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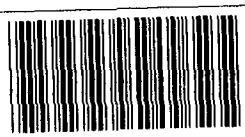

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STATEMENT OF

ELMER B. STAATS, COMPTROLLER GENERAL

OF THE UNITED STATES

BEFORE THE

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

SENATE COMMITTEE ON GOVERNMENTAL AFFAIRS

ON

THE INTERNAL REVENUE SERVICE'S EFFORTS TO COMBAT NARCOTICS TRAFFICKERS

Mr. Chairman and Members of the Subcommittee:

We are pleased to assist the Subcommittee in its inquiry into the drug trafficking problem. While our statement centers on the Internal Revenue Service's (IRS') role in the war against narcotics traffickers, that role must be discussed in the context of the overall drug problem and related Federal enforcement efforts to combat it.

In October 1979, we issued a comprehensive report to the Congress on the effectiveness of the Federal Government's drug enforcement and supply control efforts during the past 10 years. (Attachment I to my statement contains a copy of the digest of that report.) We concluded that Federal drug

supply reduction efforts have yet to achieve a well-integrated, balanced, and truly coordinated approach. Federal agencies have fought hard to reduce the adverse impact of illegal drugs on American society and some positive results have been achieved. However, the drug trade continues to flourish, and the problem persists for various reasons, including the enormous profits involved.

Incarcerating major traffickers for long periods and causing forfeiture of their financial resources are key elements to successfully reducing the drug problem. This requires close interaction and coordination among Federal law enforcement agencies, including the Drug Enforcement Administration (DEA) and IRS. However, legal obstacles, little overall direction, and changing priorities have prevented Federal agencies from fully using and coordinating their unique skills, jurisdictions, and resources. As a result, the Federal Government has had only limited success in immobilizing high-level traffickers and their organizations through conspiracy and financial investigations.

Knowledge of money flows along with other information is essential to identifying and immobilizing drug traffickers. However, investigations in the drug area have focused, for the most part, on the drugs themselves, rather than the financial transactions connected with the sale and movement of drugs. Special expertise is needed to perform financial investigations. DEA does not have extensive financial investigative

expertise although it has the legal authority to seize and cause forfeiture of traffickers' assets under various U.S. code sections (21 U.S.C. 881, 21 U.S.C. 848, and 18 U.S.C. 1963). IRS, on the other hand, has financial expertise and thus the capability to be an effective force in the war against narcotics traffickers.

But it is extremely important to emphasize that IRS must have a balanced enforcement program. The tax administration system is not essentially a criminal detection operation. About 135 million taxpayers voluntarily file tax returns every year. The most important objective of the system is to voluntarily raise about $500 billion a year in revenues. IRS has to be concerned about developing an enforcement system that ensures taxpayers' confidence in the objectivity of that system and provides proper privacy safeguards.

The remainder of our statement deals with the extent of IRS' involvement in combatting narcotics traffickers and the problems that have prevented it from assuming a more active role.

IRS HAS ACHIEVED ONLY LIMITED SUCCESS IN ITS EFFORTS TO COMBAT NARCOTICS TRAFFICKERS

IRS has not been very active in the drug area. Relatively few criminal investigations of drug traffickers have been initiated and most cases have not led to prosecution recommendations, let alone convictions.

IRS has two types of efforts to combat drug traffickers. It initiates some criminal and civil tax investigations as a result of leads provided by DEA and it self-initiates others. Neither effort has produced significant results; but IRS' independent efforts have produced better results.

In accordance with a 1976 IRS/DEA agreement, DEA provides IRS with names and background information on high-level drug traffickers referred to as DEA class I violators. Although IRS gives high priority to evaluating those leads for their criminal and civil tax potential, that process has produced few tangible results. Criminal tax cases are complex in nature and therefore usually take several years to investigate and prosecute. By the time IRS develops a tax case on a class I violator, the violator often has been incarcerated for drug-related offenses. In such instances, the Justice Department generally will not prosecute the tax charges.

During the 3 years ended June 30, 1979, DEA provided IRS with information on 868 class I violators. IRS' evaluation of 792 DEA-provided leads (76 were pending evaluation on June 30, 1979) resulted in 114 criminal investigations. Fifty other class I violators already were under criminal investigation by IRS when it received the DEA information. To date, however, only 11 class I violators have been convicted on criminal tax charges.

IRS determined that 205 DEA-provided leads merited no criminal or civil action. IRS' Examination and Collection Divisions evaluated information on a total of 423 violators. But overall statistics on the results of civil tax actions against class I violators were not readily available.

In IRS' Jacksonville district, 47 of 93 class I violators referred to IRS by DEA already had been arrested, indicted, convicted, sentenced, or incarcerated for non-tax crimes. Four of the 93 class I violators were placed under criminal investigation. Seven others already were under investigation by IRS. To date, only one class I violator has been convicted. Fifty-five of the 93 class I violators were referred by the Criminal Investigation Division to IRS' Examination and Collection Divisions for civil tax considerations. IRS could not readily provide information on the results of civil tax actions.

In the Los Angeles district, only 15 of the 96 DEA-provided leads led to criminal tax investigations and, to date, IRS has obtained no convictions. Twenty-five of the 96 leads were sent to the Examination Division for civil tax evaluations but only two have resulted in audits in which the subject was assessed additional taxes. IRS could provide us no information on 11 class I violators referred to the Collection Division in Los Angeles. The district did

not have overall statistics on the number of class I violators already indicted or convicted for non-tax offenses. However, information IRS had on 15 class I violators showed that 9, or 60 percent, were either awaiting trial or already had been jailed.

IRS-initiated efforts produce somewhat better, if not significant investigative results. Of 9,780 criminal tax investigations IRS initiated during fiscal year 1979, 279, or about 3 percent, involved narcotics traffickers. Similarly, since July 1976, 152, or about 3 percent, of all convictions on criminal tax charges were obtained on narcotics traffickers.

In June 1979, IRS' Assistant Commissioner for Compliance reported that IRS also had sought to deal with narcotics traffickers through civil tax actions. He reported that, during July 1, 1976, through March 31, 1979, IRS' Examination Division proposed deficiencies and penalties totaling $48.5 million through audits of traffickers' returns. The Assistant Commissioner did not, however, indicate how much money was actually collected.

WHY IRS' ROLE IN THE WAR AGAINST NARCOTICS TRAFFICKING HAS BEEN LIMITED

Although IRS has had some definite successes in the drug area, its impact on reducing the nation's drug trafficking problem has been limited. The President and members of Congress have stressed the need to use the tax laws and IRS' financial expertise in investigating major drug traf-

fickers. But numerous factors have inhibited IRS' ability to effectively combat drug trafficking.

--First, because IRS does not have a well-defined national strategy for its criminal investigative activities, it may not be giving adequate attention to the drug trafficking problem.

--Second, IRS' ability to cooperate and coordinate with other law enforcement agencies has been reduced by the disclosure provisions of the 1976 Tax Reform Act.

--Third, IRS' ability to quickly obtain financial records from third parties has been impaired by the summons provisions of the 1976 Tax Reform Act.

--Fourth, the Justice Department's dual prosecution policy provides little incentive for IRS to investigate drug-related tax cases.

--Fifth, IRS has limited its use of jeopardy and termination assessments as a means for getting at traffickers' assets.

--And finally, currency and foreign bank account reports required by the 1970 Bank Secrecy Act have not been used effectively to identify major traffickers.

Need for a national criminal enforcement strategy

Now I would like to expand on the first and most fundamental factor which handicaps IRS' efforts against

drug trafficking--IRS' lack of a national criminal enforcement strategy. In its August 1979 report on the subterranean economy, IRS estimated that, during tax year 1976, at least $35 billion in income from illegal sources was not reported for tax purposes, including about $24 billion from drug trafficking. While these figures are disturbing, they are probably understated.

Criminal investigations are the best means IRS has for dealing with the extensive amount of unreported income from illegal sources. Yet the complex and devious nature of schemes involving these activities limits IRS' ability to detect and deter related tax evasion. Routine audits and collection actions have little chance of detecting such schemes, which often involve no "paper trail."

On the other hand, special agents assigned to IRS' Criminal Investigation Division are specifically trained and authorized to (1) use sensitive investigative techniques, such as surveillances and controlled informants, (2) work with grand juries, strike force attorneys, and drug enforcement agents, (3) issue taxpayer and third-party summonses, and (4) otherwise gather and analyze information from sources outside IRS. Properly directed, special agents have the potential to identify much unreported income arising from illegal activities, including drug trafficking.

In November 1979, we reported that IRS had not effectively dealt with the tax fraud problem, let alone the narcotics

trafficking problem. (Attachment II to my statement contains a copy of the digest of that report.) We concluded that IRS has not developed a well-defined national strategy for its criminal investigation operations because national direction has been inadequate. The Criminal Investigation Division's long- and short-range plans are unsatisfactory and cannot be used to make resource allocation decisions. No systematic attempt is made to determine and establish priorities regarding the extent to which various criminal activities, such as narcotics trafficking, contribute to income tax noncompliance and, then, to allocate resources accordingly. Currently, IRS devotes 6 percent of its criminal investigative resources to the drug problem.

IRS faces a dilemma in determining the extent to which it should allocate its limited resources against narcotics traffickers, as opposed to other persons or groups not reporting income from other illegal or legal activities. Its reluctance to become increasingly involved in drug trafficking activities in recent years stems, in part, from the fact that it was criticized by various parties in the mid-1970s for being overzealous in efforts to investigate narcotics traffickers.

In our view, IRS can take some positive action to resolve the dilemma it faces, in making resource allocation decisions on narcotics traffickers, by implementing the recommendations contained in our November 1979 report. Effective implementation of these recommendations should enable IRS to develop better plans and allocate its resources more effectively.

Disclosure provisions of the 1976 Tax Reform Act hamper investigative activities

While the development of a national strategy would help IRS establish resource priorities, the Tax Reform Act of 1976 placed certain restrictions on IRS which limit its ability to effectively assist drug enforcement efforts.

The intent of the Congress, in amending section 6103 of the Internal Revenue Code, was to afford taxpayers increased privacy over information they provide IRS by placing substantial restrictions on other Government agencies' rights of access to tax information. In our March 1979 report on the effects of the disclosure provisions of the 1976 amendment, we pointed out that the provisions had afforded taxpayers increased privacy, but at the same time had adversely affected coordination between IRS and other law enforcement agencies, including DEA. (Attachment III to my statement contains a copy of the digest of that report.) Specifically:

--IRS cannot always disclose information about non-tax crimes.

--IRS cannot alert Justice attorneys to seek disclosure of criminal tax information.

--IRS apparently takes more time to respond to Justice requests for tax information.

--And, coordination between IRS and DEA had been slowed by the provisions' requirements.

In conducting their daily activities, IRS employees sometimes obtain information indicating that a taxpayer has committed a crime outside IRS' jurisdiction. If they obtain the information from a third party, they can disclose it to the head of the appropriate Federal agency, such as the Attorney General. However. if that information is obtained from a taxpayer, the taxpayer's records, or the taxpayer's representative, IRS cannot alert the Attorney General or other Federal agency heads of the crime, regardless of its seriousness.

A coordination problem also arises when IRS has criminal tax information on an individual which can be useful to a U.S. attorney or strike force attorney and the affected attorney does not know IRS has the information. The Tax Reform Act generally prohibits IRS from initiating discussions with Justice Department attorneys about a person's criminal tax affairs until IRS officially refers the case to Justice for prosecution. Here are some illustrations of the problem.

--A taxpayer under investigation by IRS was arrested by Customs agents for smuggling. The U.S. attorney could have considered indicting the individual on two counts--smuggling and tax fraud--if she knew in advance about IRS' investigations. But

IRS could not disclose the identity of its investigative target because it had not referred its case to Justice for prosecution.

--A corporation that had allegedly made illegal payments overseas was under investigation by the Securities and Exchange Commission. The involved U.S. attorney learned of an ongoing IRS fraud investigation of the same corporation when he was requested to enforce a summons issued by IRS. The attorney concluded that the two agencies had conducted parallel investigations thereby wasting resources through lack of coordination.

--In another instance, the strike force attorney in a major city meets with IRS officials monthly to discuss ongoing and planned efforts against organized crime. But IRS officials cannot discuss their individual cases with the strike force attorney. Prior to the Tax Reform Act, IRS could discuss individual cases with strike force attorneys and the attorneys could then provide guidance consistent with their role as Federal law enforcement coordinators. Under present law, a strike force attorney can suggest that IRS initiate a criminal tax investigation on a specific individual. If IRS

decides to conduct the investigation, however, it cannot so inform the strike force attorney.

Pursuant to the Tax Reform Act, Federal agency heads can request tax information needed in non-tax criminal cases if certain requirements are met. The Department of Justice has claimed that these requirements prevent it from quickly gaining access to needed tax information.

At the request of this Subcommittee, we recently looked at processing times in two IRS district offices--Los Angeles and Jacksonville.

In Los Angeles, during fiscal year 1979, IRS responded in an average of 68 days to head of agency requests for tax information. For court-ordered disclosures, IRS provided information in an average of 61 days. In Jacksonville, IRS needed an average of 85 days to respond to head of agency requests and an average of 80 days to comply with court-ordered disclosures.

A question can be raised as to whether two to three months is too long for an agency to wait for tax information. Unfortunately, there is no data to indicate how quickly IRS responded to such requests before the Tax Reform Act. Thus, the actual effect of the Act on processing time for such requests is unknown. It probably has increased IRS' response time if only because IRS now must evaluate the propriety of each request and ensure that all

applicable legal requirements have been satisfied. On the other hand, IRS also has to locate and review the requested records before releasing them--a time consuming process which existed prior to the Act. But, even under the current law, in extraordinary circumstances, such as during the course of a trial, IRS can expedite normal processing procedures and sometimes respond within a matter of hours to requests for necessary information from other law enforcement agencies. Therefore, given the need to strike a proper balance between law enforcement's needs and protection of taxpayer's rights, we are not convinced that the access mechanisms provided by the 1976 Tax Reform Act cause severe time problems.

The Tax Reform Act's disclosure provisions affected another aspect of coordination--the implementation of an IRS/DEA agreement designed to enable the two agencies to work together in dealing with traffickers. That agreement was signed in July 1976. Once the disclosure provisions became effective on January 1, 1977, however, questions were raised regarding the legality of the agreement and the procedures to be used in exchanging information. It took almost a year for the two agencies to resolve those problems. Finally, DEA gained access to third-party tax information on 798 alleged high-level drug traffickers. Since then, DEA has been able to obtain third-party tax

information on various traffickers through the specific access provisions in the Tax Reform Act.

In our March 1979 report, we recommended that the Congress consider the need to amend the Tax Reform Act's disclosure provisions to reduce their adverse effect on law enforcement activities, recognizing the need to maintain the balance between law enforcement and individuals' rights. Senate amendment number 734, introduced on December 4, 1979, addresses this issue. The amendment provides for exchange of information between IRS and other law enforcement agencies without obtaining a court order. We have not fully analyzed its implications, but the amendment could serve as a starting point for congressional debate on this sensitive issue.

Summons provisions of the Tax Reform Act interfere with investigative activities

Another feature of the Tax Reform Act--the summons provisions--may undermine criminal investigations through unreasonable delays. When auditing a taxpayer or conducting a criminal investigation, IRS can usually summon a taxpayer or a third-party recordkeeper--such as the taxpayer's accountant or banker--to produce books, papers, records,

or other data. Before March 1, 1977, IRS was not required to notify a taxpayer when it issued a summons to a third-party recordkeeper. Thus, taxpayers sometimes were unaware of IRS' investigations into their financial affairs.

The Tax Reform Act of 1976 now requires IRS to notify the affected taxpayer after issuing a summons to a third-party recordkeeper. The taxpayer then has 14 days within which to stay compliance by notifying IRS. If IRS initiates court action to enforce the summons, the taxpayer can intervene in the court proceedings.

IRS and the Justice Department believed that the summons provisions would unreasonably delay criminal tax investigations while benefiting, for the most part, the illegal element in our society. We have recently found evidence to indicate that their position may be valid.

IRS' Western region did a detailed analysis of summons problems. It disclosed that taxpayers stayed compliance in relatively few instances. Only 240, or 8.5 percent, of the 2,823 summonses issued by the region's criminal investigators were stayed during the first 6 months of fiscal year 1979. Significantly, however, the region found that tax protesters and individuals involved in illegal activities, including drug traffickers, were the individuals most likely to stay compliance. A total of 304, or 75 percent, of the 411 summonses pending enforcement at June 30, 1979, involved such

individuals. The region also noted that, during fiscal year 1978, taxpayers stayed compliance in 691 instances but actually contested summonses in court in only 82 instances, or about 12 percent of the time. This is a clear indication that many individuals who stay compliance seek only to delay an ongoing criminal tax investigation.

Despite these strong indications, the extent to which summons provisions are used nationwide to impede IRS investigations is unknown because IRS has not collected comprehensive data on the problem. Nevertheless, given the results from the Western region, we recommend that the Congress consider revising the summons provisons.

The Congress could adopt the stay of compliance procedures contained in section 1105 of the Right to Financial Privacy Act of 1978. That Act calls for an individual to be notified when a Government agency seeks access to financial records by means of an administrative summons. However, at the outset, the affected individual must specify to a court in writing why he or she objects to the summons. The Government must then file with the court its written justification for seeking the records. The law further authorizes the court to reach a decision based on the written affidavits.

Dual prosecution policy limits IRS case development

In addition to Tax Reform Act provisions, certain Federal agency policies limit investigation efforts. A Department of

Justice policy, for example, referred to as "dual prosecution," provides that all offenses arising out of a single transaction, such as drug trafficking and evading taxes on the ensuing profits, should be tried together.

However, time delays and duplicative legal reviews affect all criminal tax cases. These delays have a particular impact on IRS' drug-related investigations because, as I stated earlier, narcotics violators are often arrested and convicted on a drug charge before IRS can fully develop the related tax case for prosecution. If that happens, Justice will usually decline to prosecute the person for criminal tax fraud. In such instances, IRS has wasted scarce investigative resources and the drug dealers' resources remain in tact. The following examples illustrate the dual prosecution problem.

--An individual who had failed to report at least $150,000 during a 2-year period was sentenced to 1 year in prison on a narcotics misdemeanor. IRS attorneys did not forward this case to Justice for review because the individual was already incarcerated.

--In another case, the Department of Justice declined to prosecute a class I violator on criminal tax charges because he pled guilty to a felony indictment count carrying a maximum sentence of 5 years in prison. Subsequently,

the individual was sentenced to 5 years probation. IRS' investigation proved useless from a criminal tax standpoint, although civil actions may result.

To correct these problems and better use IRS' investigative skills in deterring drug traffickers, IRS and DEA should coordinate their investigations more closely. The Justice Department should also reevaluate its dual prosecution policy as it relates to narcotics traffickers.

Jeopardy and termination assessments have declined

Another agency policy inhibiting investigative efforts comes from IRS itself and involves the evolution of jeopardy and termination assessment criteria. The Internal Revenue Code provides that when the IRS determines that the collection of a tax may be in jeopardy, it may immediately assess and collect the tax--through seizure of property, if necessary. If the date for filing a return and paying income tax has not passed, a termination assessment may be made of the tax liability before the end of the tax year. If the due date for filing a return and paying the tax has passed, filing and payment is generally done pursuant to a jeopardy assessment.

Before fiscal year 1972, IRS made relatively few jeopardy and termination assessments. However, in response to the President's announcement of an expanded effort to combat drug abuse in July 1971, IRS established a high-priority project called the Narcotics Traffickers Program. The purpose of the program was to make a systematic tax investigation of middle and upper echelon narcotics dealers. IRS statistics show that, after the trafficker program was initiated, many of the jeopardy assessments and the majority of the termination assessments made were directed at individuals suspected of, or arrested for, drug law violations.

In March 1974 IRS revised the objective of the Narcotics Traffickers Program to that of achieving maximum compliance with the Internal Revenue laws rather than disrupting the distribution of narcotics. Subsequently, in May 1974 IRS issued instructions emphasizing that the same selection criteria applied to other assessments should also be applied to jeopardy and termination assessments, regardless of the background or criminal history of the taxpayer. This was to assure that only cases with substantial and documentable tax violations were included in the program. The Congress amended the law in 1976 to afford taxpayers subjected to such assessments quicker judicial remedy than had previously been available. Also in January 1977, the Supreme Court ruled that a valid search warrant was needed to seize a taxpayer's possessions on the taxpayer's private premises.

The change in law, together with IRS' revised criteria and the 1977 Supreme Court decision, led to a sharp decline in the use of these powerful tools. Total jeopardy assessments, after rising from 298 in fiscal year 1972 to 526 in fiscal year 1974, rapidly declined to 69 by the end of fiscal year 1979. Similarly, IRS made 5,311 total termination assessments during fiscal years 1972 to 1974, but it made only 756 during the next 5 years.

There was also definite evidence that IRS had abused those powers during the early and mid-1970s. The statistics indicate, however, that IRS has all but abandoned use of jeopardy and termination assessments as civil enforcement tools. Yet, nothing in the law precludes IRS from using these tools. We believe that IRS should increase the use of these tools under proper circumstances.

Currency and foreign account reports are not used effectively

Finally, I would like to discuss financial transaction reports--another means that Federal agencies have to identify criminal activity but which have not been used effectively. To facilitate Federal investigations of illegal activities, such as drug trafficking and tax evasion, the Congress enacted laws requiring that certain financial transactions be reported by individuals and financial institutions. The Congress intended that the various reports--currency, foreign bank account, and foreign trust--would be useful to Federal agencies

in carrying out their investigative responsibilities. It was believed that the financial reporting requirements would help in investigating illicit money transactions, as well as persons using foreign bank accounts, to conceal profits from illegal activities, such as drug trafficking.

In April 1979, we reported that the various reports have not been as useful to Treasury and IRS as the Congress might have expected. (Attachment IV to my statement contains a copy of the digest of that report.) While improved use of the reports alone would not lead to the detection and prevention of illegal activities, such as drug trafficking, it would provide responsible Federal agencies with information that could help them deal with those activities.

The 1970 Bank Secrecy Act requires that reports be filed on domestic currency transactions of more than $10,000 and on imports and exports of more than $5,000 in currency or monetary instruments. We recommended that Treasury centralize processing of currency reports within its enforcement communications system to improve their usefulness. By centralizing the data on Treasury's system, the reports would be readily available to Treasury personnel as well as personnel from other agencies, like DEA, which already have access to that system. Treasury agreed with our recommendation. It also recently proposed new regulations which should further improve the usefulness of currency reports for investigative purposes.

The Bank Secrecy Act also authorized the Secretary of the Treasury to require that certain individuals file reports concerning their relationship with foreign financial institutions. In a May 5, 1977, report, the House Committee on Government Operations concluded that the foreign bank account reporting requirements had not been very effective and that their value as an investigative tool could not be determined until the Treasury Department and IRS put a full effort into implementing the requirements. The Committee made 10 recommendations to IRS and Treasury designed to improve the usefulness of foreign bank acount information. Treasury responded positively.

The Congress has also required taxpayers to file foreign trust returns, specifically to enable IRS to better ensure compliance with tax laws governing foreign trusts. The returns also can be useful to IRS as a means for identifying and initiating tax investigations on individuals who use trusts as a means for storing or laundering large sums of money derived from illegal activities, such as drug trafficking. However, if IRS initiates an investigation of a trafficker through analysis of a trust form, it cannot inform DEA of that individual's identity due to disclosure restrictions discussed earlier.

In our April 1979 report, we concluded that IRS had neither developed a compliance program to ensure that required forms are filed, nor established a method for

processing and evaluating the forms designed to maximize their usefulness. As a result, the potential usefulness of the forms is unknown. In response to our recommendations, IRS agreed to take action to achieve maximum compliance with the foreign trust return filing requirements and improve their usefulness.

Although in recent months Treasury has tried to make the currency, foreign bank account, and foreign trust reports more useful, it must also monitor their use to determine their value in detecting and deterring criminal activities It also needs to determine whether the reports have other potential uses.

The reports have been useful in some instances when associated with other investigative information. On the other hand, if a person fails to comply with or avoids the reporting requirements, the reports have little value unless information developed through other means reveals noncompliance. Except for such situations, the effectiveness of the reporting requirements is necessarily limited since a person bent on violating the law would probably not risk detection by engaging in a reportable currency transaction or by voluntarily complying with a reporting requirement.

SUMMARY

In summary, unless the Federal Government makes a more coordinated and concerted effort to immobilize the financial

resources of drug traffickers, the drug business will continue to flourish. DEA has the power to seize these resources. However, it does not have extensive financial expertise and has emphasized seizing drugs and incarcerating violators whose resources remain intact. Therefore, IRS, with its financial and tax expertise, can play an important role. Although numerous problems have prevented IRS from becoming a significant force in the war against narcotics traffickers, resolving these problems alone, without interagency coordination, will not alleviate the Nation's drug problem. The key issue still is the Government's overall lack of a well-integrated, balanced, and truly coordinated approach to the problem.

Mr. Chairman, this concludes my prepared statement. I would be happy to respond to any questions.

COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

GAINS MADE IN CONTROLLING ILLEGAL DRUGS, YET THE DRUG TRADE FLOURISHES

D I G E S T

Federal agencies have fought hard to reduce the adverse impact of illegal drugs, primarily heroin and dangerous drugs, on American society. These efforts have shown some positive results as measured by decreased drug-related deaths and injuries, and reduced availability of some illegal drugs.

Nevertheless, drug trafficking and abuse still flourish despite several decades of U.S. efforts both here and abroad. The gains made are fragile, requiring constant vigilance, as

--source countries move quickly to fill temporary drug shortages,

--trafficking patterns shift, and

--the types of drugs consumed readily change.

This report assesses the Federal Government's drug enforcement and supply control efforts during the last 10 years, including information contained in a series of GAO reports issued on drug control and various related topics during this time. (See pp. 161 to 164.)

WHAT SUCCESSES HAVE BEEN ACHIEVED?

Notable successes have been attained in carrying out the Federal supply reduction strategy, as a result of actions taken in the United States and overseas to immobilize major trafficking networks and control the production of illicit drugs. (See pp. 15 to 21.)

--Turkish restrictions on poppy cultivation and increased United States and French enforcement disrupted the French-Turkish heroin connection in the early 1970s and produced a dramatic shortage of heroin in the United States.

--Joint U.S.-Mexico efforts in crop eradication and narcotics enforcement, assisted by a drought,

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October 25, 1979

are decreasing Mexico's share of the U.S. illicit heroin market. Street-level heroin currently has the lowest purity and highest price since 1973, and National Institute of Drug Abuse statistics show that heroin-related deaths have been declining.

--Enforcement activities in the United States and abroad have caused significant drug removals and increased clandestine laboratory seizures.

--Emphasis on conspiracy investigations has led to many high-level drug traffickers being convicted on conspiracy charges, some receiving substantial prison sentences.

--Other countries have increased their efforts to reduce supply on their own and through United Nations and United States programs.

--The amount of diversion of legal drugs at the wholesale and manufacturing levels has declined sharply in recent years.

Current indicators suggest that there is a major shortage of heroin in the United States, a significant accomplishment against the Nation's number one drug enforcement priority. However, this and other such hard-won successes are short-lived. Growing areas, shipment routes, trafficking organizations, and even the types of drugs abused all readily change and adapt to new conditions.

For example, the heroin shortage created by the breaking of the French Connection was temporary. Mexico emerged as the next principal supplier of heroin to the United States. Today's concern is that as Mexican heroin availability declines, heroin from Southeast Asia and the Middle East will fill the gap. Some also fear that use of dangerous synthetic drugs will continue to increase as heroin users find it difficult to obtain heroin.
(See pp. 19 to 21.)

WHY DOES THE PROBLEM PERSIST?

THE ENORMOUS SUPPLY OF AND DEMAND FOR DRUGS has created a multibillion dollar worldwide business involving millions of Americans. The National Institute on Drug Abuse has estimated that there are:

--1.7 million persons who have used heroin, with 453,000 daily users.

--13 million persons who have used stimulants such as amphetamines.

--6.9 million persons who have used PCP at least once.

--10 million who have used cocaine.

--43 million people who have tried marijuana at least once.

The marijuana market alone consumes between 60,000 and 91,000 pounds per day, resulting in an outlay of $13 billion to $21 billion per year. (See pp. 21 to 25.)

THE SOCIAL, ECONOMIC, AND POLITICAL REALITIES OF DRUG-GROWING COUNTRIES make it difficult to prevent cultivation of illicit crops and stop trafficking at the source. Most producing nations are poor, underdeveloped, struggling countries presenting problems that are too complex for a predominantly law enforcement approach to be effective in reducing drug supplies. Suppression efforts have been hindered by long-standing and socially accepted traditions of smuggling and corruption. As seen from several pilot projects, the other approach of substituting legitimate crops for drugs requires massive economic development that is both costly and long-term. To date, the developed countries of the world have been unwilling to fund such high-risk ventures. (See pp. 29 to 31, and 44 to 55.)

THE ENORMOUS PROFITS OF DRUG TRAFFICKING attract an ample number of entrepreneurs who see opportunities that far outweigh those offered by legitimate businesses. Payments by abusers and traffickers for heroin, cocaine, marijuana, and hashish in the United States are estimated to be on the order of $35 billion to $51 billion annually. Drug trafficking in the U.S. today appeals to people from all walks of life, including doctors, lawyers, accountants, businessmen, and entertainers. (See pp. 31 and 32.)

IT IS EASY TO ENTER AND DISTRIBUTE DRUGS in the United States. While nobody knows for sure how much illicit drugs come into the country, it has been estimated that law enforcement agencies seize only 5 to 10 percent of all illicit drugs available. (See pp. 31 and 32.)

ACTIONS NEEDED TO FULLY SUPPORT FEDERAL DRUG STRATEGY IMPLEMENTATION HAVE NOT MATERIALIZED. Differing views among Government agencies, as well as the public, make it difficult to attain the necessary legislative, executive, and judicial actions. Drug supply reduction efforts have yet to achieve a well-integrated, balanced, and coordinated approach. (See pp. 32 to 34.)

WHAT CAN WE DO ABOUT THE PROBLEM?

The United States must take a much tougher and consistent stance to make real gains in reducing the availability of illicit drugs. The following long-standing problems must be resolved:

--Organizational difficulties between Federal agencies diluting law enforcement efforts at borders.

--Large-scale drug traffickers, in terms of immobilization from trafficking, being incarcerated for short periods of time while their ill-gotten gains remain intact.

--Unclear Federal, State, and local enforcement roles hampering attacks on drug traffickers.

--Inconsistent and sometimes conflicting drug policies resulting in no clear overall direction.

--Businesses and individuals promoting the use of drugs through the sale of drug-oriented paraphernalia and magazines.

--Governments of developed countries and international financial institutions providing little or no support for controlling illicit drug production.

The executive and legislative branches must form a partnership to agree upon and affirm a national policy for dealing with drug abuse and support necessary legislation. A joint commission could be formed to accomplish this and to recommend a course of action to promote vigorous implementation of the agreed policy. (See pp. 34 and 35.)

BORDER MANAGEMENT PROBLEMS NEED TO BE RESOLVED

Although the U.S. border provides opportunities for interdicting illicit drugs, the availability of drugs attests to the fact that the border has not been a serious impediment to illegal entry. Large amounts of heroin and marijuana have crossed the land border with Mexico. More recently, our Southeastern States have been flooded with marijuana and cocaine shipped by air and sea from South America. (See pp. 66 to 82.)

GAO recommended in its 1977 report on the Southwest border (GGD-78-17) that the Congress require the executive branch to develop a comprehensive border control plan. A border management agency should be established to overcome organizational difficulties and better respond to the problems created by drug smuggling. (See pp. 69 and 70.)

OPPORTUNITIES TO OVERCOME OBSTACLES IN IMMOBILIZING MAJOR TRAFFICKERS

Federal efforts to reduce drug trafficking through attempts to immobilize major traffickers have fallen short of expectations. Even though numerous high-level traffickers have been convicted their organizations often continue to operate and maintain distribution capacity. A concerted effort among numerous Federal agencies to incarcerate major drug dealers for long periods and take away their financial resources has not materialized to the extent necessary. (See pp. 83 to 112.)

For recommendations to the Congress and Federal agencies that will strengthen prosecution of drug traffickers and dealers and help to better attack the tremendous financial gains from trafficking. (See pages 111 and 112.)

CHANGES IN BAIL AND SENTENCING COULD STRENGTHEN IMMOBILIZATION EFFORTS

Bail and sentencing practices in Federal courts throughout the country have diluted the effect of drug enforcement efforts. Many defendants who are released on bail continue their drug trafficking because Federal law does not allow judges to consider danger to the community a reason for denying bail. Even when convicted, drug traffickers are often not effectively immobilized for long periods because prison sentences are short. (See pp. 113 to 126.)

The Congress should consider modifications to the bail law that take into account both constitutional principles and the means to prevent traffickers from engaging in illegal activities that present a danger to the community. Correcting the sentencing problem is not easy, however; any changes to the criminal justice system must be comprehensive and approached with utmost caution. GAO therefore recommends that the Judicial Conference of the United States assess the effects of judicial discretion, including the sentencing of drug violators. (See p. 126.)

NEED TO CLARIFY FEDERAL, STATE, AND LOCAL ENFORCEMENT ROLES

Increased reliance has been placed on State and local drug enforcement efforts because Federal efforts have focused on leaders of national and international trafficking networks. Even though the Federal Government has developed numerous programs to assist and cooperate with State and local agencies, the mounting of a unified attack has been made virtually impossible by financial, political, and other realities. State and local agencies are allocating fewer resources for drug enforcement,

and Federal grants for the same purpose have declined as well. In addition, jurisdictional problems in some regions hinder attempts to fully mobilize the more than 15,000 police agencies in the United States against drug abuse and trafficking. (See pp. 127 to 134.)

In the face of these difficulties, the Attorney General must establish a clear, realistic policy on what can reasonably be expected from State and local governments and what the Federal Government should do to elicit their support. The response of the various levels of government to businesses' and individuals' promoting the use of drugs through the sale of drug-oriented paraphernalia and magazines must also be addressed. (See pp. 134, 21, and 22.)

SOMEONE MUST OVERSEE STRATEGY IMPLEMENTATION

The Congress has long recognized the Federal Government's continuing failure to provide a central mechanism to establish drug policy and be accountable for its effective implementation. Even though the Office of Drug Abuse Policy was established to do this, it was abolished before it had a chance. If any improvement is to be made in coordinating Federal drug control efforts, someone is needed who has a clear delegation of authority from the President to monitor activities and demand corrective actions. This responsibility is currently entrusted to the President's Domestic Policy Staff, and it is too early to tell whether this arrangement will ensure the vigorous implementation of the Federal drug strategy. The presence of a tough and consistent stance will go a long way in demonstrating within the United States and to other countries the strong commitment our Nation is making in combatting the drug abuse problem. (See pp. 10 to 12 and pp. 34 and 35.)

DRUG PROBLEM REQUIRES WORLDWIDE COMMITMENT

The United States has been the prime force in efforts to control illicit drug production, but

increased commitment of developed countries is needed if we are ever to have a great impact on the problem. With this reality in mind, GAO recommends that the Secretary of State, with the support of the Congress, promote a world conference and the formation of a consortium of victim countries that would develop a plan of action to fight the global drug problem in a unified way. (See pp. 37 to 65.)

To further develop strong drug control within foreign countries, GAO also recommends that the Secretary of State require the Assistant Secretary for Narcotics Matters to prepare realistic Country Narcotics Actions Plans detailing short and long-term objectives, the means of achieving these goals, and the methods for reviewing progress. For drug-producing areas that encompass several countries, action plans should be prepared on a regional basis.

GAO believes law enforcement and crop eradication will always have a major role in drug control, and can have an even greater impact if GAO's recommendations are implemented. However, there is no guarantee that the supply and use of drugs will be reduced significantly for a long time. Effective enforcement, eradication, and other controls will cause shifts and temporary disruptions in trafficking and drug use patterns and will buy time to enable the Nation to concentrate on long-term solutions. Also, it is generally acknowledged that the demand for drugs would be even greater were it not for law enforcement and supply control efforts.

One question which remains unanswered is: How does this Nation effectively curtail the demand for illicit drugs? In the Nation's search for long-term solutions to the drug abuse problem, it must continue to give high priority to each vital component of the Federal effort: law enforcement and control, treatment and rehabilitation, education and training, and research.

Eight Federal Government organizations having direct supportive responsibilities for activities discussed in this report were asked to comment on the report. The Administrative Office of the U.S.

Courts and the Federal Judicial Center offered no specific comment on GAO's report. The Department of the Treasury, the Central Intelligence Agency, and the Department of Health, Education, and Welfare in their responses did not take issue with any of the report's contents. The Departments of Justice, Transportation, and State, while generally agreeing with GAO's assessment of the drug problem and recommendations to address it, expressed some concern with certain areas in the report they considered misleading, outdated, or disappointing. Chapter 8 contains a discussion of these Departments' concerns and GAO's evaluation. (See pp. 135 to 147.)

COMPTROLLER GENERAL'S REPORT
TO THE JOINT COMMITTEE ON
TAXATION
CONGRESS OF THE UNITED STATES

IMPROVED PLANNING FOR DEVELOPING AND SELECTING IRS CRIMINAL TAX CASES CAN STRENGTHEN ENFORCEMENT OF FEDERAL TAX LAWS

D I G E S T

Taxpayers who truthfully report their income and pay the taxes required expect the Internal Revenue Service (IRS) to do all it can to make sure that everyone pays his or her fair share. IRS tries to do so through audits, collection actions, and criminal investigations.

Each year, IRS' Criminal Investigation Division recommends prosecution of more than 3,000 people who try to evade paying taxes. About 1,400 are convicted, fined, and/or jailed.

IRS has 2,800 agents to specifically work on tax fraud problems. It must use these agents as effectively as possible. Careful planning is essential if the Criminal Investigation Division is to carry out a balanced and effective enforcement program. The Division attempts to balance its cases among all types of violations in many income tax brackets, occupations, and geographical locations to promote voluntary compliance with tax laws.

However, the Division's long- and short-range plans need improvement. The national office needs to clearly define its national strategy and needs to establish additional, more specific goals for detecting and deterring tax fraud. Improved plans would

--help IRS to better ensure that its criminal investigation agents are used as productively as possible (see pp. 5 to 11),

--provide additional criteria to measure how well the Criminal Investigation Division is achieving its mission (see pp. 9 to 11), and

--improve case development activities which produce the information that Criminal

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Investigation Division managers use in selecting cases (see pp. 26 to 46).

BETTER PLANNING NEEDED

The Criminal Investigation Division's present long-range plan is general and does not clearly define a national strategy. Its short-range plans specify various pockets of noncompliance requiring national attention. But the short-range plans include only a limited number of specific, measurable goals; as a result, 58 district chiefs have overall program direction responsibility. Each District Criminal Investigation Division chief is responsible for directing a tax fraud program within the context of broad, general guidelines. (See pp. 5 to 9.)

In 1975, the Division recognized the deficiencies in these plans and began to improve them. Assisted by the National Academy of Public Administration, the Division conducted a planning model study during fiscal years 1977 and 1978. In fiscal year 1980, it will test a more rigorous long-range planning process. (See pp. 11 to 13.)

However, the Division's revised planning process lacks one vital component--more information on a regular basis from the Department of Justice's Tax Division and from U.S. attorneys. IRS recommends prosecution of alleged tax evaders, but it is Justice's Tax Division which reviews IRS recommendations and decides whether to prosecute. Similarly, U.S. attorneys prosecute most criminal tax cases. Thus, Justice plays a key role in administering the criminal provisions of the tax laws; this is why Justice officials' views must be considered in the Criminal Investigation Division's planning process. (See pp. 13 to 20.)

The Attorney General and the Commissioner of Internal Revenue need to develop a system whereby Justice provides the Criminal Investigation Division with useable input to program plans and with better guidance on case requirements. (See pp. 20 and 21.)

CASE DEVELOPMENT AND SELECTION ACTIVITIES NEED IMPROVEMENT

The basic data that Criminal Investigation Division managers use in deciding which cases warrant detailed investigation is generated by referrals from the Examination and Collection Divisions, information gathering efforts by special agents, and information item evaluations (referred to collectively as case development activities). Selection decisions are important because they determine the focus of the Division's program. Cases selected for detailed investigation require substantial resource expenditures; however, many cases selected do not lead to prosecution recommendations, let alone convictions. (See pp. 24 to 26.)

Improved planning would provide Division managers with better guidance for conducting case development activities and making case selection decisions. IRS can further strengthen case development and selection activities by

--providing its employees better and more consistent training on referrals (see pp. 26 to 34),

--affording managers better guidance for initiating and conducting information gathering efforts (see pp. 34 to 43), and

--developing criteria against which the Criminal Investigation Division can measure the potential value of information items (see pp. 43 to 46).

The Criminal Investigation Division can also further improve its case selection process by requiring that each district use the "case pool" approach. Under that system, Division managers need not consider whether staff is available before initiating a case. Rather, a "pool" of unassigned cases results, and managers can select the best case from that pool as staff becomes available. Besides affording Division

managers alternative cases to select from, the case pool approach serves as a management control over staff resource allocations. (See pp. 46 and 47.)

RECOMMENDATIONS

To improve the Criminal Investigation Division's planning process, GAO recommends that the:

--Attorney General and the Commissioner of Internal Revenue develop specific methods through which Justice and IRS can better coordinate their efforts to combat tax fraud. (See p. 21.)

--Commissioner further refine the Criminal Investigation Division's short-range program plans in light of data developed through its long-range planning process. (See p. 21.)

To improve case development activities, the Commissioner should:

--Clarify the guidance provided to referring agents by developing guidelines for referral training applicable to each district office. (See p. 48.)

--Develop guidelines which district directors and higher level IRS officials can use to evaluate the appropriateness of Division-proposed information gathering projects. (See p. 49.)

--Revise guidelines pertaining to individual information gathering activities so that files on such efforts contain clear documentation describing investigative steps performed and results leading to disposition decisions. (See p. 49.)

--Revise IRS' information item form as appropriate to ensure the future availability of data needed to analyze and improve information item evaluations. (See p. 49.)

The Commissioner should also require that each district Criminal Investigation Division chief use the case pool approach in selecting cases. (See p. 49.)

AGENCY COMMENTS

Both IRS and Justice generally agreed with GAO's recommendations. Ongoing or planned actions, described in their official comments, were generally responsive to those recommendations. (See pp. 22, 23, 49 and 50.)

COMPTROLLER GENERAL'S REPORT TO THE JOINT COMMITTEE ON TAXATION

DISCLOSURE AND SUMMONS PROVISIONS OF 1976 TAX REFORM ACT--PRIVACY GAINS WITH UNKNOWN LAW ENFORCEMENT EFFECTS

D I G E S T

The Congress, through the Tax Reform Act of 1976, tightened the rules governing the Internal Revenue Service's (IRS') disclosure of tax data and its issuance of summonses to third-party recordkeepers. The new legal provisions have had their desired effects--taxpayers have been afforded increased privacy over information they provide IRS and additional civil rights in summons matters.

DISCLOSURE PROVISIONS: EFFECTS ON LAW ENFORCEMENT NOT SUFFICIENTLY DOCUMENTED

The disclosure provisions of the Tax Reform Act, effective January 1, 1977, placed substantial restrictions on other government agencies' rights of access to tax information and authorized criminal and civil penalties for unlawful disclosures.

In February 1977, IRS and Department of Justice officials expressed concern that those provisions would make the boundaries of lawful disclosure unclear and would cause a decrease in coordination between IRS and other members of the law enforcement community. (See pp. 2 and 3.)

Taxpayers have benefited from the increased confidentiality provided by the disclosure provisions of the Tax Reform Act. The concerns of law enforcement officials were not totally unfounded, however.

The new legal provisions have confused IRS employees. Despite the confusion, the number of court actions alleging

unlawful disclosures has been small. The few court actions could mean that IRS employees, when faced with disclosure questions, have properly interpreted the law or have erred on the side of caution by not disclosing data that could have been disclosed. Another possibility is that unlawful disclosures have gone unnoticed. Whichever the case, recent IRS efforts to provide additional disclosure training should help alleviate employee confusion. (See pp. 17 and 18.)

The disclosure provisions also have adversely affected coordination between IRS and other law enforcement agencies. Based on available evidence, however, some of the coordination problems produce little cause for concern. IRS, for example, almost assuredly takes more time now to respond to Department of Justice requests for access to tax information. The time IRS takes to respond to those requests, however, does not seem unreasonable considering the increased concern for privacy and the fact that Justice was unable to cite any examples of specific problems caused by IRS' response time. (See pp. 14, 15, and 19.)

Other coordination problems are more troublesome. For example, coordination with the Department of Justice has been affected because IRS is restricted, in some situations, from alerting attorneys that it has tax information that may be of value to them in their role as Federal law enforcement coordinators. (See pp. 10 to 12 and 19.)

Although the disclosure provisions have had some adverse effects, the record of those effects is insufficient to warrant recommending revisions to the law. In this regard, GAO is uncertain as to whether any revisions could be made without disturbing the balance between criminal law enforcement and individuals' rights. That balance is particularly important in tax administration because taxpayers should

be able to satisfy their income tax obligations with the knowledge that information they provide IRS will be used only as authorized by law. (See p. 20.)

Matter for consideration by the Congress

GAO is not advocating changes to the disclosure provisions of the Internal Revenue Code. The types of coordination problems being experienced, however, point up the need for Congress to consider whether the adverse impacts on Federal law enforcement activities warrant revision of the legislation and whether any revision can be made without disrupting the balance between criminal law enforcement and individuals' rights.

Agency comments

IRS agreed that taxpayers have been accorded increased privacy over information they provide the Service. Also, IRS acknowledged that the disclosure provisions have had no direct effect on IRS' enforcement of the tax laws.

The Department of Justice expressed the belief that GAO had understated the impact of the disclosure provisions and that the Tax Reform Act may not have struck a proper balance between privacy and law enforcement. In seeking to demonstrate that point, Justice referred to various matters, such as investigative delays, cumbersome procedures, diminished coordination, and duplicative investigations. Although GAO does not fully agree with each of Justice's comments, it does understand Justice's concerns. GAO also understands congressional and public concerns for privacy.

Aware of the need to strike an appropriate balance between varying concerns and mindful of the problems in trying to assess whether the Tax Reform Act has struck that balance, GAO's conclusion remains the same: it has seen insufficient evidence to warrant

recommending that the disclosure provisions be revised. (See pp. 20 to 23.)

SUMMONS PROVISIONS: ADMINISTRATIVE CHANGES ARE NEEDED

The summons provisions of the Tax Reform Act, effective March 1, 1977, require IRS to notify the affected taxpayer after issuing a summons to a third-party recordkeeper. The taxpayer then has 14 days to stay compliance, that is, to order the recordkeeper not to comply with the summons. If IRS initiates court action to enforce the summons, the taxpayer can intervene in the court proceeding.

In February 1977, IRS and the Department of Justice warned that the summons provisions would unduly delay criminal tax investigations and would tend to benefit those whose illegal activities extend beyond the tax laws. Unless IRS and Justice can substantiate the existence and extent of those problems, however, the Congress cannot be expected to look favorably on requests for changes to the law. The reporting system IRS initiated to monitor the effects of the summons provisions is not providing the type of data that can be reliably used to meet that need. (See pp. 4 to 6 and 29 to 35.)

Statistics GAO developed indicate that the investigative delays anticipated by IRS and Justice have occurred. Although delays are unavoidable when taxpayers are given the right to contest the legality of third-party summonses, procedures followed by IRS and the Department of Justice in processing requests for summons enforcement contributed to those delays. IRS and Justice have taken appropriate steps to streamline those procedures. (See pp. 35 to 37.)

Even if its reporting system were providing more reliable data on the effects of the summons provisions, IRS would find it difficult to demonstrate a need to amend those provisions since they have resulted in the withdrawal of many third-party summonses. Some of those summonses were withdrawn because they were determined to be defective or unnecessary. Most were withdrawn, however, because IRS employees were not fully conversant with the procedures to follow in preparing and issuing summonses. (See pp. 24 to 29.)

GAO's review was limited to those summonses on which taxpayers stayed compliance. But summonses not stayed by taxpayers are also likely to contain technical and procedural errors and may, in a few instances, be defective or unnecessary. Recognizing that, additional controls are needed to protect against such summonses being issued in the first place.

If IRS takes action to improve its summons issuance process and collects accurate and useful data to demonstrate the adverse impact of the summons provisions, it may be in a better position to seek changes to those provisions in the future. (See p. 39.)

Recommendations

GAO recommends that the Commissioner of Internal Revenue

--provide additional training to all employees responsible for issuing summonses to better insure that they fully understand all legal and technical aspects of the summons process and

--require the Director of IRS' Internal Audit Division to monitor the effectiveness of IRS' summons training program.

GAO also recommends that the Commissioner revise the summons reporting system to

--provide field office personnel with more specific guidance on accounting for summonses, stays, and interventions;

--collect information designed to determine whether those whose illegal activities extend beyond the tax laws tend to exercise their rights to stay summonses and intervene in enforcement actions more than the average investigative subject; and

--accumulate statistics on investigative delays caused by the summons provisions of the Tax Reform Act. (See pp. 39 and 40.)

Agency comments

IRS agreed with GAO's recommendations. It pointed out, however, that GAO's findings do not support a conclusion that the summons provisions of the Tax Reform Act have protected the legitimate rights of taxpayers in any substantial number of cases. While not disagreeing with IRS, GAO emphasizes that it (1) did not attempt to identify every instance nationwide in which the summons provisions have protected the legitimate rights of taxpayers and (2) has no assurance that it even identified every instance in the field offices it visited.

Both IRS and the Department of Justice expressed the belief that GAO had not adequately considered issues such as delays resulting from judicial consideration of summons enforcement action and the extent to which tax protesters and persons involved in illegal activities are benefiting from the summons provisions.

The absence of hard evidence hindered GAO's discussion of these concerns. The basic message of GAO's report is not that IRS' and Justice's concerns about the summons provisions are unfounded but rather that they have not been demonstrated. IRS has

not been accumulating the type of data that would facilitate such a demonstration.

Both IRS and Justice expressed concern that many taxpayers who stay compliance with third-party summonses fail to intervene in the summons enforcement procedure. In considering solutions, both referred to the Right to Financial Privacy Act of 1978 (title XI of P.L. 95-630, Nov. 10, 1978).

Like the summons provisions of the Tax Reform Act, the Right to Financial Privacy Act calls for an individual to be notified when a government agency seeks access to financial records through an administrative summons. The Right to Financial Privacy Act makes it more difficult, however, for the affected individual to stay compliance with the summons. Justice concluded that the rules pertaining to IRS summonses should be no different than the rules pertaining to summonses issued by other agencies and that Congress should consider amending the Internal Revenue Code accordingly.

Because GAO's review was limited to summonses issued under the Tax Reform Act of 1976 and the Right to Financial Privacy Act was just recently enacted, it did not compare the effectiveness of the different procedures for staying compliance. GAO believes, however, the idea of using the stay of compliance procedure mandated by the Right to Financial Privacy Act for IRS summonses has merit and should be considered by the Congress. (See pp. 40 to 43.)

MATTER FOR CONSIDERATION BY THE CONGRESS

The Congress may want to monitor the use of the stay of compliance procedure under the Right to Financial Privacy Act and consider whether the adoption of similar provisions for IRS summonses would be appropriate. (See p. 43.)

COMPTROLLER GENERAL'S REPORT
TO THE SUBCOMMITTEE ON OVERSIGHT
COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

BETTER USE OF CURRENCY AND FOREIGN ACCOUNT REPORTS BY TREASURY AND IRS NEEDED FOR LAW ENFORCEMENT PURPOSES

D I G E S T

To facilitate Federal investigations of illegal activities, such as drug trafficking and tax evasion, the Congress enacted laws requiring that certain transactions be reported by individuals and financial institutions.

Some changes in the methods Treasury and the Internal Revenue Service (IRS) follow in processing and using such reports could improve their value.

GAO reviewed IRS' use of

--currency transaction reports;

--reports of international transportation of currency or monetary instruments;

--reports describing the creation of or transfers of money or property to certain foreign trusts;

--annual returns describing certain transfers of money or property to foreign trusts with U.S. beneficiaries; and

--reports of foreign bank, securities, and other financial accounts.

Generally, the various forms have not been as useful to IRS as the Congress might have expected when it established the reporting requirements. Improved use of the forms alone would not resolve such problems as tax evasion and drug trafficking. However, it would provide the Treasury Department, IRS, U.S. Customs Service, Justice Department, and other Federal agencies with information that could help them deal with those problems.

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CURRENCY REPORTS: ACTIONS WHICH MIGHT IMPROVE THEIR VALUE

Currency reports are required by the Bank Secrecy Act. By themselves, they are not good indicators of criminal tax violations nor do they have much audit or collection potential. Nevertheless, IRS tries to use the reports as the bases for initiating criminal investigations, audits, and collection actions. (See pp. 4 to 8.)

Currency reports might be more valuable if IRS were to use them to supplement other information it possesses concerning possible tax law violations. For example, IRS might be prompted to investigate a tax fraud allegation against an individual if several currency reports had been filed with respect to that particular individual. The reports would serve as a means for separating the tax fraud allegation from dozens of similar ones IRS cannot pursue because of limited resources.

The Treasury Department operates a computerized information storage and retrieval system--the Treasury Enforcement Communications System--designed to assist Federal personnel in carrying out various law enforcement missions. The Customs Service already enters international transportation of currency or monetary instruments reports on the data system. Currency transaction reports could also be entered on the system. (See pp. 8 to 12.)

If these reports were entered and IRS made more effective use of the data system, currency reports might be more useful and unnecessary exchanges of data among Federal agencies could be eliminated. The Treasury Department said it plans to enter the reports into the system. However, Treasury should

--ensure that IRS effectively uses the system to supplement its evaluations of tax fraud allegations and

--monitor the usefulness of the currency reports and determine whether they have other potential uses. (See pp. 12 and 13.)

FOREIGN TRUST RETURNS:
BETTER HANDLING NEEDED

IRS' handling of foreign trust returns has been characterized by indecision. It has no program for ensuring compliance with the filing requirements and has not established a meaningful method for evaluating and using the returns.

In effect, the few taxpayers who voluntarily file one of the forms have no assurance that IRS is doing all it can to identify and pursue others who choose not to file. Unless IRS can rectify the situation, it might be best to relieve the compliant taxpayer of the burden by eliminating the returns. (See pp. 15 to 19.)

FOREIGN BANK ACCOUNT REPORTS:
SOME IMPROVEMENTS MADE

In response to recommendations made by the House Committee on Government Operations in a May 1977 report, the Treasury Department:

--Began entering foreign bank account data on the Treasury Enforcement Communications System.

--Apparently resolved disclosure problems caused by the Tax Reform Act of 1976.

--Established a Reports Analysis Unit. (See pp. 21 to 28.)

Having taken those actions, Treasury now should monitor the use of computerized foreign bank account data and determine whether it has other potential uses. (See p. 28.)

RECOMMENDATIONS

The Secretary of the Treasury, in implementing the plans to enter currency transaction reports on the Treasury Enforcement Communications System, should:

--Eliminate unnecessary processing of currency reports by (1) ensuring that all currency reports are filed

with the group designated to enter the reports on the Treasury Enforcement Communications System and (2) eliminating wholesale exchanges of currency reports between IRS, Customs, and Treasury.

--Ensure that IRS uses the system to improve evaluations of information it receives and possesses concerning possible tax law violations. (See p. 13.)

The Secretary should also:

--Monitor the use of currency transaction reports, once entered on the Treasury Enforcement Communications System, and the foreign bank account data to determine if their value has improved.

--Determine whether currency reports and foreign bank account information have other potential uses. (See pp. 13 and 28.)

If the Secretary determines that the value of currency reports and foreign bank account information cannot be improved, he should request the Congress to reconsider the need for the reporting requirements. (See pp. 14 and 28.)

The Commissioner of Internal Revenue should determine whether IRS can effectively use foreign trust returns by developing

--a program for maximum compliance with the filing requirements and

--appropriate evaluation criteria aimed at making maximum use of the forms.

If the Commissioner finds that IRS cannot use the forms effectively, he should concurrently

--request, through the Secretary of the Treasury, that the Congress reconsider the need for the filing requirements and

--develop an alternative plan to help ensure taxpayer compliance with the

tax laws governing foreign trusts.
(See p. 19.)

The Commissioner should also provide necessary training and take appropriate steps to ensure that IRS personnel understand and know how to use the Treasury Enforcement Communications System. (See p. 14.)

AGENCY COMMENTS

Treasury and IRS, in a joint response, generally agreed with GAO's recommendations. They pointed out, however, that the scope of GAO's review was limited and the report did not give adequate recognition to the usefulness of currency and foreign bank account reports to other Federal law enforcement agencies.

GAO agrees that the scope of the review was limited and that, in particular instances, currency and foreign bank account reports have proven useful to Federal law enforcement agencies. GAO, however, has seen no evidence that Treasury has conducted an overall evaluation of the reports to determine their usefulness and whether the benefits are worth the associated costs of preparing, processing and disseminating the reports. GAO contends that such an evaluation is necessary before an opinion can be rendered on the overall usefulness of the currency and foreign bank account reports. (See pp. 14, 19, 20, 28, and 29.)