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**Criminal Investigation's Use of Confidential
Funds for Undercover Operations Is
Appropriate; However, Certain Aspects of
Undercover Operations Need Improvement**

September 2002

Reference Number: 2002-10-196

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

September 24, 2002

MEMORANDUM FOR ACTING CHIEF, CRIMINAL INVESTIGATION

FROM: Pamela J. Gardiner
Acting Inspector General

SUBJECT: Final Audit Report - Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement (Audit # 200110029)

This report presents the results of our review to evaluate the appropriateness of confidential expenditures relating to selected Criminal Investigation (CI) undercover operations.

In summary, we found that CI's use of the approximately \$4 million in confidential expenditures in the 12 undercover operations we reviewed was appropriate. However, we identified numerous instances where the identities of undercover agents, confidential informants, or undercover entities were in jeopardy of being breached. CI management also needs to focus more attention on some categories of expenses because these expenses were unauthorized, unsupported, or unrelated to ongoing investigations. Additionally, we determined that CI management did not always effectively perform the necessary checks to ensure that informants were in compliance with federal tax laws and did not always properly document payments to informants.

We recommended CI management ensure that potential security breaches of undercover identities are minimized, provide closer scrutiny of certain higher-risk expenses, reemphasize existing procedures over payments to confidential informants, and emphasize adherence to administrative reviews and record keeping.

Management's Response: CI management agreed with our findings and recommendations. Specifically, CI agreed that the safety and security of undercover operations must be protected at the highest standard. In addition, CI agreed that

expenditures related to the undercover operations require close scrutiny, and administrative reviews of undercover operations must be conducted timely. In a continuing effort to improve the undercover program, CI implemented policy changes and increased oversight of undercover operations during the course of our review and agrees to make additional changes and improvements where necessary to address the remainder of our concerns. Management's complete response to the draft report is included as Appendix V.

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.

Criminal Investigation’s Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

Background

The Criminal Investigation (CI) function is responsible for investigating potential criminal violations of the federal internal revenue laws and related financial crimes. One of the investigative techniques used by CI to facilitate the completion of an investigation is an undercover operation. This involves an operative of the Internal Revenue Service (IRS), either an undercover agent or a confidential informant, assuming a covert identity to gain evidence or information which would not be available but for the reliance of the target of the investigation on the operative's covert role.

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[REDACTED]

There are certain risks associated with the use of confidential funds. These risks can include compromising the undercover nature of an operation through lax financial management and misuse of funds such as incurring expenses that:

- Do not directly contribute to the completion of an undercover operation.
- Were not approved for an undercover operation.
- Were not related to an undercover operation.

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[REDACTED]

The CI function closed 227 Group I and Group II undercover operations during the period January 1, 1999 to May 1, 2001. As of May 2001, there were 63 Group I and Group II open undercover operations.

We selected 12 undercover operations (5 closed and 7 open) at 7 field offices based on the level of funding and related risks. While audit work included reviewing most

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[REDACTED]

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undercover operations over the life of the project, storefront operations were reviewed for the 3-year period prior to the closing date or the date of our review. Audit work was conducted in the Office of the Chief, CI, and the Atlanta, Chicago, Dallas, New York, Plantation (FL), San Diego, and Seattle field offices. The audit was conducted between May 2001 and April 2002, using CI criteria in effect at the beginning of our review. With the exception of the scope impairment described below, the audit was conducted in accordance with *Government Auditing Standards*.

We were initially denied access by CI management to information related to the selected undercover operations, which delayed the audit for almost 5 months. CI expressed concerns about access to any open undercover operation and to operations that contained grand jury information. We worked with CI and Counsels for both the IRS and the Treasury Inspector General for Tax Administration (TIGTA) to gain access. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

In general, CI's use of the approximately \$4 million in confidential expenditures in the 12 undercover operations we reviewed was appropriate, and CI management has recognized the need to improve certain aspects of these operations. To further this improvement, CI management should ensure that potential security breaches of undercover and confidential informant identities are minimized, provide closer scrutiny of certain higher-risk expenses, reemphasize existing procedures over payments to confidential informants, and emphasize adherence to administrative reviews and record keeping.

During our review, we identified numerous instances where the identities of undercover agents, confidential informants, or undercover entities were in jeopardy of being breached.



Lax Execution Could Have Jeopardized the Identity of Undercover Operations

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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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• [Redacted]

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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

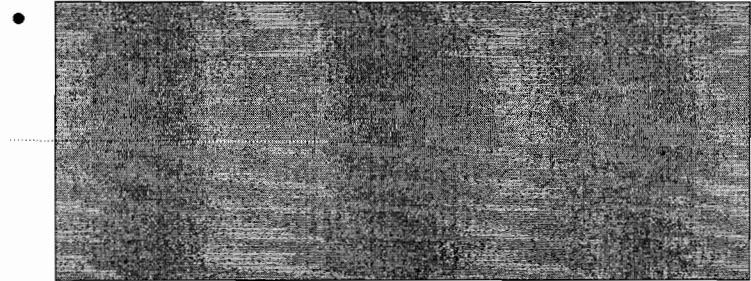
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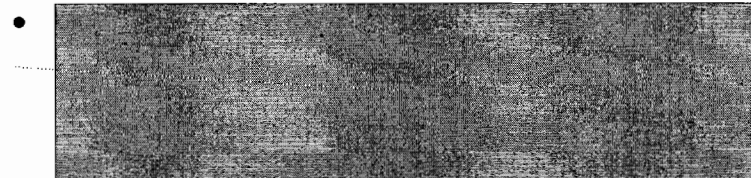
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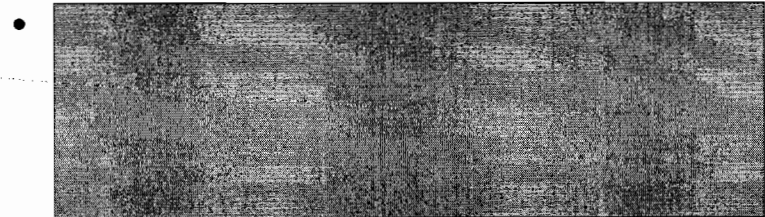
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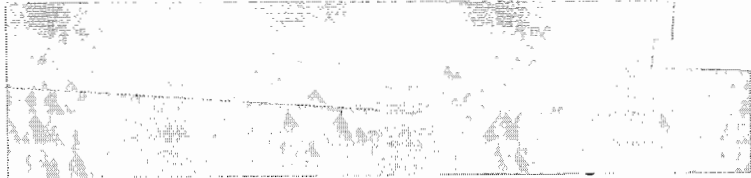
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When security over undercover operations is not maintained at the highest possible level, the risk of detection is increased and identities can be compromised.

Technology features, such as telephone caller identification, displays of numbers dialed, and last call dialed -- features which are commonly available to the public -- increase the

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need for vigilance in maintaining heightened security while agents serve in an undercover capacity.

We recognize that there may be financial or operational circumstances that necessitate undercover activities be conducted a certain way. Also, we are not aware of any actual security breaches resulting from the examples listed above. However, CI management advised that there have been instances in the past where the very nature of the operation was risky, or identities were compromised, and agents were put in harm's way. For example, during 1 undercover operation, an undercover agent was kidnapped and a confidential informant disappeared with \$80,000 in government funds. In another undercover operation, an estimated \$50,000 has not been recovered because the targets were able to place the funds outside of government reach before CI could secure them.

Recommendations

1. CI management should increase awareness about security issues and potential identity breaches to its agents assigned in undercover capacities.

Management's Response: CI will conduct training and emphasize security issues. [REDACTED]

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[REDACTED] will be stressed during an upcoming Continuing Professional Education conference scheduled for October 2002. In addition, the Special Investigative Techniques (SIT) Section [REDACTED]

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2. CI management should develop a methodology for determining when IRS employees access tax identifying numbers that are associated with undercover identities and entities. The ability to identify when accesses occur would provide a means for alerting CI to the possibility of IRS employees compromising an undercover operation.

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Management's Response: CI will seek authorization from the responsible IRS function to monitor undercover IDRS accounts.

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[Redacted]

[Redacted]

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When properly authorized, approved, and documented, these types of expenses are relatively low risk for waste and mismanagement.

However, we did identify some categories of expenses where management should focus more attention.

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[Redacted]

We determined that approximately \$44,000 of \$975,000 (5 percent) reviewed in these areas were either unauthorized, unsupported, or unrelated to ongoing investigations.

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[Redacted]

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We identified approximately \$24,000 in [Redacted]

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[Redacted] For example:

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- [Redacted] Police.

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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

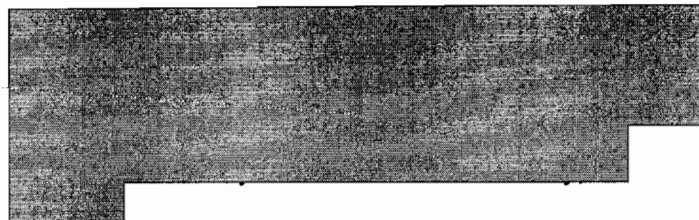
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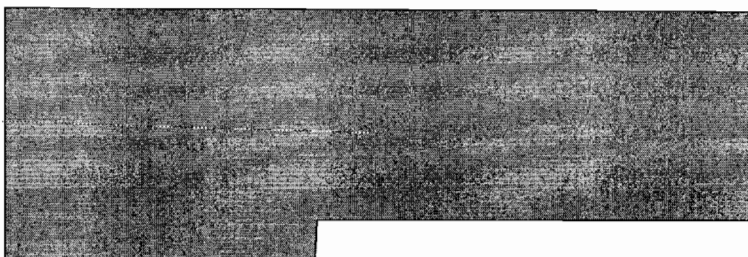
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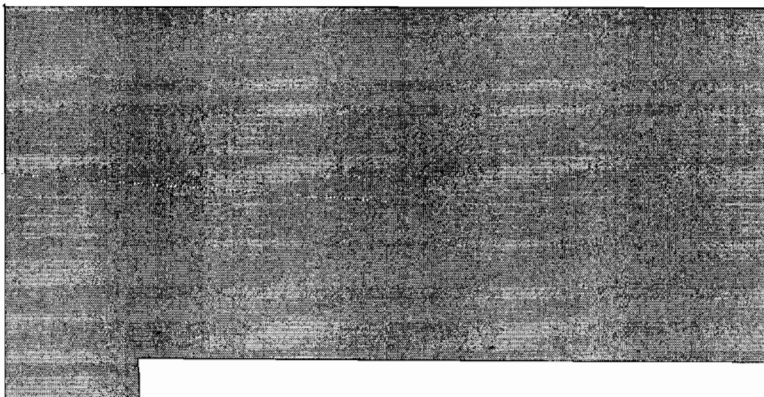
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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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We identified almost \$5,000 in

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Capital equipment

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We identified an expense for nearly \$3,000

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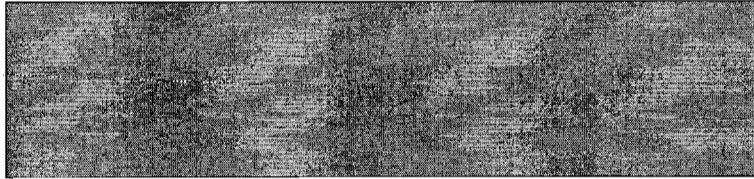
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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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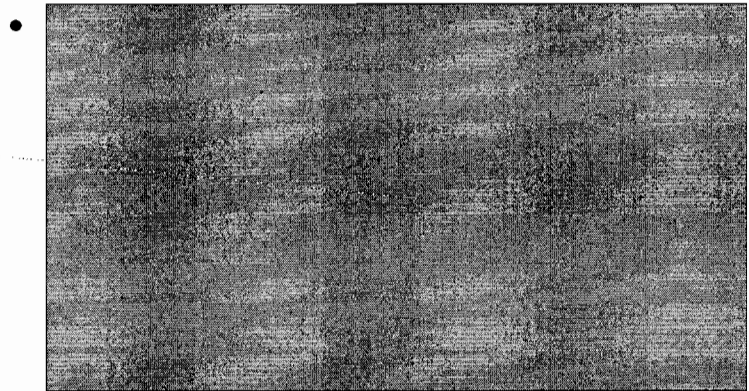


Miscellaneous

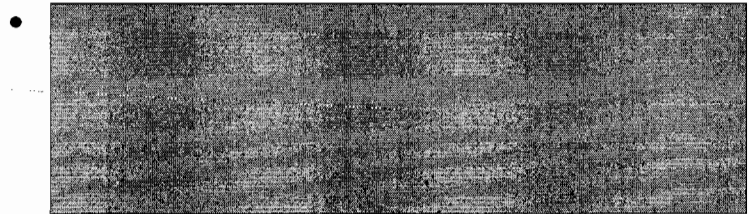
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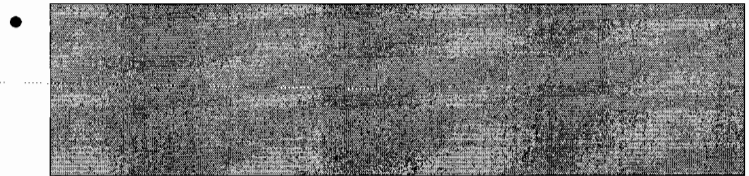
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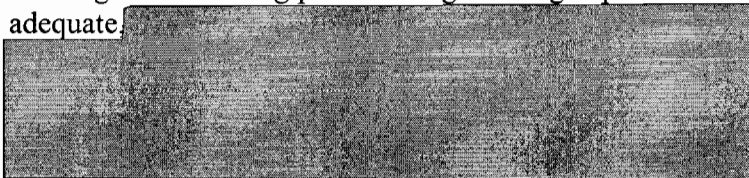


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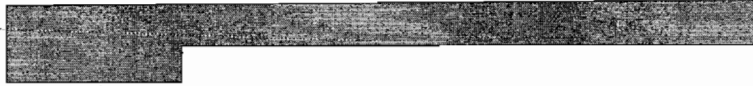
Although CI's existing procedures governing expenses are adequate,

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Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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Recommendations

3. CI management should provide more emphasis on reviewing certain categories of expenses to determine appropriateness. In particular, expenses should be reviewed for proper authorization and documentation and to ensure they were incurred for the advancement of the undercover operation.

Management's Response: CI has outlined guidelines governing the documentation necessary to obtain, review, and approve confidential expenditures in the SIT Reference Guide issued in June 2002 and posted on the SIT website. In addition, the Reference Guide will be disseminated to all SACs and Assistant SACs at the annual conference scheduled for October 2002.

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CI should also consider providing additional guidance to ensure that capital equipment dollar thresholds are established and consistently applied.

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Management's Response: CI established [redacted] Procedures and disseminated them on April 11, 2002. All [redacted] associated with undercover operations must comply with the new procedures. The SIT Section will reemphasize the procedures at the annual conference scheduled for October 2002.

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Controls Over Payments to Confidential Informants Can Be Strengthened

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We identified CI's use of 11 confidential informants associated with the [REDACTED] selected for review. At our request, CI obtained 18 tax returns covering a range of 1 to 4 years for these informants, depending on the time frame of the payments. In addition, we reviewed documentation associated with the payments to the confidential informants. We determined that CI management did not always perform effective checks to ensure that informants were in compliance with federal tax laws and did not always properly document payments to informants.

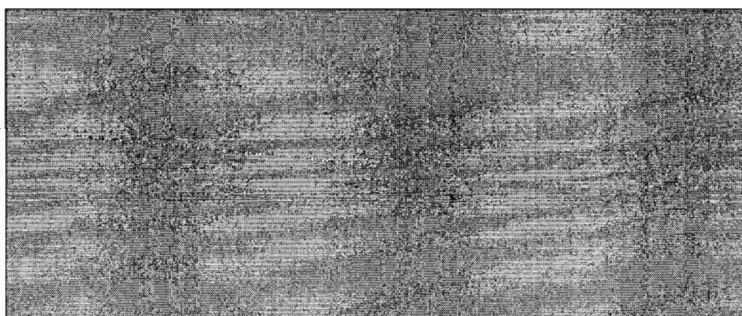
Tax compliance checks can be strengthened

CI management is required to advise confidential informants that payments for information are taxable and should be reported on their tax returns. CI fulfills this requirement during a February review for the previous year's payments.

In addition, CI is required to prepare a report certifying that it verified the informant filed a tax return and reported all payments received from CI during the previous year. CI fulfills this requirement during a December review for the same payments that were reflected in the February review. When an informant does not report all payments, CI should attempt to further advise the informant that the payments received were taxable. When the informant does not comply, CI should prepare an information item to be evaluated for civil or criminal action. CI should not use the confidential informant again.

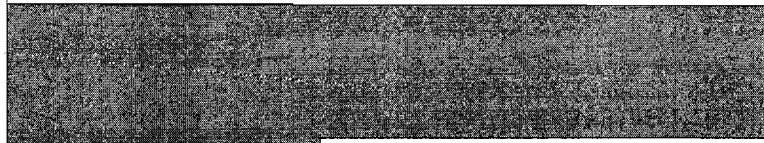
Non-Filers

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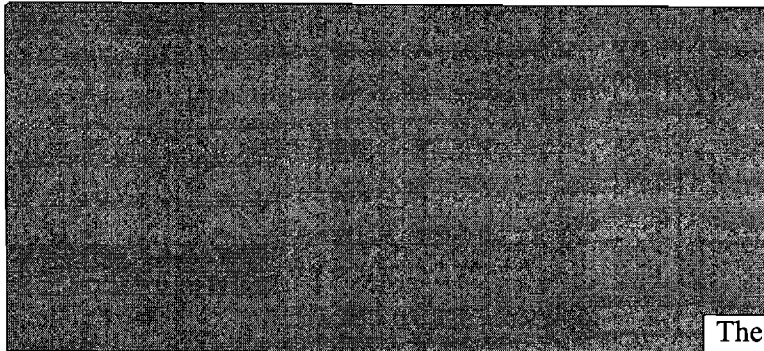
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The potential tax effect on these non-filers could be as high as \$6,161 or more, depending on the taxpayer's filing status, other income or deductions, and other return characteristics. See Appendix IV for further details.

Proper returns

(b)(3):26 U.S.C. 6103



The potential tax effect on these taxpayers could be as high as \$32,551 or more, depending on the taxpayer's filing status, other income or deductions, and other return characteristics. See Appendix IV for further details.

CI's required reviews and checks would not always be effective to identify these instances of potential non-compliance with the tax laws by confidential informants. Based on discussions with CI, the same form was being used to capture information for both the February and December reviews, which caused some confusion among field offices as to what the requirements were for the two periodic reviews. While information was captured for the February reviews reflecting information for the previous calendar year's payments, the December review was capturing information for the current year's payments rather than for the same previous year's payments that were reflected in the February review.

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When the reviews are not timely or effectively fulfilled, CI is at risk of continuing to make payments to confidential informants who are not in compliance with previous year's tax obligations, which could bring discredit to the use of these informants and the value of the information they provided. CI agreed with this concern and has already begun to take actions that should improve the existing process.

Informant payments can be strengthened administratively

In general, the approximately 400 payments to confidential informants, totaling over \$500,000, were adequately supported by required receipts. However, some payments were not always made by the special agent in the presence of a witness, as required. We determined that 4 of 11 informants received 16 payments totaling \$12,350 without the required 2 signatures.

Although CI's existing procedures governing payments to informants are adequate, agents and managers did not always follow them. When making payments to informants, a receipt is required to be obtained from the informant which is to include both agents' names and the informant's code or designation number. Without the presence of a witness, the risk is increased that unauthorized or inappropriate payments could be made.

Recommendations

5. CI management should reemphasize existing procedures for ensuring tax compliance of confidential informants who receive payments from CI for information and aggressively pursue instances of non-compliance. Management should consider accelerating the requirement for checking compliance from December to August to more closely coincide with filing due dates, thus providing a means for limiting the amount of payments to non-compliant informants.

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

Management's Response: CI has implemented new procedures for establishing informants and controlling informant payments. With these guidelines, CI established a new centralized national informant database at Headquarters. In addition, CI updated manuals and revised forms to accelerate the requirement for checking compliance from December to August. CI will also update manuals to ensure that reviews are performed of an informant's entire filing picture in any year in which he or she receives a payment.

6. CI management should also reemphasize existing procedures regarding payments to confidential informants, including the requirement for two signatures.

Management's Response: CI has outlined new guidelines on informant procedures and controlling informant payments in the SIT Reference Guide issued in June 2002 and posted on the SIT website. In addition, the Reference Guide will be disseminated to all SACs and Assistant SACs at the annual conference scheduled for October 2002. CI will use operational reviews to ensure the appropriate authorization and documentation of expenditures.

Undercover Operations Can Be Strengthened Administratively

CI management timely approved requests for undercover operations, extensions of time, deviations to plans, and additional funds. Pre-operational meetings were conducted and documented as required by written procedures. Closing reports were prepared and issued in accordance with the procedures. However, we did identify some administrative issues warranting management's attention.

Operational and financial reviews

Operational and financial reviews were not always performed as frequently as required. Operational reviews are intended to provide an overview of all ongoing undercover operations and create an awareness of all undercover activities within CI. Eight of the 12 undercover operations in our sample were to have operational reviews

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done every 90 days in accordance with procedures. The other 4 operations were mandated to have these reviews done every 60 days.

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[REDACTED]

Eleven of the 12 undercover operations in our sample were to have

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[REDACTED]

The other operation was mandated to have the reviews done every 45 days.

We determined that CI did not conduct 44 of the required 133 operational reviews (33 percent) and 39 of the required 132 financial reviews (30 percent) when required, even though CI has sufficient procedures to guide the timing and extent of these reviews. In many instances, CI covered the entire period of the project when reviews were done but did not conduct the reviews as frequently as required. We could not determine why reviews were not performed.

While CI management identified some similar issues in their operational and financial reviews, conducting all reviews when required will provide greater assurance that problems or concerns, such as those detailed in our report, are timely addressed.

Storefront logs

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[REDACTED]

We reviewed storefront logs for five of the undercover operations.

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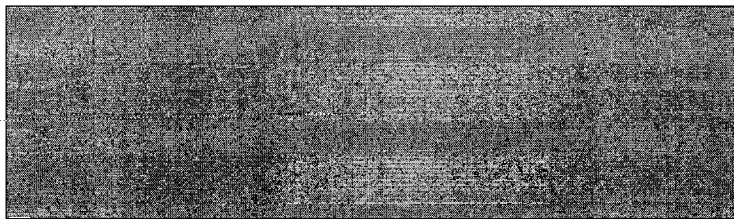
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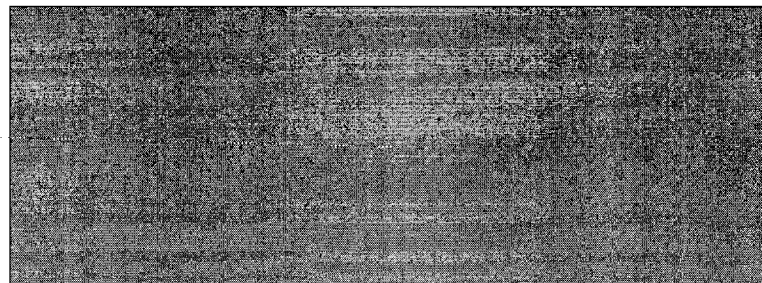
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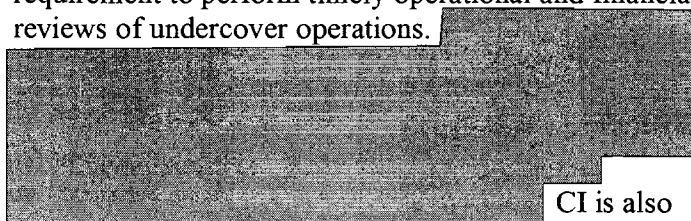
Storefront logs should enhance security and assist in demonstrating the cost benefit of the storefront. In addition, summaries from the storefront logs are to be included as the basis for continued funding of the storefront operations. When the storefront logs are not complete and consistent, information may not be available for CI management to make informed financial and investigative decisions.

Recommendation

7. CI management should reemphasize the procedures to ensure that operational and financial reviews are timely performed as required and prescribe the level of detail to be recorded in storefront logs to enhance the usefulness of this document as a monitoring and evaluative tool.

Management's Response: The Director, SIT Section, has implemented new procedures emphasizing the requirement to perform timely operational and financial reviews of undercover operations.

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CI is also

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implementing changes to the Internal Revenue Manual and Law Enforcement Manual to standardize storefront logs and storefront oversight.

Detailed Objective, Scope, and Methodology

Our audit objective was to evaluate the appropriateness of confidential expenditures relating to selected Criminal Investigation (CI) undercover operations. To accomplish this objective, we:

- I. Identified the total number of open undercover operations and the number closed since January 1, 1999, and selected a sample of these operations with related confidential expenditures. We:
 - A. Obtained listings of the 227 undercover operations that were closed between January 1, 1999, and May 1, 2001, and the 63 operations that were open at the time of our review. CI management provided these listings to us, and we did not independently validate their accuracy.
 - B. Selected a judgmental sample of 12 undercover operations based on the level of confidential expenditures or approved confidential funding and the risks associated with the expenditures. We used judgmental sampling as we did not plan on projecting our results to the universe of all undercover operations.
 - C. Reviewed confidential expenditures for each of the 12 undercover operations for the period reviewed.
- II. Reviewed the approvals, issues identified by CI reviews, and actual confidential expenditures for the selected 12 undercover operations. We also interviewed CI personnel and reviewed the following documentation:
 - A. Requests for Undercover Operation (Form 8354) and attached narratives.
 - B. Pre-Operational meeting memoranda (10 of 12 available).
 - C. Results of Undercover Program Managers reviews.
 - D. Results of financial reviews.
 - E. Undercover Operation Closing Reports (closed operations only; 8 of 9 available).¹
- III. Evaluated the appropriateness of the specific confidential expenditures by interviewing CI personnel and reviewing the following documentation:

¹ Four investigations with undercover operations were open at the time of our review, but the undercover operations associated with these investigations were closed. CI had completed three of the four closing reports at the time of our review; the fourth closing report was in draft status.

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- A. Daily Expense Sheets prepared by the undercover agents.
 - B. Daily Memoranda of Activity prepared by the undercover agents.
 - C. Leases signed by the undercover agents.
 - D. Monthly Summaries of Expenses prepared by the cover agents.
 - E. Monthly Balance Sheets (Form 8563) prepared by the cover agents.
 - F. Claims for Reimbursement for Expenditures on Official Business (Standard Form 1164) prepared by the cover agents.
 - G. Original receipts for the confidential expenditures.
 - H. Records supporting the purchase of assets.
 - I. Storefront logs.
 - J. Results of undercover operations including arrests, indictments, convictions, forfeitures, seizures, and additional assessments of taxes, interest, and penalties documented in the closing reports (if operation was closed).
- IV. Evaluated the appropriateness of informant expenditures by reviewing the following additional documentation where available:
- A. Document approving the use of the informant.
 - B. Approved Confidential Informant -- Monthly Log (Form 9834).
 - C. Memoranda of Contact (Form 9833).
 - D. Receipt of Cash (Form 9832).
 - E. Special Agent in Charge reviews of the use of the informants.
 - F. Special Investigative Techniques Section reviews of record keeping for informant payments.
 - G. Source documents that confirm the informant exists.
 - H. Information related to ensuring tax compliance.

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Appendix II

Major Contributors to This Report

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Appropriate; However, Certain Aspects of Undercover Operations Need Improvement**

Appendix III

Report Distribution List

Commissioner N:C
Deputy Commissioner N:DC
Deputy Chief Financial Officer, Department of the Treasury
Director, Operations Policy and Support CI:OPS
Director, Special Investigative Techniques CI:OPS:SIT
Director, Field Operations CI:FO:C
Director, Field Operations CI:FO:MS
Director, Field Operations CI:FO:NA
Director, Field Operations CI:FO:P
Director, Field Operations CI:FO:SE

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Increased Revenue – Potential; \$38,712 individual income tax (see page 11).

Methodology Used to Measure the Reported Benefit:

For all taxpayers, we used a filing status of single and the standard deduction, with one exemption. [REDACTED]

(b)(3):26 U.S.C. 6103	<u>Taxpayer</u>	<u>Year</u>	<u>Adjusted Gross Income</u>	<u>Taxable Income</u>	<u>Tax</u>	<u>Tax As Reported</u>	<u>Tax Effect</u>
	<u>Non-Filers</u>						
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Total						\$ <u>6,161</u>
	<u>Proper Returns</u>						
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
(b)(3):26 U.S.C. 6103	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	Total						\$ <u>32,551</u>

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

Appendix V

Management's Response to the Draft Report



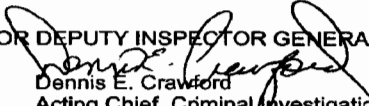
Criminal Investigation

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

RECEIVED
SEP 17 2002

SEP 17 2002

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: 
Dennis E. Crawford
Acting Chief, Criminal Investigation CI

SUBJECT: Response To Draft Audit Report—Criminal Investigation's Use of Confidential Funds for Undercover Operations is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement
(Audit # 200110029) ECMS IR No. 0209-5DXM9RYC

I reviewed your draft audit report on Criminal Investigation's (CI) undercover program. Your report summarizes the audit results of twelve (12) of CI's Group I undercover operations. It also summarizes the audit results of payments to eleven (11) confidential informants associated with the undercover operations selected for review. Undercover operations are critical to the success of CI's mission. We take your findings and recommendations seriously and will use them to improve our undercover program.

I agree we must protect the safety and security of all undercover operations at the highest standard. I also agree that expenditures related to undercover operations require close scrutiny, that we must consistently perform informant tax compliance checks, and that we must conduct administrative reviews of undercover operations in a timely manner. In our continuing effort to improve the undercover program, CI implemented many policy changes and increased its oversight of undercover operations. Some of these changes relate to issues raised in your audit, which we had initiated prior to your report. In addition, this response discusses additional changes that we plan to make to address the remainder of your concerns.

Lax Execution Could Have Jeopardized the Identity of Undercover Operations

I agree that the incidents listed in your audit report identify potential breaches of security. However, these instances do not indicate a systemic problem. In fact, our internal review process identified a number of these security issues prior to your audit. For instance, page four of your report highlights an incident where a non-CI IRS employee

(b)(3):26 U.S.C. 6103

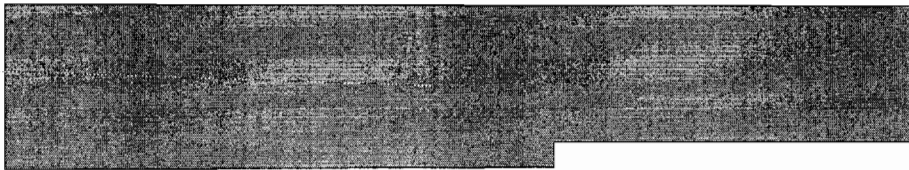
Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

(b)(3):26 U.S.C. 6103



To further enhance security awareness, we will incorporate the issues raised in your report in the Continuing Professional Education conference for undercover agents, scheduled for the week of October 28, 2002. In addition, the Special Investigative Techniques (SIT) Section will continue to conduct operational reviews to identify and correct any potential security breaches.

(b)(2),(b)(7)(E)



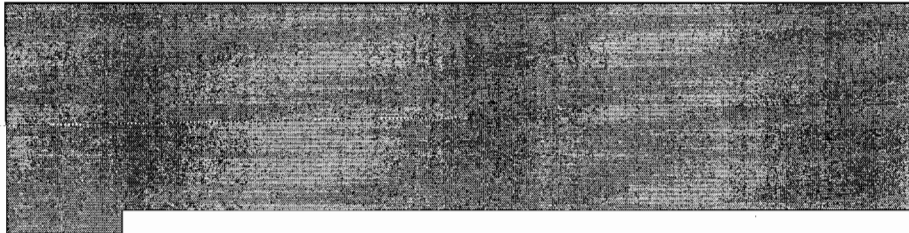
I must clarify the information in your report about the kidnapping of an undercover agent and the loss of recoverable funds. Specifically, the report implies that the undercover agent's disclosure of "covert identifying information" caused the kidnapping. In fact, the undercover agent never disclosed his or her covert identity. Instead, the kidnapping occurred because the kidnapers, who were unrelated to the undercover operation, believed the undercover agent was wealthy, and therefore a desirable target for kidnapping and ransom. After this incident, CI enhanced the training course for contact/cover agents. This training, which we implemented in February 2001, reemphasizes the risks involved in this activity and provides advice on the prevention of similar incidents in the future.

(b)(2),(b)(7)(E)



The confidential informant that absconded with the \$80,000 in recoverable funds established a history of reliable work with CI. The confidential informant acted voluntarily and his conduct was not related to any close relationship with the special agent or any compromise of covert identity.

(b)(2),(b)(7)(E)



Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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Certain Categories of Expenses Require Closer Scrutiny

(b)(2),(b)(7)(E)

[REDACTED] Criminal Investigation agrees that agents must have proper authorization and documentation for all undercover operations expenditures. [REDACTED]

(b)(2),(b)(7)(E)

[REDACTED] during the Continual Professional Education conference scheduled for the week of October 28, 2002. In addition, we outlined the guidelines governing the documentation necessary to obtain, review and approve confidential expenditures in the Special Investigative Techniques Reference Guide we issued in June 2002. The SIT Section will continue to conduct operational reviews to identify and address any potential expenditure issues.

With regard to Recommendation four of your report, on April 11, 2002, we established new standardized thresholds for capital equipment and distributed these guidelines to the field offices. We will provide additional guidance to undercover agents, cover agents and management officials to ensure compliance with these new procedures.

Controls Over Payments to Confidential Informants Can Be Strengthened

I agree we must strengthen CI's controls over payments to confidential informants. Criminal Investigation already initiated new procedures to improve control over establishing confidential informants and recording payments to informants. We established a new centralized national database for all CI confidential informants in Headquarters. In addition, we updated manuals, revised forms, and implemented the new procedures. These policy changes enhanced CI's control of payments to confidential informants as suggested in Recommendations five and six of your report. While we agree that prior implementation of these procedures may have had a measurable benefit on tax administration, we believe that, barring an audit of the tax returns, the variables involved make it impossible to quantify the amount of revenue that may have resulted (Appendix IV).

Undercover Operations Can Be Strengthened Administratively

I agree we should conduct operational reviews and financial reviews on a timely basis. The Director, Special Investigative Techniques Section already issued a communication to the Headquarters Analysts and Undercover Program Managers to ensure timely operational reviews and appropriate documentation in those instances where no review is warranted.

Our comments on the specific recommendations in this report are as follows:

IDENTITY OF RECOMMENDATION #1

Criminal Investigation management should increase awareness about security issues and potential identity breaches to its agents assigned in undercover capacities.

ASSESSMENT OF CAUSE(S)

We found no systemic cause.

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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CORRECTIVE ACTION(S)

(b)(2),(b)(7)(E)

Criminal Investigation will continue to conduct training and emphasize security issues and potential identity breaches. [REDACTED] during the Continual Professional Education conference scheduled for October 2002. In addition, the Special Investigative Techniques Section [REDACTED]

(b)(2),(b)(7)(E)

IMPLEMENTATION DATE

January 1, 2003

RESPONSIBLE OFFICIAL(S)

Director, SIT

(b)(2),(b)(7)(E)

CORRECTIVE ACTION(S) MONITORING PLAN

Special Investigative Techniques will use operational reviews to [REDACTED]

(b)(2),(b)(7)(E)

IDENTITY OF RECOMMENDATION #2

Criminal Investigation management should develop a methodology for determining when IRS employees access tax identifying numbers that are associated with undercover identities and entities. The ability to identify when accesses occur would provide a means for alerting CI to the possibility of IRS employees compromising an undercover operation.

ASSESSMENT OF CAUSE(S)

Criminal Investigation does not have the appropriate authorizations to access and review IDRS accounts for undercover agents and entities.

CORRECTIVE ACTION(S)

Criminal Investigation will continue to seek authorization from the responsible IRS function to monitor undercover IDRS accounts.

IMPLEMENTATION DATE

January 1, 2004

RESPONSIBLE OFFICIAL(S)

Director, Operations Policy and Support
Director, SIT

CORRECTIVE ACTION(S) MONITORING PLAN

Not Applicable.

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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IDENTITY OF RECOMMENDATION #3

Criminal Investigation management should provide more emphasis on reviewing certain categories of expenses to determine appropriateness. In particular, expenses should be reviewed for proper authorization and documentation, and to ensure they were incurred for the advancement of the undercover operation.

ASSESSMENT OF CAUSE(S)

Criminal Investigation management at the field office level may not be fully aware of their responsibilities when reviewing and approving confidential expenditures associated with undercover operations.

CORRECTIVE ACTION(S)

Criminal Investigation already provided additional guidance to management officials on the review and approval of confidential expenditures associated with undercover operations. We have outlined the guidelines governing the documentation necessary to obtain, review and approve confidential expenditures in the Special Investigative Techniques Reference Guide issued in June 2002 and posted on the Special Investigative Techniques web-site. In addition, the reference guide will be disseminated to all Special Agents in Charge (SAC) and Assistant Special Agents in Charge (ASAC) at the annual SAC/ASAC conference scheduled for October 2002. Criminal Investigation will also continue to [REDACTED]

(b)(2),(b)(7)(E)

(b)(2),(b)(7)(E)

IMPLEMENTATION DATE

January 1, 2003

RESPONSIBLE OFFICIAL(S)

Director, SIT

CORRECTIVE ACTION(S) MONITORING PLAN

Special Investigative Techniques will use operational reviews to monitor expenses for proper authorization and documentation.

(b)(2),(b)(7)(E)

IDENTITY OF RECOMMENDATION #4

(b)(2),(b)(7)(E)

[REDACTED] Criminal Investigation should also consider providing additional guidance to ensure that capital equipment dollar thresholds are established and consistently applied.

ASSESSMENT OF CAUSE(S)

The lack of a standardized definition and/or dollar amount limit caused confusion over what capital equipment purchases managers should include on capital assets inventories maintained by the field offices.

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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CORRECTIVE ACTION(S)

We established Criminal Investigation Property Management Procedures and disseminated them on April 11, 2002. All equipment purchases associated with undercover operations must comply with these procedures. Special Investigative Techniques will reemphasize the procedures at the annual SAC/ASAC conference scheduled for October 2002.

IMPLEMENTATION DATE

January 1, 2003

RESPONSIBLE OFFICIAL(S)

Director, SIT

CORRECTIVE ACTION(S) MONITORING PLAN

Not Applicable.

IDENTITY OF RECOMMENDATION #5

Criminal Investigation management should reemphasize existing procedures for ensuring tax compliance of confidential informants who receive payments from CI for information, and aggressively pursue instances of non-compliance. Management should consider accelerating the requirement for checking compliance from December to August to more closely coincide with filing due dates, thus providing a means for limiting the amount of payments to non-compliant informants.

ASSESSMENT OF CAUSE(S)

The decentralized nature of informant records may have caused confusion about the proper documentation of payments to informants and related tax compliance checks.

CORRECTIVE ACTION(S)

Criminal Investigation implemented new guidelines for establishing informants and controlling informant payments. With these guidelines, we established a new centralized national informant database at Headquarters. In addition, we updated manuals and revised forms to accelerate the requirement for checking compliance from December to August. We will also update manuals to ensure that we review an informant's entire filing picture in any year in which he or she receives a payment.

IMPLEMENTATION DATE

October 1, 2003

RESPONSIBLE OFFICIAL(S)

Director, SIT

CORRECTIVE ACTION(S) MONITORING PLAN

Special Investigative Techniques will use the national informant database and operational reviews to monitor non-compliant confidential informants.

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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IDENTITY OF RECOMMENDATION #6

Criminal Investigation management should reemphasize existing procedures regarding payments to confidential informants, including the requirement for two signatures.

ASSESSMENT OF CAUSE(S)

The decentralized nature of informant records may have caused confusion about the proper documentation of payments to informants and related tax compliance checks.

CORRECTIVE ACTION(S)

Criminal Investigation recently implemented new guidelines on informant procedures and controlling informant payments. We outlined these procedures in the Special Investigative Techniques Reference Guide issued in June 2002 and posted on the Special Investigative Techniques web-site. In addition, we will distribute the reference guide to all Special Agents In Charge (SAC) and Assistant Special Agents In Charge (ASAC) at the annual SAC/ASAC conference scheduled for October of 2002. Criminal Investigation will also continue to utilize operational reviews to monitor informant records including payment procedures.

IMPLEMENTATION DATE

January 1, 2003

RESPONSIBLE OFFICIAL(S)

Director, SIT

CORRECTIVE ACTION(S) MONITORING PLAN

Special Investigative Techniques will use the national informant database and operational reviews to monitor the proper documentation of payments to informants

IDENTITY OF RECOMMENDATION #7

Criminal Investigation management should reemphasize the procedures to ensure that operational and financial reviews are performed timely, and prescribe the level of detail to be recorded in storefront logs to enhance the usefulness of this document as a monitoring and evaluative tool.

ASSESSMENT OF CAUSE(S)

(b)(2),(b)(7)(E)

[REDACTED] We believe a misunderstanding of the purpose of storefront logs, and the specific information need, may have led to inconsistencies of the information maintained.

(b)(2),(b)(7)(E)

CORRECTIVE ACTION(S)

The Director, SIT Section recently implemented new procedures emphasizing the requirement to perform timely operational and financial reviews of undercover operations.

(b)(2),(b)(7)(E)

(b)(2),(b)(7)(E)

Criminal Investigation's Use of Confidential Funds for Undercover Operations Is Appropriate; However, Certain Aspects of Undercover Operations Need Improvement

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(b)(2),(b)(7)(E)

[REDACTED]
Criminal Investigation is also implementing changes to the Internal Revenue Manual and Law Enforcement Manual to standardize storefront logs and storefront oversight.

IMPLEMENTATION DATE
October 1, 2003

RESPONSIBLE OFFICIAL(S)
Director, SIT

(b)(2),(b)(7)(E)

CORRECTIVE ACTION(S) MONITORING PLAN
Special Investigative Techniques will use [REDACTED]
[REDACTED]

(b)(2),(b)(7)(E)