpretation and provided clarification or examples if they believed the guidance may not be interpreted consistently.

We identified numerous errors in the CIMIS data relating to the subjects who were sentenced. Of the 172 cases reviewed, 127 (74 percent) had 1 or more errors in the following data fields:¹⁴

- Probation expiration date - 69 cases (40 percent).
- Amount of fine - 36 cases (21 percent).
- Number of months probation or supervised release - 32 cases (19 percent).
- Sentencing violation - 29 cases (17 percent).
- Number of months sentenced to confinement - 21 cases (12 percent).
- Other fields (judicial district code, court docket number, and terms met) - 42 cases (24 percent).

We identified significant errors in dollar amounts in two data fields: the amount of the fine to pay and the amount of criminal deficiency. Although these figures are not routinely reported to external or internal stakeholders, errors in them raise concerns about the overall accuracy and reliability of the information input to the CIMIS. As described below and in Appendix IV, we identified approximately \$6 billion in overstatements in these 2 data fields, which adversely affects the reliability of management information that could be provided in ad hoc reports generated from the CIMIS.

Inaccurate fine amounts

The CIMIS contains a data field for entering the amounts of fines to be paid by individuals who are sentenced for criminal acts. We identified errors in the amounts of the fines that were input to the CIMIS of \$8.4 million for

¹⁴ Due to our sampling methodology, our results cannot be projected to the overall accuracy of the CIMIS data. See Appendix I.

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2 cases in our review. In both instances, the amount of restitution required to be paid to organizations other than the IRS was input rather than the amount of fine to pay. To evaluate whether this condition existed during the most current fiscal year available, we reviewed the 10 largest amounts input to the CIMIS for FY 2002. This revealed similar errors totaling \$1.3 billion. A standard CIMIS management report reflected an average fine to pay amount of \$1.2 million for FY 2002. Correcting the errors in these 10 cases alone would reduce the average fine to pay for FY 2002 to under \$80,000.

Inaccurate criminal deficiency amounts

The CIMIS also contains a data field for recording the amount of criminal tax calculated in a special agent's report of an investigation when a case is recommended for prosecution. Instructions for the input of these data stated the sum of the individual criminal deficiencies should not exceed the overall deficiency for the entire investigation. If an investigation involves more than one individual, the criminal deficiency amount should be apportioned among them or input for only one, if not apportioned in the special agent's report.

Three cases included in our review were part of 1 investigation that had the criminal deficiency amount for the overall investigation input for each of numerous subjects, resulting in an overstatement of over \$2.7 billion. To evaluate whether this condition existed during the most current fiscal year available, we conducted a limited review of large and/or repetitive amounts of criminal deficiencies input to the CIMIS for FY 2002. This showed that over one-half of the \$7.4 billion total (approximately \$4.7 billion) was in error as follows. For 2 investigations, the cents had been input as dollar amounts, resulting in overstatements of the criminal deficiency amounts of \$1.2 billion. Incorrect criminal deficiency amounts had been input for 2 other investigations in addition to being input for multiple subjects, resulting in overstatements of \$2.6 billion. Similar input errors occurred for another investigation, resulting in a \$900 million overstatement. In addition, the actual amount for this investigation should

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have been input to another CIMIS data field rather than the criminal deficiency data field.

While none of the identified inaccuracies affect the CI function's reported accomplishments to external stakeholders (for example, in IRS Data Books, in the CI function's Annual Business Reports, or on its public web site),¹⁵ our results indicated the CIMIS contained many data errors that could affect analyses used for internal management decisions or results presented in ad hoc reports provided to either internal or external stakeholders.

Results of prior CIMIS reviews

In April 2003, the IRS Offices of Program Evaluation and Risk Analysis (OPERA) and Statistics of Income (SOI) issued the results of a validation of the accuracy, timeliness, and presence of documentation for various CIMIS data fields that had been conducted in collaboration with the CI function. The validation indicated that CIMIS data tested had an accuracy rate of approximately 91 percent. However, the accuracy rate was this high because of the sampling methodology used. If data were not applicable for a case, the data were considered accurate. Because criminal investigations take several years to complete, many cases selected for the validation had not yet resulted in prosecutions or sentencing. Over 300 of the 475 cases sampled did not have applicable data for the principal sentencing violations and months served data fields.

The summary of the OPERA and Office of SOI validation results also advised the validity rates for some fields were closer to the 80 percent validity rate estimated by CI function subject matter experts. The CI function may want to consider emphasizing those data fields as well as assessing the clarity of guidance for coding them.

¹⁵ IRS Data Books are published annually and contain various statistical data pertaining to IRS programs. Reported accomplishments in the three sources include the number of investigations initiated and the number of subjects convicted, sentenced, and incarcerated.

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The Treasury Inspector General for Tax Administration previously recommended¹⁶ the Chief, CI, establish a process by which the CIMIS data will be verified and validated. The Chief, CI, disagreed, stating project plans for a new CIMIS included verification and validation functions and, until the implementation of the new system, the CI function would continue relying on field office management officials to ensure the information in the CIMIS is both current and accurate. Based on discussions with CI function personnel regarding enhancements planned for the upgraded CIMIS, the new system will not have verification and validation functions that would identify or prevent the types of errors identified. Also, based on our tests, field office management officials were not identifying what should have been obvious errors in the CIMIS data.

An effective management information system is necessary for measuring program results and making management decisions. As such, the information recorded in the system should be accurate. Without accurate information, CI function management may rely on incorrect data for making management decisions.

Recommendations

The Chief, CI, should:

5. Develop a process to verify and validate the CIMIS data, as previously recommended.

Management's Response: The Chief, CI, agreed with our recommendation and stated the CI Research section will develop a process to identify questionable data field entries for those CIMIS data fields involved with reporting and monitoring terms and conditions of probation and that do not have internal validity checks. The Research section will periodically send a listing of identified questionable entries in the applicable conditional terms of probation data fields to the responsible field office(s) for verification and/or correction.

¹⁶ GPR: *Criminal Investigation Can Improve Its Performance Measures to Better Account for Its Results* (Reference Number 2002-10-009, dated January 2002).

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Office of Audit Comment: Although CI function management agreed to take action to correct questionable entries in the CIMIS, they did not agree with our statements that these errors have a measurable impact on tax administration because the CI function does not report information from these data fields. We previously recognized in our report that these data fields are not routinely used in external or internal reports, but they nonetheless could be used in ad hoc reports for internal management deliberations, as both fines and criminal deficiency amounts can be an integral part of the impact of investigative cases. As such, these data fields should be accurate, so management can have reasonable assurance that the information is reliable. To clarify, we characterize errors of this nature as “reliability of information,” which we express as the absolute value of overstatements or understatements of amounts recorded on an organization’s systems.

6. Assess the clarity of guidance for coding some data fields and revise as recommended by the IRS OPERA and Office of SOI.

Management’s Response: The Chief, CI, agreed with our recommendation and stated that the CI function will review its existing policy and guidance procedures and CIMIS input instructions on identifying, reporting, and monitoring terms and conditions of probation. The CI function will revise existing policy and guidance documents as needed and issue any clarifying communications to its field offices.

In addition, the Chief, CI, stated the pending upgrade of the CIMIS will require a wholesale change of the existing CIMIS manual that details the input information and criteria for each data field identifying, reporting, and monitoring terms and conditions of probation on tax investigations.

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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine if the Criminal Investigation (CI) function's controls and procedures were effective to ensure convicted criminals comply with the terms of their sentences requiring the settlement of Internal Revenue Service (IRS) civil tax liabilities. To accomplish our objective, we obtained an extract from the CI function's Management Information System (CIMIS)¹ for the period ended September 30, 2002. We confirmed through our transaction testing, described below, that the data in the CIMIS are not completely reliable. However, in all selected cases, the subjects had been sentenced. Specifically, we:

- I. Reviewed applicable policies and procedures defining responsibilities to ensure compliance with terms of sentences relating to the settlement of civil tax liabilities. In addition, we consulted with the Treasury Inspector General for Tax Administration Counsel regarding legal matters discussed in our report.
- II. Determined if subjects identified as having had conditional terms of their sentences relating to civil tax liabilities complied with the conditional terms and if appropriate actions were taken if they did not comply.
 - A. Selected all subjects for 4 judgmentally selected CI function field offices whose cases were closed as having been sentenced during October 1, 1999, through September 30, 2002, and had conditional probation expiration dates input to the CIMIS that were earlier than October 1, 2002. The Chicago, Illinois; Cleveland, Ohio; Newark, New Jersey; and Portland, Oregon, field offices were selected based on geographic location and the number of cases closed with subjects having been sentenced and having conditional probation expiration dates in the CIMIS. The total number of cases in the 4 field offices that met the criteria was 37. The total number of cases that met the criteria in all CI function field offices was 215. The sampling methodology used was due to the small number of cases and because we did not intend to project our results to the entire universe of cases.
 - B. Randomly selected 34 cases that were closed during the same period but did not have conditional probation expiration dates input to the CIMIS from each of the 4 judgmentally selected CI function field offices, for a total of 136.² The total number of cases from each selected office that met the criteria was 627 (146, 135,

¹ The CIMIS is a database that tracks the status and progress of criminal investigations and the time expended by special agents. It is also used as a management tool that provides the basis for decisions of both local and national scope.

² One case was a duplicate selection. A total of 135 different cases were reviewed.

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235, and 111, respectively). The total number of cases that met the criteria in all CI function field offices was 5,946. We used this sampling methodology because we did not intend to project our results to the entire universe of cases.

For those subjects selected in tests II.A. and II.B., we:

1. Obtained and reviewed United States (U.S.) District Court documents.
2. Reviewed the subjects' tax account data.
3. Interviewed CI function and Small Business/Self-Employed Division personnel.

III. Determined if the CIMIS accurately identified and contained information relating to the sentences of the subjects selected in tests II.A. (37 cases) and II.B. (135 cases, excluding the 1 duplicate case) and assessed the impact of any inaccuracies on the CI function's reported accomplishments.

- A. Compared data obtained from U.S. District Court documents to data in the CIMIS relating to convictions and sentences for those cases selected in our samples.
- B. Reviewed selected CIMIS data for Fiscal Year 2002 relating to fines assessed and criminal deficiencies. We reviewed court documents and contacted CI function personnel to determine the actual amounts.
- C. Reviewed CI function accomplishments reported internally and externally in CIMIS reports, in Business Performance Review Reports, in IRS Data Books,³ and on the CI function public web site.

³ IRS Data Books are published annually and contain various statistical data pertaining to IRS programs.

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Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

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Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on the reliability of information in the Criminal Investigation (CI) function's Management Information System (CIMIS).¹ Reliability of information is expressed as the absolute value of overstatements or understatements of amounts recorded on the organization's systems. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Reliability of Information – Actual; an overstatement of \$4.7 billion was identified for the criminal deficiency amounts recorded in the CIMIS for Fiscal Year (FY) 2002 (see page 11).

Methodology Used to Measure the Reported Benefit:

We conducted an analysis and review of select large and/or repetitive criminal deficiency amounts entered in the CIMIS for FY 2002. We subsequently reviewed court documents and followed up with appropriate CI function personnel to determine the correct amounts that should have been entered in the CIMIS. The overstatement is accounted for as follows:

For 2 investigations, the cents had been input as dollar amounts, resulting in overstatements of the criminal deficiency amounts of \$1.2 billion.

Incorrect criminal deficiency amounts had been input for 2 other investigations in addition to being input for multiple subjects, resulting in overstatements of \$2.6 billion.

Similar input errors occurred for another investigation, resulting in a \$900 million overstatement.

Type and Value of Outcome Measure:

- Reliability of Information – Actual; an overstatement of \$1.3 billion was identified for the fine amounts recorded in the CIMIS for FY 2002 (see page 11).

Methodology Used to Measure the Reported Benefit:

We conducted an analysis and review of the 10 largest fine amounts entered in the CIMIS for FY 2002. We subsequently reviewed court documents to determine the correct amounts that should have been entered in the CIMIS.

¹ The CIMIS is a database that tracks the status and progress of criminal investigations and the time expended by special agents. It is also used as a management tool that provides the basis for decisions of both local and national scope.

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Appendix V

Management's Response to the Draft Report



Criminal Investigation

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

RECEIVED
FEB 23 2004

FEB 23 2004

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

Wancy J. Jardini
Chief, Criminal Investigation CI

SUBJECT:

Response To Draft Audit Report—Courts Are Not Always
Notified When Criminals Fail to Comply With Their Sentences
to Settle Civil Tax Liabilities (Audit #200310012)
ECMS IR No. 0401-5VGM42YC

Criminal Investigation (CI) reviewed the Treasury Inspector General for Tax Administration (TIGTA) Draft Audit Report referenced above. Criminal Investigation coordinated this response with representatives from the Small Business and Self-Employed (SB/SE) Operating Division. Your auditors have duly noted that the IRS reorganization took its toll on coordinating efforts and procedures in this subject area. Nonetheless, CI agrees that certain steps can and will be taken to enhance the coordinating process with SB/SE and the United States Attorney Offices (USAO).

In fact, prior to the inception of this particular audit, a working group consisting of representatives from IRS and the Tax Division of the Department of Justice had already been studying the interpretive and procedural issues attaching to the ways in which restitution can be used to collect at least a portion of the tax liability due and owing by a taxpayer who has been convicted of a federal criminal tax violation. The working group also explored some of the problems which complicate the use of restitution for this purpose. In addition, several field offices took the initiative to partner with their local USAOs, Probation Office and IRS Fraud Referral Specialists to study the restitution process. Criminal Investigation will leverage these collective efforts to substantially improve the conditional probation reporting and monitoring process.

Recommendation Comments

Criminal Investigation currently has guidelines in place to monitor investigations where conditions of probation include the settlement of civil tax liabilities. Criminal Investigation is in the process of reinforcing and enhancing these guidelines internally and with SB/SE.

For recommendation one, CI disagrees with TIGTA because the existing case closing documents in CI's document manager electronic forms program instructs the case agent to attach the Judgment and Commitment Order to certain forms and memorandums sent to the civil functions for monitoring terms and conditions of probation. Criminal Investigation will take steps to reinforce these existing procedures.

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For recommendation two, CI agrees with the training of its first line managers, but disagrees with establishing a periodic systemic report requirement for monitoring terms and conditions of probation. We object because two periodic systemic reports already exist within the Criminal Investigation Management Information System (CIMIS) and CI's Measures for Managers (MOM) computer program application.

In CIMIS, the last page of standard Report Seven lists for the Special Agent in Charge (SAC) all investigations in their field office that have unexpired terms of probation. The SAC has the ability to review and disseminate this information to the first line managers where appropriate.

In MOM, there is a custom query that provides more extensive detailed investigation information, such as sentencing violation; months to serve; months of probation; fines to pay; conditions of probation expiration date and whether or not conditional terms of probation have been met. This information is directly available to the first line-manager for all investigations in CIMIS assigned to that specific work group that list terms and conditions of probation.

For recommendation four, both CI and SB/SE disagree with TIGTA's recommendation because procedures already exist within both divisions. The disclosure procedures and authorizations are currently referenced in Internal Revenue Manual (IRM) 11.3.22.18 (08/01/2003) Probation Proceedings. Subsection seven allows information concerning the taxpayer's filing status for years specified in the conditions of probation to be disclosed under Internal Revenue Code (IRC) 6103(h)(4). Subsection eight allows information about other tax years to be disclosed under IRC 6103(h)(4)(A) if the probation officer shows that the information is material in the court's consideration of revoking or extending probation. Both CI and SB/SE will reference these manual sources in any communication issued to the field offices on identifying, reporting and monitoring terms and conditions of probation.

For recommendation three, both CI and SB/SE agree with TIGTA. Criminal Investigation also agrees with **recommendations five** and **six**.

Other Comments

Criminal Investigation disagrees with TIGTA that the errors found in certain data fields (fines and criminal deficiency amounts) of CIMIS could affect CI's external or internal management reporting. Criminal Investigation does not report information from those data fields either internally or externally. Criminal Investigation has proposed steps to correct the CIMIS data field errors. These steps are listed in the corrective action section for recommendation five.

Additionally, CI disagrees with TIGTA's statement regarding measurable benefits on tax administration for the same reason – CI does not report information either internally or externally from the data fields where errors were found. Therefore, CI has serious concerns with the TIGTA report reference "as measured by \$6 billion identified as overstatements in the criminal deficiency..." It is almost certain that current and

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future readers of the report will not interpret this figure within its proper context. There is no correlation between this figure and “measurable benefits.”

In several locations in the draft report, TIGTA mentions that disclosure restrictions on tax and tax return information may have prevented a referral back to the courts on those individuals that did not comply with terms and conditions of their probation. It would be important for CI and SB/SE to know if this scenario actually occurred (and if so, on how many occasions and in what locations) or whether this is just an assumption.

There is no information in the draft report or the response that should be withheld from public disclosure.

Criminal Investigation’s and SB/SE’s comments on the specific recommendations in the report are as follows:

Recommendation #1

Establish procedures to ensure that, at the time of the case closing, court documents are obtained and verified to determine if the settlement of civil tax liabilities is a part of the sentence.

Corrective Action(s):

Not Applicable

Implementation Date:

Completed _____ N/A _____ Proposed _____ N/A _____

Responsible Official(s):

Not Applicable

Corrective Action(s) Monitoring Plan:

Not Applicable

Recommendation #2

Establish periodic systemic reports for first-line managers to use to identify and monitor those closed cases requiring the settlement of IRS tax liabilities, or provide formal training to first-line managers on the use of the MOM system.

Corrective Action(s):

Criminal Investigation will include a session in the scheduled Supervisory Special Agent (first-line manager) workshops to help first-line managers understand and effectively use MOM’s existing custom query and periodic systemic report to identify, report and monitor terms and conditions of probation on tax investigations.

Implementation Date:

Completed _____ N/A _____ Proposed _____ June 30, 2004

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Responsible Official(s):

Director, Office of Strategy

Corrective Action(s) Monitoring Plan:

Once the MOM training for managers has been completed, CI's Review and Program Evaluation (RPE) section will incorporate as part of their rotational peer review process an audit of the CIMIS information related to terms and conditions of probation. Implementation of the training on MOM is expected to increase field office compliance regarding the CIMIS' identification, reporting and monitoring on the terms and conditions of probation on tax investigations. The expected increase in CIMIS compliance will be exhibited through the RPE field office audit reports that are distributed to CI's Executive Management and Senior Staff.

Recommendation #3

Coordinate with SB/SE division management to develop clear and concise procedures to define responsibilities and ensure the IRS is controlling and monitoring the accounts of the individuals whose court sentences require the settlement of their civil tax liabilities. These procedures should address the tools needed for monitoring, as well as monitoring other types of conditional terms such as the filing of returns.

Corrective Action(s):

Criminal Investigation and SB/SE will review and revise as necessary their existing procedures and guidance on reporting and monitoring terms and conditions of probation on tax investigations. Criminal Investigation will coordinate its revisions with SB/SE to ensure that closed criminal tax investigations containing terms and conditions of probation are properly identified, reported and monitored.

Implementation Date:

Completed _____ N/A _____ Proposed ____ December 31, 2004

Responsible Official(s):

For CI - Director, Operations Policy and Support

For SB/SE – Director, Payment Compliance SB/SE Division

Corrective Action(s) Monitoring Plan:

Once the existing CI and SB/SE policies and procedures have been reviewed and additional guidance, if needed, has been distributed to CI and SB/SE field offices for implementation, CI's RPE section will incorporate as part of their rotational peer review process an audit of the CIMIS information related to terms and conditions of probation. Compliance in the field offices with the policy and guidance on terms and conditions of probation on tax investigations will be exhibited through the RPE field office audit reports that are distributed to CI's Senior Executives. For SB/SE, the Program Manager, Technical & Insolvency, will advise the Director, Payment Compliance, of any corrective action delays.

Recommendation #4

Seek the advice of the respective CI function and SB/SE Division Counsels, in concert with the Office of the Assistant Chief Counsel (Disclosure and Privacy Law), regarding

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disclosure of tax returns and tax return information to probation officers in determining noncompliance with conditional terms of probation or supervised release, and revise the appropriate IRM procedures accordingly.

Corrective Action(s):

Not Applicable

Implementation Date:

Completed _____ N/A _____ Proposed _____ N/A _____

Responsible Official(s):

Not Applicable

Corrective Action(s) Monitoring Plan:

Not Applicable

Recommendation #5

Develop a process to verify and validate the CIMIS data, as previously recommended.

Corrective Action(s):

Criminal Investigation's Research section will develop a process to identify questionable data field entries for those CIMIS data fields involved with reporting and monitoring terms and conditions of probation and that do not have internal validity checks. The Research section will periodically send a listing of identified questionable entries in the applicable conditional terms of probation data fields to the responsible field office(s) for verification and/or correction.

Implementation Date:

Completed _____ N/A _____ Proposed _____ September 30, 2004

Responsible Official(s):

Director, Office of Strategy

Corrective Action(s) Monitoring Plan:

Criminal Investigation's RPE section will incorporate as part of their rotational peer review process an expanded audit of the CIMIS information related to terms and conditions of probation. Compliance in the CI field offices with the proper CIMIS input on terms and conditions of probation on tax investigations will be exhibited through the RPE field office audit reports that are distributed to CI's Senior Executives.

Recommendation #6

Assess the clarity of guidance for coding some data fields and revise as recommended by the IRS' Offices of Program Evaluation and Risk Analysis (OPERA) and Office of Statistics of Income.

Corrective Action(s):

First, CI will review its existing policy and guidance procedures and CIMIS input instructions on identifying, reporting and monitoring terms and conditions of probation.

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Next, CI will revise existing policy and guidance documents as needed. Lastly, CI will issue as needed any clarifying communication to its field offices.

Secondly, the pending upgrade of CIMIS will require a wholesale change of the existing CIMIS manual that details the input information and criteria for each data field identifying, reporting and monitoring terms and conditions of probation on tax investigations.

Implementation Date:

Completed _____ N/A _____ Proposed ____ September 30, 2004 (Part One)

Completed _____ N/A _____ Proposed ____ March 1, 2005 (Part Two)

Responsible Official(s):

Director, Operations Policy and Support for Part One
Director, Office of Strategy for Part Two

Corrective Action(s) Monitoring Plan:

Criminal Investigation's RPE section will incorporate as part of their rotational peer review process an expanded audit of the CIMIS input information on terms and conditions of probation as well as the field offices' compliance with identifying, reporting and monitoring terms and conditions of probation. Compliance in the CI field offices will be exhibited through the RPE field office audit reports that are distributed to CI's Senior Executives.

If you have any questions, please call me on (202) 622-3200 or a member of your staff may contact José I. Marrero, Deputy Director, Strategy, (202) 622-5876.