96TH CONGRESS
2d Session

SENATE

REPORT
No. 96-887

ILLEGAL NARCOTICS PROFITS

REPORT

OF THE

COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

MADE BY ITS

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

together with

ADDITIONAL VIEWS

T 4 (legislative day, JUNE 12), 1980.—Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1980

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AUGUST 4 (legislative day, JUNE 12), 1980.—Ordered to be printed

Mr. NUNN, from the Committee on Governmental Affairs, submitted the following

REPORT

I. INTRODUCTION

ORGANIZED CRIMINALS EVADE TAXES

Organized crime syndicates in this country can be traced at least as far back as Prohibition. To manufacture, distribute and sell large amounts of liquor, criminals learned the benefits of cooperation and organization. Organizing themselves into syndicates, gangsters made untold millions of dollars in the bootleg liquor business. They combined their illicit alcohol profits with proceeds from other illegal activities such as gambling, prostitution, extortion, political bribery, labor racketeering and narcotics.

As the Prohibition era wore on, it became apparent to Federal law enforcement officials that the extravagant financial successes of organized criminals constituted, ironically, the point at which these same criminals were most vulnerable to detection, prosecution and conviction. Failing to stop many organized criminals from making profits illegally, officials decided to try to prosecute them for not paying taxes on their profits. For organized criminals to prosper, for the big crime syndicates to survive, vast amounts of money had to be earned. Illegally earned or not, it was still income and income is subject to Federal income tax. Even criminals are required to pay income tax.

COURT

In 1927, this principle—the concept that illegal earnings can be taxed—was upheld by the U.S. Supreme Court when it ruled that a bootlegger named Manly Sullivan had to pay his income tax.[1] Sullivan filed no tax return, arguing that income from illegal transac-

[1] *U.S. v. Sullivan*, 274 U.S. 259 (1927).

tions was not taxable and that to declare such income would be self-incriminating within the meaning of the Fifth Amendment. The Court disagreed. It found no reason "why the fact that a business is unlawful should exempt it from paying taxes that if lawful it would have to pay." As for incriminating himself, the Supreme Court said, "It would be an extreme if not extravagant application of the Fifth Amendment to say that it authorized a man to refuse to state the amount of his income because it had been made in a crime."

With this Supreme Court decision, Federal authorities had a new weapon to use against organized criminals. From the taxation point of view, gangsters found themselves undermined by their very success, the large profits they were earning from their illicit enterprises. Here was a problem they had not bargained for. And in the courtroom, tax returns made excellent witnesses for the prosecution. Tax returns did not suffer from failing memories. They could not be bribed or intimidated. Their families could not be threatened. They did not lose their composure under vigorous cross-examination. The Government brought tax cases against many organized criminals of the Prohibition era. Al Capone, one of the most notorious of the gang leaders, was sentenced to 11 years in prison on a tax evasion conviction. The taxation approach did not end with the Prohibition era. The Government continued to use it. In 1957 another notorious gangster, Frank Costello, was sent to prison for tax evasion, demonstrating the continued effectiveness of charging mob leaders with tax evasion. More recently, Joseph (Doc) Stacher, a successor to Bugsy Siegel in the Meyer Lansky criminal organization, was convicted of tax evasion in April of 1964.

VIOLATIONS

There was an added advantage to this approach. It was that in gathering information on tax matters, Internal Revenue Service agents were often able to develop non-tax evidence of criminality that could prove helpful to other Federal law enforcement agencies. Frequently this information was shared and prosecutions on non-tax violations were begun or enhanced on the basis of facts first developed by the IRS and then turned over to other investigators.

As the Government's principal revenue collection agency, the Internal Revenue Service itself has benefited over the years from the favorable publicity surrounding those cases in which well-known criminals like Capone and Costello went to jail on tax charges. The IRS, and its parent Department of Treasury, believed that publicized trials like those served as a reminder to all Americans that tax fraud is a serious crime and that even clever, conspiring hoodlums are not able to get away with it. Such convictions, it is felt, both encouraged law-abiding Americans to pay their taxes; and also assured the average American taxpayer that the system is equitable and that the overwhelming majority of citizens are paying their fair share.

Among law enforcement agents in general, the IRS was seen as a valuable resource. While an individual's tax return is confidential, non-tax intelligence developed by the IRS could be shared with other criminal investigators after established procedures of disclosure were

followed. In turn, these investigators were encouraged to turn over tax-related intelligence they had developed to the IRS. In some instances, cooperation evolved among Federal law enforcement agencies. This cooperation was exemplified in the Federal organized crime strike forces set up in the 1960's in the nation's big cities. The purpose of the strike forces was to mobilize under one roof the best investigative and prosecutorial resources of the executive branch in a coordinated assault on organized crime. IRS agents cooperated in the strike force approach.

Tax Reform Act and Policy Change Limit IRS Role in Organized Crime Cases

To the disappointment of other law enforcement agencies, IRS began in the mid-1970's to pull back from its previous role in initiating or assisting in cases against organized criminals. This new policy was reflected in remarks by IRS Commissioner Donald Alexander when, in 1974, he said "Selective enforcement of tax laws designed to come down hard on drug dealers and syndicated crime, for example, may be applauded in many quarters but it promotes the view that the tax system is a tool to be wielded for policy purposes and not an impartial component of the democratic mechanism which applies equally to all." Alexander, who served as Commissioner from 1973 to 1977, went on to say, ". . . The overall emphasis of our criminal enforcement activities has been shifted away from special enforcement programs such as narcotics traffickers and Strike Forces and have been aimed more directly toward the taxpaying public in general" (exhibit 38; pp. 496–507).[2]

In addition to the IRS policy, as articulated by Alexander, Congress placed new restraints on IRS, limiting its powers to share information and to cooperate in other ways with other law enforcement agencies in the pursuit of organized criminals. Known as the Tax Reform Act of 1976, the legislation was signed into law by President Ford on October 4, 1976. The new law affected a wide variety of tax issues, including tax shelters, tax treatment of foreign income, simplified tax forms, capital gains and losses, foreign trade and social security taxes. One key section of the Tax Reform Act of 1976 had to do with the disclosure of tax returns and tax-related information. This section placed restrictions on what information Federal law enforcement agencies could request access to from IRS. It also tightened and made more cumbersome the procedures agencies would have to go through to obtain such information.

The IRS interpreted the new law in a strict manner, sharply curtailing the amount of information it could share within the law enforcement community. Simply stated, the new law had the effect of reducing severely the amount of information the IRS could give to other law enforcement agencies. Added to that was the IRS interpretation of the new law—and that reduced even further the amount of information IRS could share with authorized agencies. For example, some IRS agents believed that if they were to come upon information

[2] Unless otherwise indicated, page numbers in parentheses refer to pages of the printed hearing entitled "Illegal Narcotics Profits."

indicating that a major non-tax crime was being planned they were prohibited from reporting that information outside their own Service. There was a resulting reduction in IRS participation in the Government's effort to collect intelligence on, investigate, prosecute, and otherwise immobilize organized criminals. This decline was viewed with concern by officials in the Department of Justice, in the Federal Bureau of Investigation, the Drug Enforcement Administration, and by some officials in the Treasury Department itself. The decreased role of the IRS was apparent in the Service's declining participation in cases against major narcotics dealers and in the work of Federal organized crime strike forces.

Subcommittee's Interest, Jurisdiction in Federal Drug Enforcement

The Senate Permanent Subcommittee on Investigations has had a continuing interest in the nation's drug problems and in particular in how the executive branch organizes itself to enforce Federal drug laws. It was the Subcommittee's parent Senate Government Operations Committee, now known as the Governmental Affairs Committee, that in 1973 reviewed Presidential Reorganization Plan No. 2, thereby allowing the creation of the Drug Enforcement Administration in the Department of Justice. As part of its continuing oversight responsibility regarding Government organization and efficiency and its jurisdiction in organized and syndicated criminal conduct, the Subcommittee issued an interim report on July 19, 1976 in which it evaluated the effectiveness of the Federal drug enforcement effort. Of primary concern to the Subcommittee in that investigation were integrity issues that had burdened Federal drug control programs for three decades; the methodology used by Federal drug agents whose mission was supposed to be the pursuit of major drug distribution syndicates and their leaders; and allegations that in the three years since the implementation of Reorganization Plan No. 2 the nation's capability to protect its borders against smuggled drugs had been rendered ineffective because of a lack of coordination between the Drug Enforcement Administration and the U.S. Customs Service. In a series of recommendations for corrective action, the Subcommittee advocated stronger internal inspection procedures at DEA to better address the integrity issue; greater focus on interdicting and immobilizing major narcotics smuggling and distribution syndicates, with a corresponding reduction in expenditures for tracking low-level operatives in the drug traffic; and the shaping of a national drug law enforcement strategy that would give appropriate and necessary attention to the border enforcement mechanism. In varying degrees, these recommendations have been implemented by Federal drug enforcement agencies.

BARRIER

It was a matter of deep concern to the Subcommittee, then, when information came to its attention that the disclosure provisions of the Tax Reform Act of 1976, the IRS interpretation of the act and a reported new IRS policy on organized crime and narcotics cases had combined to constitute a barrier to the execution of an efficient, effec-

tive and comprehensive attack on syndicated criminals. Senator Sam Nunn of Georgia, Chairman of the Subcommittee, directed that a preliminary investigation be started into this matter. Senator Charles H. Percy, Jr., of Illinois, the Ranking Minority Member of the Subcommittee, concurred in Senator Nunn's decision.

The preliminary investigation sought to provide the Subcommittee with information on the scope of the drug problem today, and an evaluation of the extent and effectiveness of the effort by the Internal Revenue Service to join in the overall Federal drug control program. The Subcommittee sought to determine to what degree the Tax Reform Act of 1976 may be limiting the ability and willingness of the IRS to work with other law enforcement agencies in combatting the drug traffic. The Subcommittee also sought to assess how efficiently and effectively the executive branch is implementing those features of the Bank Secrecy Act which were intended to help investigators trace the transfer through the banking system of large amounts of money. The movement of money from bank to bank is a device used by organized criminals to conceal illicit profits. This technique of laundering illicit cash was found to be a favorite tactic of major drug dealers.

The Subcommittee's authority to conduct this investigation is derived from section K of Rule XXV of the Standing Rules of the Senate, pertaining to the jurisdiction of the Senate Governmental Affairs Committee, of which the Subcommittee is part, and from Senate Resolution 79, agreed to March 7, 1979. The Subcommittee's jurisdiction includes the authority to investigate all branches of the Government to determine their efficiency and economy. Also, the authority to investigate syndicated or organized crime falls within the Subcommittee's mandate as prescribed in Section 3 of S. Res. 79.

The Subcommittee held public hearings on December 7 and 11–14, 1979.

Senators Open Subcommittee Hearings

In his remarks opening the hearings, Senator Sam Nunn, the Chairman of the Subcommittee, described the proliferation of illegal narcotics as one of the most serious domestic problems facing the nation. He said illegal drug use has been increasing each year to such an extent that there are now indications that some pre-teenagers are users.

Referring to the Subcommittee's recommendations for corrective action in its July 1976 report on Federal drug enforcement, Senator Nunn said, "This Subcommittee has spent a great deal of time over the past four years exploring the narcotics problem and especially the Federal Government's response to it. In recent years, the Drug Enforcement Administration has streamlined its organizational structure, has shifted its enforcement emphasis from small-time street 'busts' to big-time narcotic traffickers, has improved its own internal security, has set more realistic goals for heroin enforcement, and has made strides in improving cooperation with other law enforcement agencies. But there is a lot more that needs to be done" (p. 2).

Senator Nunn said one of the most effective methods of immobilizing big narcotics syndicates is through financial investigations resulting in tax prosecutions or in prosecutions based on other financial violations. The major drug dealers do not come near the narcotics, he

said, so the best way to get at them is through "sophisticated financial investigations which follow the trail of ill-gotten money, and particularly tax evasion cases." That is often the only method of "piercing the veil of secrecy that insulates the top people in most criminal organizations," he said (p. 2).

DECLINE

The Internal Revenue Service once worked with the Federal Bureau of Investigation in bringing organized crime leaders to justice on tax evasion charges, Senator Nunn said. But the Subcommittee's preliminary investigation showed a marked decline in IRS participation with other Federal efforts in organized crime and illicit narcotics cases. He said the number of organized crime cases which originated from IRS-developed tax information had dropped from 620 in 1974 to 221 in the first nine months of 1978.

The Tax Reform Act restrictions on the disclosure of IRS information to law enforcement were a response to the "scandals that came to light a few years ago regarding the use of tax returns by the White House for political purposes," Senator Nunn said, adding that he did not wish to weaken the individual's right to privacy which those provisions of the law were designed to protect. But, he said, it is the Subcommittee's job to evaluate the impact this statute had on Federal law enforcement and to recommend amending the law if necessary (p. 3).

In turn, IRS may have interpreted the Tax Reform Act of 1976 in such a way as to unnecessarily weaken law enforcement efforts in organized crime and drug cases. Independent of the Tax Reform Act of 1976, IRS itself apparently decided to "concentrate the Service's efforts on investigating the average taxpayer rather than big time narcotics traffickers or organized crime figures," Senator Nunn said. "Obviously, the IRS must be aggressive in collecting the nation's taxes from all sources, but I can understand the skepticism of a small town waitress who is caught for underreporting her tips when organized crime millionaires escape without even filing a tax return" (p. 3).

Senator Nunn added, "If the average taxpayer knows that the IRS can successfully collect taxes from the mob, he is a lot more likely to ante up his fair share, if for no other reason than fear of being caught. More likely, the average taxpayer will have confidence in our voluntary tax collection system and feel that his taxes will be well spent, at least on Federal law enforcement activities. On the other hand, if he sees criminals getting away with tax evasion on top of murder and extortion, and narcotics peddling, his natural skepticism towards U.S. tax policy will increase. We will examine these and other problems by concentrating during these hearings on one specific area: illegal narcotics profits and law enforcement response to those profits" (p. 3).

WATERGATE

In his opening statement, Senator Percy, the Ranking Minority Member of the Subcommittee, said the hearings would seek to determine whether the Tax Reform Act of 1976 and policy changes within the Internal Revenue Service had "gone too far in limiting the law enforcement power of IRS." While the Tax Reform Act tax disclosure

section was enacted in response to Watergate, and while the individual's right to privacy must be protected, it is also the obligation of Congress "to make refinements in the law where necessary" in the interests of effective law enforcement, Senator Percy said (pp. 5–6).

Stressing his belief that the nation's tax laws provide a highly effective method for bringing major mob figures to justice, Senator Percy took the occasion of his opening remarks to give a brief history of how Al Capone, the Chicago gang leader, operated, how the IRS succeeded in charging him with tax evasion and how this same effort could be made today against major narcotics dealers. Senator Percy said:

"Drug dealers come in all shapes and sizes. They range from the pre-teen peddler to the transcontinental trafficker. But arresting the street corner pusher, although necessary, will not end the problem. The big money is going to people who never touch the contraband. No matter how effective our drug interdiction program or trafficking laws are, this upper echelon of crime operates with no fear of arrest. Yet, these people, who are orchestrating these illegal operations and gleaning enormous profits, are the very ones we need to put out of business. The key to prosecuting and convicting them rests in the profits they make. They are vulnerable only to the most complex and detailed financial investigations.

CAPONE

"A case in point is one of the Nation's most notorious gangsters. For years, Al Capone dominated the Chicago crime scene, having a hand in bootlegging, gambling, prostitution, and an estimated 200 gangland killings. Yet he had the unique ability to be miles away from the crimes he masterminded. Every school boy knew his face but no prosecutor could touch him. He was indicted several times, once for over 5,000 prohibition violations, but the charges were always dismissed, or the witnesses disappeared. He went to jail in 1931 after conviction for tax evasion, and that was no easy task.

"Capone never maintained a bank account, never signed a check or receipt, never bought property in his own name. He paid for everything in cash out of a strongbox he kept under his bed. IRS went after him on the basis of his net worth and net expenditures. After combing sales records throughout Chicago, including the number of towels he took to his laundry, he was brought to trial on 22 counts of tax evasion. Despite his attempts to have the tax agents testifying against him killed, and to bribe and intimidate the prospective jurors, he was convicted and sentenced to 11 years in prison. It is no wonder that organized crime kingpins have always feared the IRS" (p. 5).

"Federal, State and local law enforcement officials believe that the IRS should be one of the most effective agencies in combatting narcotics traffickers and organized crime. Yet these same officials say the IRS had been virtually eliminated from the fight against crime" (p. 5).

"Our oversight responsibility is to find out why there apparently has been a deemphasis on criminal investigations of narcotics traffickers and organized crime at the Internal Revenue Service, and to do whatever is necessary to rekindle that commitment" (p. 6).

Because many of the illicit drugs that are used in this country—heroin, morphine, cocaine, marijuana and hashish—are grown, harvested and processed outside the United States, the act of smuggling is central to the illegal drug trade. And because of its location, its geography, its 3,425 miles of shoreline on 1,350 miles of coastline, because of the 250 airstrips and because its warm climate and vacation environment attract visitors from everywhere, Florida is the site where the overwhelming majority of marijuana and cocaine are brought into this country. Representing Florida in the U.S. Senate, Subcommittee Member Lawton Chiles urged the Subcommittee to make a special study of the drug situation in his State. The Subcommittee followed his recommendation and received considerable testimony and evidence on the status of the drug traffic in Florida.

WAR

Senator Chiles said in his opening remarks, "The people of the United States and its Government are in the process of losing an undeclared, but very real war. The illegal drug industry is generating around $50 billion a year in untaxed revenues. This makes this industry about the same size as General Motors; $50 billion is more than anyone can contemplate. But I think that we can comprehend what $50 billion in illegal revenue can do to a society. It causes vast damage to our voluntary system of paying taxes. It is used to corrupt our courts and our public officials. It introduces our coming generations to a contempt for society's laws. It certainly causes vast inflation. It diverts badly needed revenues from programs that we could use to help the poor and the sick and the elderly. It strengthens organized crime and it certainly further oppresses the middle class, who end up paying the bill for everything in our society today.

"Sadly, we are not doing much to defend ourselves against the enemy. We must regard the drug traffickers as the enemy. I think we have to forget the image of marijuana as a couple of giggling teenagers behind the high school gymnasium smoking a joint. We are talking about cold blooded killers, and organized crime, an international financial operation which floats billions of dollars from bank to bank around the world. In an 18-month period we had 150 unsolved murders in Miami alone. We have frequent, and sometimes daily reports of innocent people that are killed simply because they happen to be in the wrong place at the wrong time and stumble across some narcotic operation.

"We are sort of fighting with one hand tied behind our backs. The State and local authorities in Florida are out in the street, they are the infantry, they bust mules and the street dealers and occasionally they get a middle-sized hit when they are particularly shrewd or particularly lucky. But this is all we can reasonably expect from our State and local officials. We can't expect that the Sheriff of Polk County is going to be able to trace the offshore banks, the flow of money into offshore banks in the Caribbean, back through Swiss banks and then follow the conversion of the laundered cash as it goes back into legitimate businesses in the United States. That all happens outside of Polk County, which is my home county in the State of Florida,

and mostly outside of the United States. This is the reason why we are losing this war. The State, and local people, the DEA, Customs and Coast Guard, are fighting infantry actions as they try to interdict the flow of drugs through Florida and other coastal States to the rest of the country. But somehow we [need to] have a heavy artillery to fight the rest of the drug cycle, as the drugs are converted into currency and then laundered in banks throughout the world. A heavy artillery certainly is the Internal Revenue Service. What we seek to find through these hearings, as we go into next week, is the reason and an explanation why IRS like Achilles has retired to its tent while the battle is on. Why have the big guns gone silent" (pp. 7, 8)?

Senator William S. Cohen of Maine pointed out that "if the public truly desires more convictions of white collar criminals, public officials need the tools to do the job. The creation of such tools, however, creates a concomitant danger—their abuse by those in power for vindictive, illegal, and unethical purposes" (p. 9). With respect to the disclosure provisions of the Tax Reform Act of 1976 impeding effective law enforcement, Senator Cohen said, "I am one who believes that history does, in fact, swing on the arc of the pendulum, and we perhaps have swung too far in one direction" because of concern for the rights of privacy (p. 84). He cautioned, however, "in our rush to correct our errors, we not abandon those legitimate concerns for the privacy of individuals because of the tremendous power the Federal Government does, in fact, have and the tremendous capability it does have to collect and to disseminate information about private citizens" (p. 85).

II. DRUGS GENERATE BILLIONS OF UNTAXED DOLLARS

Huge Amounts of Money In Drugs

No one knows how many untaxed dollars are generated by the drug traffic in the United States. But experts agree it is large. The National Narcotics Intelligence Consumer Committee (NNICC) is an organization composed of Federal agencies working on the drug problem. Chaired by the Drug Enforcement Administration in the Justice Department, the NNICC, in a report issued in November of 1979, estimated that the retail or street value of illicit drugs in the U.S. was between $44 billion and $63 billion in 1978.

Those are big figures and it is hard to place them in perspective. To give the Subcommittee and the public a less astonishing glimpse at the amounts of money involved in the drug traffic, the DEA brought to the hearing room $3.2 million in $20, $50 and $100 bills. This was the cash seized in a recent narcotics raid by DEA and U.S. Customs agents in Los Angeles. Investigators, assisted by a police dog, seized the cash after drug traffickers had rented an armored car to transport their money. Because the investigation was still going on at the time of the hearing, no further details about the case were provided. But, pointing to the huge stacks of currency before him, DEA Administrator Peter B. Bensinger told the Subcommittee that this money was only the "tip of the iceberg, of the money flow in this very dangerous and damaging traffic" (p. 58).

Also reflective of the vast amounts of money drug violators deal in, Bensinger said, is the equipment they use to keep track of it. With that, Bensinger called the Subcommittee's attention to a currency counting machine. "That machine will count $150,000 in bills in a minute," Bensinger said. "It is used by traffickers because the money is so vast that they really don't have time to count it individually. One organization has been utilizing scales to weigh the amount of cash. Others go into the more specific method of cash counting utilizing the type of machinery that you see right in front of you" (p. 58).

Estimates of Size and Scope of Drug Traffic and Drug Use

Describing the extent of illicit drug use in the United States, the U.S. General Accounting Office in an October, 1979 report painted a picture of widespread violations of the nation's drug laws (exhibit 17, p. 110). Since 1973 at any given time about 450,000 to 500,000 persons use heroin daily. About 7,800 persons died in 1977 as a result of drug use. In 1977 an estimated 1.7 million persons used heroin on less than a daily basis. About 19 percent of the property crimes committed in the U.S. are heroin-related. Heroin is readily available to American soldiers in Europe. Among civilians the use of the hallucinogen PCP

has nearly doubled over the past year and surpassed the use of LSD. PCP is regarded by many medical experts as potentially the most harmful of the commonly abused drugs.

Cocaine and marijuana use has moved from the fad stage and has become accepted by an increasing number of the American people. Cocaine use is increasing. Its use often begins by boys and girls as young as 12 years old. In 1977 it was reported that cocaine was being used by sixth graders in some schools. The public at large uses marijuana more than any other psychoactive drug. About 43 million Americans have tried marijuana and its use has been rising steadily in the past decade. The percentage of young people using marijuana on a daily basis is increasing and is now approaching nine percent among high school seniors nationwide. Average monthly use of marijuana is estimated at one person in 25 for youngsters 12 and 13 years old; and one in seven for 14 and 15 years olds. GAO said the marijuana market consumes between 60,000 and 91,000 pounds a day, resulting in an outlay of $13 billion to $21 billion a year.

GAO said the enormous profits of drug trafficking attract many profit-seekers who see opportunities in the narcotics trade that far outweigh those offered by legitimate businesses.

Availability of Heroin, Cocaine and Marijuana

The NNICC found that heroin availability has been on a downward trend since 1976. Similarly, the street purity—that is, the relative potency of the drug when it finally reaches the user—has declined from 6.6 percent to 3.5 percent. Since 1976, the street price has risen from $1.26 per milligram to $2.25. The NNICC said there were about 380,000 heroin addicts in 1978 compared to 580,000 in 1974, a 35-percent decline. Heroin imports fell 25 percent in 1978 and since 1975 have declined from a high of 7.5 metric tons to between 3.7 and 4.5 metric tons in 1978. The NNICC said that 45 percent of heroin imports come from Mexico, 38 percent from Southeast Asia and 17 percent from the Middle East.

Especially troubling to Government officials are heroin imports from the Middle East. "This year, opium production in Iran, Pakistan and Afghanistan will exceed 1,500 tons—more than 100 times what is likely to be produced in Mexico," DEA Administrator Bensinger testified. He added that Mexico has "political stability and a commitment on the part of the government" to reduce heroin production but "the grave and serious situation in the Middle East today precludes us from even accurately assessing the problem, much less developing solutions" (p. 63).

COCAINE

Nineteen to 25 metric tons of cocaine were smuggled into the U.S. in 1978, an increase of 5 percent over the previous year, the NNICC said, pointing out that virtually all of this supply was derived from leaves harvested from coca plants in Bolivia and Peru. The street value of cocaine in 1978 was between $12.3 billion and $16.2 billion. "According to indicators," DEA Administrator Bensinger said, "cocaine continues to be widely abused and its popularity seems to be accelerating". He said that street prices and purity or potency levels have changed

only slightly over the past three years, indicating consistent availability. The National Institute on Drug Abuse estimated that in 1978 about 6.5 million Americans used cocaine at least once a month (pp. 63, 64).

Bensinger traced the marketing, sale and resale of one kilo of cocaine from the South American peasant farmer who grows the coca leaves to its ultimate destination on the streets of American cities. One kilo or kilogram is equal to 2.2 pounds. The farmer sells 500 kilos of coca leaves for about $250, Bensinger said, explaining that the coca leaves are converted into about 2.5 kilos of coca paste, which sells for $3,000 to $5,000. The 2.5 kilos of coca paste are processed into one kilo of cocaine base, which is sold for $8,000 to $11,000. The one kilo of cocaine base is converted into one kilo of cocaine hydrochloride; this sells for $15,000 to $20,000. On the East Coast of the U.S., the kilo of cocaine nets $38,000 to $40,000. The cocaine has now doubled in value because of the importation into the U.S. Wholesalers cut or dilute the cocaine to 50 percent of strength; the quantity is now sold for $76,000 to $80,000. By the time it reaches the street, the original amount of 100 percent pure cocaine has been cut or diluted to 12 percent of its original purity and it now sells for $800,000. "Considerable profits are involved for everyone throughout the illicit cocaine distribution chain with the one exception, perhaps, of the peasant farmer," Bensinger said (p. 64).

MARIJUANA

The biggest seller of all the illicit drugs on the U.S. market is marijuana. According to NNICC estimates, marijuana accounted for about 35 percent of all income from drug transactions in the U.S. in 1978, and between 10,700 and 16,400 metric tons of the substance were sold here. The National Institute on Drug Abuse said 26.5 million Americans smoked marijuana in 1978, an increase of 10 percent over 1977 (p. 65).

Ninety to 95 percent of the marijuana sold here is smuggled from Colombia and Mexico. The 5 to 10 percent that is produced domestically could increase, particularly if demand should go up for Hawaiian and Northern California marijuana, which is more potent.

Mexico provided virtually all of America's marijuana until the Afghanistan could have dire effects on the American Governments resulted in a drastic reduction of Mexican production. However, Colombia picked up the slack. NNICC estimated that in 1978 Mexican marijuana accounted for only 25 percent of the drug on the U.S. market while Colombia was supplying about 70 percent (pp. 65, 72).

About 10 percent of heroin, cocaine, marijuana and other illicit drugs in the U.S. are seized by Federal, State and local law enforcement agents. In April, May and June of 1979, DEA agents seized one pound of opium, 105 pounds of heroin, 311 pounds of cocaine, 598,777 pounds of marijuana, 43,478 pounds of hashish and 7.1 million dosage units of dangerous drugs, Bensinger said, reminding the Subcommittee that these figures reflect DEA confiscations only.

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Assessment of Southwest Asian Heroin Supply

In his December 7, 1979 appearance before the Subcommittee, DEA Administrator Bensinger warned that increasing opium production in the Southwest Asian countries of Iran, Pakistan and Afghanistan could have dire effects on the American Government's ability to control heroin smuggling and use in the United States. But, Bensinger said, DEA did not have enough information about Southwest Asian heroin to be very specific in its assessment of how serious a problem it posed at that time.

In January of 1980, after the Subcommittee hearings ended, DEA did make an assessment of the impact of Southwest Asian heroin on the U.S. In a report, "Southwest Asian Heroin Intelligence Assessment," DEA said that opium production in Iran, Pakistan and Afghanistan is proving to be highly lucrative to heroin traffickers. Heroin from Southwest Asian opium is being smuggled into Western Europe and the United States in ever increasing numbers. This heroin, DEA said, is more potent—and thus more rewarding to users—than heroin currently available. DEA said that for the first time in three and half years heroin purity is moving upward.

The DEA report said Southwest Asian heroin is not only potent; it is also abundant. Total illicit opium production in Iran, Pakistan and Afghanistan was estimated to be 1,600 metric tons in 1979. An annual production of only about 80 metric tons of opium from Turkey was responsible for the heroin traffic to the U.S. in the 1960's and early 1970's, DEA said, pointing out that this traffic serviced an American heroin addict population of more than 700,000.

OPIUM

The DEA report said the vast supplies of high quality heroin produced from Southwest Asian opium could become pre-eminent in the U.S. and Western European market in the 1980's. Because of its availability and high purity, this heroin could lead to increased heroin use in the United States and more addicts, DEA said. Southwest Asian heroin began showing up in New York City and Washington, D.C. in significant amounts in 1977 and 1978 and by 1979 was being used across the country.

Southwest Asian heroin has had a dramatic impact on West Germany, according to DEA. The West Germans did not have a serious heroin addiction problem until 1974 when Southwest Asian heroin was brought into the country. By mid-1979, DEA said, there were 60,000 to 80,000 heroin addicts in West Germany. Heroin overdose deaths increased from nine in 1969 to 378 in 1978 and to 601 in 1979, DEA said. The 1979 West German figure represents 9.69 deaths per million population. This is six times greater than the present U.S. heroin overdose figure of 1.64 deaths per million, DEA said.

Smugglers' Routes and Methods of Entry

With the exception of Hawaiian and Northern Californian marijuana, which accounts for no more than 10 percent of the total supply, all heroin, cocaine and marijuana are grown and harvested over-

seas. Consequently, the first crime that is committed in the marketing of drugs in the U.S. is the Federal crime of smuggling.

Bensinger, whose Drug Enforcement Administration shares responsibility for controlling drug smuggling with the U.S. Customs Service, said Southeast Asian heroin is smuggled into this country either by way of Western Europe, mainly through the Netherlands, or directly into the United States, generally to the West Coast. Until late 1978, Bensinger said, about 75 percent of the Middle Eastern heroin came into the U.S. by air (p. 64). Today sailors onboard Turkish flag vessels bring in increasing amounts. One common smuggling method—used for both Southeast Asian and Middle Eastern heroin—is to have air travelers carry the drug or to stash it in air freight. It is also smuggled in by crew members or concealed on ocean freighters. A small amount of Southeast Asian heroin enters the U.S. by land from Canada. Bensinger said Mexican heroin is usually transported across the border in cars and trucks (p. 64).

Half the cocaine smuggled into the U.S. comes by air, 30 percent by ship and 25 percent by overland route across the Mexican border, Bensinger said (p. 64).

TRAFFIC

As for marijuana, Bensinger said, "We have every reason to believe that Colombian marijuana will continue to be preeminent in the United States. The heavy air and sea traffic will continue, and it is likely that there will be further establishment of the trend toward long-range air transportation. The large volume of seizures during 1977 and 1978 have caused the smugglers to modify their methods of operation. Thus, although the traffickers will, no doubt, continue their maritime operations, they are expanding away from Florida north along the Atlantic Coast and west along the Gulf Coast. To a far lesser extent, motherships are departing from Colombia's Pacific coast to the U.S. west coast. Colombian motherships are also utilizing the Bahamas and other Caribbean Islands as transshipment points in order to avoid apprehension in what some traffickers feel are less secure waters closer to the United States. Mexico, and Central America may be used increasingly as transshipment points for South American drugs destined for the United States. Mexican trafficking organizations are capable and ready to smuggle drugs into this country. Just over 50 percent of all Mexican marijuana smuggled into the United States is transported via single engine all-purpose aircraft destined for clandestine runways or airdrops over the Southwestern United States. A smaller amount is smuggled overland, either through established ports of entry or through illegal crossing points. Jamaican marijuana is smuggled into the United States by both sea and air" (p. 65).

Additional information on smugglers' routes and methods of entry was given by Robert Asack, Director of Customs Air Control for the U.S. Customs Service. Asack said ships carrying marijuana to Florida and elsewhere in the Southeastern U.S. usually start out from Guajira on the north coast of Colombia (p. 132). The ships either sail directly into Florida ports or hover off the coast from 50 to 100 miles out and from there they transfer their cargo to smaller vessels which ferry the illicit drugs to shore. Transit is through the Yucatan Passage, the

Windward Passage or the Mona Straits between Puerto Rico and Hispaniola, Asack said (p. 132).

"NIGHT TRAIN"

A 100-foot vessel, Asack said, is capable of carrying more than 50 tons of marijuana, while a 400-foot freighter may carry 100 tons of marijuana. One vessel, the *Night Train*, evaded Customs and Coast Guard spotters for two years, becoming "almost mythical" in its ability to escape detection, Asack said. The *Night Train* was finally caught in the northern Bahamas, carrying a 50-ton, $30-million marijuana load, Asack testified. He said smaller fishing boats, unable to transport more than one or two tons of marijuana, are often used to ferry loads of marijuana ashore from the bigger motherships. A ton, sold at wholesale rates, would be worth $600,000, Asack said. He said the skipper of one such fishing boat was bold enough to sail up the Miami River past the U.S. Customs office with a load of marijuana before authorities arrested him (pp. 132, 133).

Some of the smaller boats used in the ferrying operation are capable of speeds up to 50 miles an hour and are faster than anything the Coast Guard has to pursue them, Asack said (p. 133).

In the instance of the *Maya*, a banana boat that sailed to Miami regularly, authorities discovered 157 pounds of cocaine in the hold. Referring to that seizure, Asack said, "We are talking street values that are incredible." He said that the cocaine was probably stashed on the *Maya* by a crew member and without the knowledge of the boat operator (p. 134).

JAILS

Along with private aircraft designed for business travel such as the 601 Aerostar, the Cessna Titan and the Cessna Citation, smugglers also used the DC–4, a bigger airplane that can fly with 15,000 pounds of marijuana with a wholesale value of $4.5 million, Asack said (p. 134). One DC–4, which brought in a $4.5 million marijuana shipment, was being leased for $22,000 a month but once they landed it and unloaded, the pilot and crew abandoned the aircraft, Asack said. DC–3 aircraft are also used in dope smuggling, he testified (p. 135).

Pilots are reluctant to fly over Cuba and smuggling ships do not often stray into Cuban waters, he said, explaining the Cubans "are very harsh on drug smugglers and those folks that go down into Cuba are in for hard jail time, with limited rights" (p. 134).

Because of the great profits to be gained from drug smuggling and the increasingly effective air detection equipment used by the government, pilots take risks in the air they might not take otherwise. ". . . we have a large percentage of folks that fly very, very low in the dark without lights, attempting landings on short strips and extending their fuel ranges and they often come to grief," Asack said (p. 136).

Richard J. Davis, Assistant Secretary of the Treasury, said the law of *posse comitatus*, which prohibits the active participation of the U.S. Armed Services in civilian pursuits under ordinary circumstances, is a "well based and important principle," one that he "would be very cautious" about changing. But Asack said the law could be

amended in such a way as to enable the military to detect and track civilian aircraft that are not considered hostile but which are suspicious nonetheless and then notify Customs of their position [2] (pp. 136–137).

Impact of Drug Traffic on Florida

"Through an accident of nature and geography, Florida has become an international port of entry for most of the illicit drugs entering the United States. . . . We now accept as fact that the drug business is, indeed, the biggest retail business in Florida" (pp. 157, 171). These were the statements of Jim Smith, the Attorney General of Florida, who testified before the Subcommittee on the impact of illicit drug trafficking in Florida.

As Smith called the drug trade the biggest retail business in the State, Florida Department of Law Enforcement Commissioner James York, told the Subcommittee just how big—and corrosive—this industry is. York said the estimated gross value of the marijuana and cocaine trade in Florida in 1978 was more than $7 billion. He said $6.5 billion was in marijuana while cocaine accounted for $500 million. He said 1979 figures would be even bigger, particularly regarding cocaine. When any illegal pursuit becomes so large, York said, it generates corruption, social reordering and violence. He cited Florida's murder rate as reflective of the impact of the drug trade. The State reported 786 murders in the first nine months of 1979. Of these, he said, 41 were directly related to illegal drug trafficking. In Dade County, which includes Miami, 244 of the 786 murders occurred. York said that, while Dade County accounts for 16.7 percent of the State's population, it recorded 31 percent of the murders. He said 27 of Dade County's murders, or 11.5 percent, were drug related (p. 167).

CORRUPTION

Murder is but one crime spawned by the illicit drug trade. York said Florida police have had to investigate and arrest officials at all ranks of Government in Florida, from lower echelon workers up to circuit court judges, in drug cases. He said that he expects continued instances of official corruption as long as there is an abundance of profits from drug dealings. Corruption spills over into the private sector as well, York said, citing examples of businessmen who charge exorbitant prices for private aircraft sold for the purpose of smuggling. Similarly, the fishing and seafood industries, with their direct and frequent accessibility to docking areas, are vulnerable to corruption, York said. "So, I think it is obvious that the corruption problem, and the violence problem will continue to escalate with the huge amounts of uncontrolled cash flow involved," York said (p. 171).

Attorney General Smith said Florida, with its thousands of miles of shoreline, is "a smuggler's paradise," an easy destination for ships and aircraft carrying contraband drugs from Central and South America and the Caribbean. The traffic has become so massive that

[2] For a discussion of the *posse comitatus* statute, see Chapter V of this report.

police despair of stopping or substantially reducing it. "For every pound of contraband seized nine pounds get through," Smith said. "The result is a torrent of narcotics coming into the State that has overwhelmed the ability of authorities to dry it up. We don't feel that we have even significantly slowed it down." Marijuana and cocaine and other illicit drugs are brought into Florida in great quantities, Smith said, but only a portion remain there. These drugs are used throughout the nation, he stressed, making the problem national in scope. Florida cannot begin to cope with this problem alone, and it should not have to. "The sellers of addiction, dependency and wasted promise observe no State boundaries in the search for customers," he said. "When the Comptroller General [of the United States] described Florida as a 'drug disaster area' in a recent report to Congress, I assure you he was not exaggerating. We need the help of Congress and the commitment of the Federal Government in this disaster as much as we ever needed it to recover from the ravages of a hurricane. In many ways, this is a more serious threat. We can always rebuild our shattered homes. It is a great deal more difficult to renew shattered lives" (p. 158).

PROFITS

Smith said profits from the drug trade are so large that smugglers can afford sophisticated radio equipment—some of it capable of intercepting police radio calls—for their aircraft and ocean vessels, and, he said, they can pay their workers sufficient sums of money to motivate them to assume the risk of arrest (p. 161). Commissioner York provided a breakdown of how the money is distributed on an illicit drug venture. One drug organization was found to be bringing into the United States one to three loads of marijuana a week. Each of the loads averaged 40,000 to 80,000 pounds. York said the importer who was dealing with the drug organization paid about $40 a pound for the marijuana in Colombia. The importer then sold the marijuana for $115 a pound once the marijuana had been smuggled into the United States and stashed in a warehouse. The marijuana was then sold for $215 to $315 a pound in minimum lots of one-half ton, the price depending on the quality of the marijuana and the terms of the sale, York said. He said that the importer of the drugs has been grossing about $7 million a month while the syndicate supplying the marijuana has taken about $200 million out of the United States. At the lower end of the smuggling venture, York said, were the off-loaders who received $10,000 to $15,000 for one night's work in unloading a boatload of marijuana. Aircraft pilots who flew to Colombia and back with loads of marijuana were paid $50,000 to $100,000 for a round trip, York said (pp. 168–169).

With so much money involved, operatives in these drug ventures are willing to accept the risk of capture. And occasionally they are caught. When that happens, Attorney General Smith said, drug couriers and others involved in the drug trade are defended by capable, high-priced lawyers who know how to win dismissals and acquittals and reduced sentences. "Bail in six figures is posted routinely and willingly forfeited," Smith testified. "In many instances, lawyers are waiting at booking desks when the defendants arrive. These expenses are readily accepted as a cost of doing business" (p. 161).

MURDER

Should a drug violator receive a prison sentence, his family may be paid $2,000 to $3,000 a month for the entire time of his incarceration, said Commissioner York. He said these prisoners have been assured by higher-ups in the drug trade that their families will be well taken care of while they are in jail (p. 161). These kinds of assurances guarantee that drug smuggling will continue to attract job seekers, particularly Latin Americans who are very poor to begin with. Colombians frequently work in the dope traffic, Attorney General Smith said, adding that murder, a commonplace occurrence in the narcotics business, happens so often to Colombian drug dealers and smugglers that it is said of them: "Colombians are like Dixie cups. You use them once and throw them away" (p. 158).

Smith went on to say that profits are so plentiful in the Florida drug trade that money often is no object. Violators know no limits in what they will spend to keep their business going. Smith told of one trial in which accused drug dealers offered to pay a million dollars to disrupt their trial by bribing a juror, murdering a witness and "perhaps even murdering the Federal district court judge" (p. 162). Smith said drug dealers and their associates carry hundreds of thousands of dollars around in cash in suitcases; but they do not hesitate to leave their cash behind, along with huge amounts of expensive narcotics, and flee at the first sign of police presence. One drug defendant in a South Florida trial spoke seriously of paying $20 million to take control of a small Central American nation, Smith said (p. 162). So lucrative is the drug trade, Smith said, that it is common for police to find private airplanes abandoned at clandestine rural airstrips, left behind by spendthrift smugglers who figure the expense of a new plane as part of the cost of doing business.

CASH

What Smith called "the unbelievable flow of cash" into Florida banks was documented by testimony and exhibits from Irvin B. Nathan, Deputy Assistant Attorney General in the Criminal Division of the U.S. Department of Justice (p. 162). Nathan said that in 1978 the Federal reserve banks in Florida reported a cash currency surplus of more than $3.2 billion. This figure represented 77 percent of the entire Federal reserve currency at that time, Nathan said, explaining, "What this means is that all other Federal reserve banks throughout the country have money flowing out that needs to be replaced, but in Florida, money—cash in small denominations—is flowing into those banks in tremendous quantities so that there was a $3.2 billion surplus" (p. 19).

Elaborating on that point, Florida Law Enforcement Department Commissioner James York said that during the past three years cash receipts at the Miami branch of the Federal Reserve System increased 83 percent from $1.4 billion to $2.7 billion. York said large cash deposits totalling $950,000, mostly in $20 bills, had been brought into banks in Miami in bags, boxes and suitcases by casually dressed young men who refused to show any identification. York said millions of dollars of cash had been transferred from South Florida banks to ac-

counts in Panama, Switzerland, the Bahamas, Venezuela and the Cayman Islands (p. 168).

Florida Attorney General Jim Smith said much of the money coming into Florida in the drug trade ends up in the legitimate economy of the State. "The hidden power of these dollars is frightening," he said. "They represent an enormous potential for bribery, corruption and economic harm to legitimate business through anti-competitive activity" (p. 162). That point was endorsed by Commissioner York, who said drug traffickers enjoy a continuous and positive cash flow that gives them a decided edge over their competition in reputable business pursuits.

VALUES

The transfer of funds from the drug traffic to the legitimate economy shows up vividly in the housing market in Florida where land values reflect a massive infusion of new money. Charles Kimball of Miami is an economist and a real estate analyst, whose clients included major banks in New York and Florida as well as large homebuilding firms. Kimball has made many studies of the impact of drug money on housing costs, starts and trends, and at the request of Senator Nunn, Chairman of the Subcommittee, Kimball was given access to certain law enforcement information which was of assistance to him in tracing investments by organized crime and drug traffickers in the Florida area. Kimball told the Subcommittee that the degree of foreign investment in Florida is so significant that parts of the real estate economy are becoming increasingly dependent on funds from overseas sources (p. 184). Vast amounts of that foreign investment is from the narcotics trade, Kimball said. He added, "Obviously, if we were to cut off the narcotics money coming into the State of Florida, we would precipitate a substantial real estate recession in many parts of the State. Many large condominium projects that are under construction would end up in foreclosure and there would be a collapse of some real estate markets, certain types of investment properties. If the prices would fall substantially and many people who would innocently invest in such properties would be hurt because they went along with the prices, the inflated prices generated by this type of investment on their own and the prices of many types of properties would fall. It would not be a pleasant thing to look at" (pp. 195–196). Kimball said that if all the narcotics money were removed from the Florida economy, the State would suffer but it could recover. However, he said, if the infusion of illicit funds continues at present rates for 10 more years, the State will be economically dependent on this source of money.

Kimball said that in 1969 foreign investment was well below 5 percent of the total dollar volume in Florida real estate (p. 183). But in 1971 and 1972, there was a substantial increase in foreign purchases of real estate (p. 183). Kimball worked on a study, commissioned at the request of the Internal Revenue Service and the State of Florida, that showed considerable amounts of narcotics and organized crime money in the foreign investment, much of it by offshore corporations. This trend accelerated, Kimball said. In Dade County, where Miami is located, 40 percent of all real estate transactions of $300,000 or more are made by offshore corporations or foreign entities (p. 184). In Broward County, where Fort Lauderdale is located, the rate of for-

eign investment is growing rapidly and represents 25 percent of all real estate deals (p. 184). By the end of 1979, Kimball said, more than $1.5 billion in Broward County properties will have been bought by foreign concerns (p. 184).

NETWORK

"Staggering" was the word Kimball used to describe the amount of investment that organized narcotics dealers initiated in Florida since about 1976 (p. 185). They put their money into all manner of income producing properties—apartments, shopping centers, office buildings and warehouses. Serving the drug trade investors well is a network of attorneys, accountants, brokers and other professionals, who, working out of offices in Fort Lauderdale, Miami, Miami Beach, St. Petersburg and Tampa, manage the investments of organized crime syndicates and narcotics dealers. All the studies he has read indicate to Kimball that the wealth generated in terms of investments by narcotics dealings in the last two or three years in Florida has easily well exceeded all previous investment activity by organized crime in Florida since 1960 (p. 185). It is Kimball's estimate that the total amount of investment in Florida from illicit narcotics revenues equalled $2.5 billion in late 1979 (p. 186).

Corporations and other entities based in the Netherlands Antilles, Cayman Islands, Panama, Liechtenstein and the Guernsey Islands enjoy a privileged tax status because of legislation and treaties between those countries and the United States. The entities pay no taxes on capital gains made in the U.S. These entities have made $240 million in acquisitions in Dade County and Broward County in a recent six-month period, Kimball said (p. 186). These corporations are allowed to operate in virtual secrecy in the countries of their origin, making it difficult to find out where their funds come from and who owns them. Kimball said it is difficult to identify the true stockholders of these entities. And because they have a privileged tax status with the United States, the countries where they locate enable the firms to profit while paying little taxes, Kimball said. Criminals invest heavily in these firms, he said, to avoid paying taxes and to avoid the possibility that someone might be able to determine where the investors' money comes from. Kimball said the U.S. Government should revoke the privilege these countries have of paying no capital gains on profits earned in America. He said the United States is such a sound investment usually that no legitimate foreign investor would be hurt by having to pay taxes here on his earnings. In addition, Kimball asked, why should foreign investors be given a privilege not given to ordinary American citizens? (P. 186.)

BISCAYNE

As their funds show up more and more in reputable businesses, narcotics dealers can be expected to exercise increasing political strength, Kimball said. ". . . these very professionals who on the surface seem to be legitimate businessmen can contribute heavily to certain political campaigns for their own nefarious purposes," Kimball said (p. 189).

Money from narcotics transactions is plentiful in Florida, Kimball said, so plentiful that it has forced up the cost of real estate. "To buy an existing condominium today on Key Biscayne, if someone comes

along, he has to pay a premium because of the fact we permitted these markets to be taken over by this hot money that comes into the country," Kimball said (p. 189). He cited a large building in Coral Gables that was bought by foreign investors who were willing to make a large down payment and to realize a one-percent return on the building because their goal was to make legitimate their money, not necessarily to show a decent profit. No prudent American investor can compete in such a market, Kimball said. The impact of the drug money hits not only the legitimate competitor who must realize a real profit; but also adversely affected are ordinary consumers who will have to pay higher prices for goods and services. "If the doctor has to pay more for his office, or a warehouse which keeps brooms in the warehouse has to have higher rent because of this type of inflation, you can begin to see the impact on every citizen, not only in the State of Florida, but wherever this type of trafficking investment goes on," Kimball said (p. 190). Kimball said the impact of narcotics money has inflated the cost of the average home in South Florida by $2,000 (p. 189).

Narcotics money is invested in all manner of enterprises and all investments are designed to cleanse or launder the illicitly gained funds, Kimball said. Ultimately, however, the narcotics money investor returns to real estate, for nowhere else can he find such a convenient way to launder his cash, Kimball said. He testified that in 1979 a plot of land that was sold to a Netherlands Antilles firm in 1976 for $3 million was sold for $12 million in cash. Every aspect of this sale, beginning with the $600,000 down payment check, was handled through foreign banks and foreign entities—and not a cent of it was processed in Florida banks, Kimball said (p. 190).

FRONTS

He described an instance in which two men combined their reported resources to buy $45 million in new shopping centers and office buildings in Broward and Palm Beach Counties. Kimball said one of the men was an associate of "the previously identified major fronts of organized crime investment, one of the Meyer Lansky group." The other man was connected with an organized crime-controlled corporation that was $1.3 million behind in Federal taxes. Further inquiry revealed that the two men were not the true principals in the acquisitions but instead were fronting for an enterprise located in Liechtenstein. "They were simply holding points in the traditional criminal sense," Kimball said, adding that if the two men ever tried to claim the properties for their own use "they would probably disappear." Later in the inquiry authorities identified eight Latin American men who were the actual owners of the properties and two of them were "discovered to have definite connections with narcotics fronts," Kimball said. This organization has purchased properties in Florida worth more than $150 million, Kimball said. One of the eight men connected with this syndicate was arrested in the fall of 1979, not in connection with drugs, but while transporting several million dollars in stolen securities. His involvement in stolen securities, Kimball said, demonstrates that "the type of people that are being utilized for this foreign investment activity have substantial experience in every other type of illicit activity that goes on in this country, and they cannot be restrained from

financing through their profits . . . additional criminal enterprises of every kind" (pp. 191–192).

Kimball said criminals profiting from the drug trade are not only breaking smuggling, currency and narcotics laws; but they are also benefiting from the American tax system which they have figured out how to circumvent. First, Kimball said, criminals pay no taxes on their illicitly gained profits. Next they take their money out of the nation and invest it in tax sheltered corporations in offshore countries. These offshore entities frequently invest their money in American enterprises, which enables the criminals to launder their profits. As a result, there is a circular flow of money from drug traffickers in the United States to offshore entities and back to the United States—with very little of this money being taxed.

In doing his analyses of major organized crime and narcotics business investments in Florida, Kimball relied on public documents. He said these documents are available to anyone who wishes to read them. He was critical of the Internal Revenue Service for not doing more studies of such transactions.

GAO Reports On Florida Drug Situation

In a report issued October 25, 1979, the United States General Accounting Office discussed the drug situation along the Southeast border of this nation. The report, entitled "Gains Made In Controlling Illegal Drugs, Yet The Drug Trade Flourishes," termed the Southeast border region, particularly Florida, a "drug disaster area." The report is generally supportive of the testimony given the Subcommittee by Florida Attorney General Jim Smith, Florida Commissioner of the Law Enforcement Department James York and Miami economist and real estate analyst Charles Kimball.

GAO said drug smuggling in the Southeastern United States had become a major business in recent years. Tonloads of marijuana and hundreds of pounds of cocaine are regularly shipped into this region for distribution throughout the nation. Billions of dollars in income is earned by violators, GAO said, but none of it is taxed and significant amounts of the money are taken to foreign countries.

Law enforcement agencies are overwhelmed by the drug traffic, GAO said, adding that police are not aided by the fact that U.S. law generally does not make it illegal for Americans to possess drugs on the high seas. Nor is the law enforcement effort enhanced by the lack of international agreements to deal with large ships carrying drugs beyond the 12-mile limit, GAO said.

TARGET

While Florida has been a target for drug smugglers for many years, the State became the pre-eminent gateway for drugs when Mexico declined as a marijuana exporter. The success of the eradication program in Mexico has resulted in increased use of Colombian marijuana while U.S. demand for cocaine, grown chiefly in Peru and Bolivia, has increased, GAO said.

As drug smuggling has increased in Florida and elsewhere in the Southeast United States, so have drug seizures, but the significance of

these seizures is debatable. GAO said that during a six-month period in 1978, the U.S. Coast Guard, Customs Service and Drug Enforcement Administration reported seizures of 477 tons of marijuana and 359 pounds of cocaine. In the same period, GAO said, the Colombian authorities seized 610 tons of marijuana. DEA said these seizures represented more drugs than were seized by Federal law enforcement agencies for all of 1977. Other law enforcement agencies found little to be encouraged about in these big seizure statistics, telling GAO that the size of the confiscations indicates just how massive the smuggling trade is. Conversely, GAO said, the U.S. Justice Department, acknowledging the increasing magnitude of the drug traffic, interprets the confiscation statistics as evidence of improved cooperation among law enforcement agencies. Justice Department officials also say the percentage of marijuana being seized, destroyed or abandoned at sea may be more than 20 percent of the entire volume intended to be shipped into the U.S.

GAO quoted law enforcement officials in Florida to the effect that the drug situation "is completely out of control." Large mother ships carrying tons of marijuana remain beyond the 12-mile limit and transfer their cargo to smaller vessels which ferry the contraband to U.S. shores.

VESSELS

GAO endorsed legislation that would make possession or transfer of illicit drugs on the high seas by American subjects against the law. The measure, HR 2538, passed the House and was before the Senate at this writing. But, GAO said, while this bill could help the enforcement effort, a separate difficulty then emerges that most mother ships carrying massive hauls of dope are either foreign registered or stateless. The U.S. Coast Guard has blanket authority under international treaties to board stateless vessels. But in the case of foreign ships the Coast Guard must seek permission of the vessel's country of origin before boarding, searching and taking appropriate action. This process is time consuming, GAO said, and since international treaties ordinarily do not deal with this issue, the affected nations will have to resolve it. "Otherwise, the mother ships will continue to operate," GAO said.

Concluding its comments on the Florida drug situation, GAO said, "It is obvious that our Southeast border has not been controlled effectively. The Congress has recognized the problem, and the administration has taken some steps to strengthen drug enforcement in the area, including application of additional resources and the creation of joint enforcement task forces. While it is too early to assess the impact of these actions, the problem is not likely to go away. To improve the effectiveness of our present resources at U.S. borders, an integrated management plan is necessary."

IRS Help Is Requested in Florida

Witnesses testifying about Florida's problems with the narcotics trade and its ramifications in the State's economy urged greater involvement by the Internal Revenue Service in law enforcement work

there. Charles Kimball, the economist and real estate analyst who described how narcotics money is invested in legitimate business, said so much of the illicit narcotics funds are invested for the purpose of avoiding taxes that the IRS could make a major contribution to Florida's efforts to control this activity. He said the dollar return to the U.S. Treasury would far outweigh the cost of expanding IRS participation.

Similarly, Jim Smith, the Florida Attorney General who described the extent of drug traffic in Florida, also had some comments about IRS, several of them critical. Smith said in a number of narcotics cases the IRS has helped Florida police but in others the IRS has not only refused to assist but has not even been cooperative. "Lack of such cooperation, and a lamentable absence of communications and cooperation among Federal agencies themselves, are the chief frustrations of our State and local law enforcement agencies," Smith said. "It is particularly frustrating to know that an agency such as the Internal Revenue Service has information that could lead to criminal prosecutions, but is unable to share it. It is the ultimate irony when two Government agencies, presumably with a common goal, engage in competition that discourages harmony of purpose" (p. 164). Smith said the Congress should direct IRS to cooperate more with law enforcement agencies trying to make drug cases. He said Florida authorities have "absolutely unpicked vineyards" of investigative opportunities just waiting for tax evaluation by experienced IRS agents. No one can better understand the complex financial dealings of the narcotics syndicates than the IRS, he said (p. 174).

Smith's comments were seconded by James York, the Commissioner of the Florida Department of Law Enforcement. State and local investigators in Florida, no matter how experienced, are not as capable in financial inquiry as are IRS personnel, York said. He testified that "IRS is decades ahead of us. They have the expertise, they have a proven track record. It is very frustrating that they are not able to use it" (p. 174).

The Impact of the Drug Traffic on Colombia

The Subcommittee received testimony and exhibits on the changes that have occurred in Florida since that State became the major gateway for illicit drugs entering the United States. The Subcommittee also sought information on what happens to the nation that produces and then ships to the United States large amounts of drugs. The country of Colombia, a nation of 18 million population in northwestern South America with coasts on both the Caribbean and the Pacific Ocean, is the principal supplier of marijuana to the United States, providing about 70 percent of the American market. Colombia is also the major processor of cocaine for the American market. Processing the coca leaf compounds shipped to them from Peru and Bolivia, Colombians produce about 70 percent of the cocaine smuggled into the U.S. The combination of marijuana and cocaine have brought billions of dollars to Colombia. To find out how these new riches have affected Colombia, the Subcommittee turned to the U.S. Ambassador to Colombia, Diego C. Asencio, who made very clear his feelings on what the drug traffic has done to Colombia. He told the Subcommittee, ". . .

Colombia has been facing a severe economic challenge from narcotics traffickers. The integrity of its financial institutions has been placed in jeopardy. A growing inflation rate has been accelerated by illegal monies. Legitimate business enterprises have had to defend themselves from absorption by criminals. Land values, both agricultural and residential, are soaring, leaving farmers and middle-class home buyers in a quandry. The spector of corruption remains ever present. The very bases of the political power structure has been challenged by criminals" (p. 205).

PESOS

Expressing skepticism about the reliability of statistical estimates of the drug trade, Asencio testified that there were "credible estimates" indicating that Colombia's narcotics trade for 1979 would be more than $3 billion. This figure he said, included dollar holdings by Colombians in foreign banks, dollars circulating in the reported $800 million Colombian black market and those dollars converted into pesos in Colombia, transactions which reportedly totalled $700 million. He cited estimates that 100,000 Colombia families are involved in the drug trade, including growers, transporters and "the Mafia families" (p. 203).

Even though the 1970's saw Colombia's role in the drug traffic grow rapidly, the public perception was that the problem was one for the North Americans to worry about and not them, Asencio said, adding that the new President, Julio Cesar Turbay-Ayala, was able to focus media attention on the narcotics issue and since the time of his inauguration in 1978, the Colombian people have come to view this problem as a threat to their country too. "This new perception was strengthened by the awareness of the vast sums of money involved, the huge profits to traffickers, the corruption of public officials, the growth of an illegal economy outside the power and taxation of the government, the temptation to legitimate sectors to become peripherally involved in the profits and the impetus to inflation caused by the influx of illegally gained funds," Asencio said (p. 202).

Profitable coffee prices and other legitimate exports have helped Colombia achieve its highest foreign exchange reserves—$3.8 billion—but, Asencio said, "part of it is derived from drug sources." These new monies can bring financial disarray to the nation, freeing "extremely large amounts of uncontrolled cash circulating in Colombia's free market economy," he said (p. 202).

Asencio said Colombia's inflation rate is 30 percent—and that 4 to 6 points, in the opinion of Colombian economists, is caused by the drug trade. Government fiscal policy, seeking to control inflation through the money supply, is hampered by the existence of the parallel economy made up of drug profits. Asencio explained, "It must be realized, of course, that there are many factors impacting on the growth of the money supply. What is peculiarly disturbing about the illicit narcotics earnings, however, is that they are largely out of control of the monetary authorities in the first instance" (p. 203).

AFFLUENT

A new class of affluent people, made rich from the drug trade, has caused a distortion of traditional values and undercut the people's

trust in their government's ability to control inflation. ". . . the new criminally wealthy consume conspicuously and flaunt their wealth," Asencio said. "This exacerbates the perception of income maldistribution which in turn increases demand for higher taxes and wages." This has been apparent in housing, he said, where narcotics money has tended to force up construction costs, created fresh demand for luxury units and, in turn, tended to reduce the availability of middle- and low-income housing. Consequently, the Ambassador testified, Colombia, a poor country, has a boom in luxury housing construction and, at the same time, a downturn in middle- and low-income housing starts (p. 204).

Inflation, intensified by the drug traffic, has led the Colombian government to reduce spending on needed public programs. Asencio said the "Government has had to hold back on public sector investment, education, health, other social needs and the infrastructure that any developing country needs and the fact that the principal instrument to control inflation is to restrict credit, has to hurt the average Colombian" (p. 208).

INFLUENCE

Large tracts of agricultural land are being bought up by the criminally wealthy, Asencio said, and they tried, and nearly succeeded, to buy controlling interest in Colombia's third largest bank. Their influence extends into politics where in the parliamentary elections of 1978 veteran Colombian Congressmen were surprised to find themselves challenged by unknown candidates with apparently unlimited financing. "This, needless to say, caused a profound and probably healthy shock," Asencio said (p. 205).

The power, resources and corruptive potential of the Colombian drug dealers was seen in a raid conducted by the Colombian national police on cocaine laboratories in Bogota last September. Asencio said a world record amount of 580 kilograms of cocaine was seized. The value of this much cocaine sold on the streets of the United States was estimated to be equal to Colombia's national budget for two years. Asencio said the 21 national policemen who conducted the raid were offered bribes totaling $500,000 to desist (p. 205).

Asked what would happen to the Colombian economy if the drug industry were shut down, Asencio said, Colombia is enjoying good coffee prices now so the dependency on drugs is not substantial. But, he added, "I have had sort of a nightmare in the back of my mind that at some point if the price of coffee should drop precipitously, the economy may indeed become dependent on narcotics income and I would like to get them out of there before that happens" (p. 212).

BAIL

Asencio said Colombians resent being accused of corrupting American youth through the drug traffic. He said many Colombians believe the U.S. is not committed to controlling the drug trade at home. He said low bails and other features of the criminal justice system in this country show that the U.S. is not really serious about solving its own drug problem, according to many Colombians' point of view.

Another observation about the Colombian drug situation was offered by Florida Attorney General Jim Smith, who toured that South American country in September of 1979 on a fact-finding trip. Smith testified that he saw vast rural areas of Colombia where there was little government control and marijuana is grown openly and with impunity. He said Colombia has a centuries old tradition of smuggling, that Colombian smugglers are experts at their trade and that is an important reason why cocaine and quaalude processing operations have been located in Colombia.

Asencio, Smith and Commissioner York all testified that Colombian President Turbay is making a sincere effort to lead his country out of the narcotics business.

Why People Get Started in the Drug Trafficking Business

Not everyone in the drug trafficking business fits the conventional stereotype of the hardcore criminal. Many people who had previously led law-abiding lives have become mixed up with the drug trade. Stewardesses and diplomats, for example, have enlisted in drug smuggling syndicates, serving as couriers or "mules" on a onetime basis or regularly. In its October 1979 report, the General Accounting Office said drug trafficking is engaged in by persons from virtually all walks of life including lawyers, accountants, businessmen, doctors and entertainers (exhibit 17; p. 110). So many different kinds of people engage in drug trafficking because of the great profits contrasted with the diminished likelihood that they will be caught. GAO gave five reasons why violators consider the risk to be small. First, the U.S. border defenses against contraband have not been serious impediments for smugglers. Second, Government success in immobilizing trafficking has been limited. The third reason is that only an estimated 5 to 10 percent of all illicit drugs available in the United States are seized by authorities. Fourth, efforts to attack and confiscate the financial resources of traffickers have been disappointing, and, fifth, lenient bail policy and sentencing of convicted violators have failed to provide a strong deterrent to drug trafficking.

III. BIG DRUG CASES REQUIRE FINANCIAL INVESTIGATION

Financial Evidence Is Essential in Many Drug Cases

With so much money to be made, major narcotics dealers frequently cannot resist the temptation to spend too much too fast, thereby making themselves conspicuous. Robert J. Perry, an Assistant U.S. Attorney in Los Angeles and Chief of the Controlled Substances Unit for the Central District of California, gave the Subcommittee several examples of dope dealers whose big spending habits led to their arrest.

Perry said that Jose Valenzuela was one of the leaders of the Valenzuela family heroin organization. In a three-year period, Valenzuela spent $63,000 in cash to purchase luxury cars. Valenzuela and his brother invested $80,000 in cash in a taco factory, Perry said, adding that they then laundered more than $70,000 in small bills through the company's books. Moving away from a home where he lived and paid $70 a month rent, Valenzuela in October of 1975 paid $335,000 for a mansion in San Marino, California. He paid for the home in cashier's checks from Mexico, Valenzuela spent an additional $61,000—$40,000 of it in cash—to redecorate the mansion (p. 91).

Perry acknowledged that without information gained from Valenzuela's financial dealings, the Government did not have much of a case. "Our evidence of Valenzuela's involvement in the massive heroin operations of his organization was fairly skimpy," Perry testified. "But the financial evidence of Valenzuela's expenditures enabled us to show that he was the leader of the organization." Tried and convicted of numerous drug charges, Valenzuela was sentenced to life imprisonment and two concurrent 60-year terms. Perry told the Subcommittee, "I prosecuted the Valenzuela case, and I believe that without the evidence of Valenzuela's expenditures, he might not have been convicted, and even if convicted, would not have received such a substantial sentence." In the same case, eight co-defendants were convicted of lesser narcotics violations. This was a significant victory for Federal prosecution for it dismantled the Valenzuela family operations, which included the operation of heroin laboratories in Culiacan, Mexico. The family then smuggled huge amounts of heroin to relatives in California. The high quality heroin was then redistributed to five distinct trafficking groups in New York City (pp. 91–92).

BINGE

Like Jose Valenzuela, Leroy Anderson went on a buying binge that ultimately bought him a trip to prison. Perry said Anderson spent $350,000 in a two-year period when he was employed as a newspaper delivery truck driver. Anderson made a $120,000 down payment in

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cash on a home he bought; paid $23,000 in cash to have the grounds landscaped; had a swimming pool installed for $12,000 in cash; bought in cash a $34,000 mobile home; paid $45,000 in cash for improvements to his parents' home; made cash loans of $40,000; and bought several cars worth a total of $49,000. Convicted of narcotics and income tax violations, Anderson got a 17-year prison sentence and a $45,000 fine. "In my opinion," Perry said, "the financial information was of critical importance in obtaining the conviction and the substantial sentence" (p. 92).

The owner of a pharmacy, Ralph Godoy got into the habit of carrying around large amounts of cash. Perry said Godoy deposited $100,000 in cash into an escrow account for the purchase of a Las Vegas casino. All told, Assistant U.S. Attorney Perry said, Godoy bought properties worth $800,000. Godoy was found to be buying big quantities of quaaludes, which were then resold illicitly. Godoy was convicted of narcotics and racketeering charges said Perry, who concluded, "The evidence of Godoy's expenditures left no doubt regarding his criminal involvement" (p. 92).

Perry told the Subcommittee that the Valenzuela, Anderson and Godoy cases—all of which Perry worked on—show the necessity of conducting financial investigations if police and prosecutors are to succeed in making their charges stick against major narcotics dealers. "Financial information is reliable and non-biased and helps to balance informant witnesses," Perry said. He also pointed out that financial information is especially persuasive when a judge is setting bail. When the judge understands how much money the defendant may have access to, he is less likely to set a low bail. Perry went on to say, "We have found that financial evidence has a profound impact on jurors and judges and often results in longer sentences. I attempt to develop financial evidence in every major narcotics case investigated in our district" (p. 92).

BARNES

Another major conspiracy case that relied heavily on financial investigation was the Leroy (Nicky) Barnes case in Harlem. Another witness, Irvin B. Nathan, Deputy Assistant Attorney General in the Criminal Division of the Justice Department, called Nicky Barnes the leader of "which was believed at the time to be one of the largest heroin trafficking networks in the United States." Because Barnes was charged with violation of the continuing criminal enterprise statute, the Government had to prove that substantial amounts of his income were from narcotics. With the help of Barnes' tax returns—obtained from IRS after lengthy delays—the Government was able to prove its case. Barnes was convicted of engaging in a continuing criminal enterprise, of conspiring to distribute heroin and cocaine, and of distributing large amounts of heroin. He was sentenced to life in prison and fined $125,000. Barnes had been directing a $1 million a month heroin and cocaine operation out of a garage in Harlem. Ten members of the Barnes syndicate were convicted of lesser charges and eight of them received sentences from 15 to 30 years. Nathan said that Barnes' tax returns were "very useful to us because those returns showed that Barnes and his colleagues had put down in the category of miscel-

laneous income about $250,000 each year for each of them which they couldn't explain . . . this went a long way toward establishing that the $250,000 [was income] that they were declaring in order to avoid the kind of net worth case that was made against Capone. . . ." Unlike the Capone case where the IRS played a central role in the prosecution, IRS delays in turning over Barnes' tax returns nearly caused the Government to lose the verdict. "If those tax return had been delayed any longer, that conviction might never have been obtained," Nathan said (p. 27).

The Araujo Case Was Successful

The investigation and successful prosecution of the Araujo drug syndicate in Los Angeles is often cited by law enforcement officials as a textbook illustration of how a major assault on bigtime organized narcotics traffickers should be implemented. The Araujo organization was a large heroin syndicate based in Los Angeles and Mexico. The group's leadership, dealing in millions of dollars in drug sales, was smart, not the kind of people who were going to make foolish mistakes. They knew it was likely that police had them under surveillance, and they conducted themselves accordingly. At times they seemed to leave no stone unturned in their efforts to avoid detection and prosecution. Robert Perry, the Assistant U.S. Attorney in charge of the Controlled Substances Unit in Los Angeles, gave the Subcommittee an illustration of how careful Araujo gang members were. Perry said that in the course of the investigation a wiretap was put on the phone in Jaime Araujo's residence. On one occasion, Jamie used that phone to order a gang member to pick him up. The two men then drove to a public pay phone. Jaime placed a call. They waited. A second gang member drove up. He took Araujo to Disneyland, a drive of some 50 miles. Araujo paid the admission to the amusement park. Inside Disneyland, he went to a public pay phone. He placed a call. Then he left.

Despite such elaborate security precautions, the Araujo syndicate was immobilized—by a combined effort of agents from DEA, Customs, the Internal Revenue Service and Los Angeles police. Bank records obtained during the investigation revealed that from September 1975 through October 1978 the Araujo organization derived more than $32.8 million in currency from the sale of narcotics—about $900,000 a month. This money was laundered through bank accounts under fictitious names in the United States and Mexico. More than $1.5 million was then used to purchase residences and make real estate investments in the United States.

Indictments

In August of 1979, 22 members of the Araujo organization were indicted on various Federal charges. Nine of the defendants were apprehended and pleaded guilty. The remaining defendants are believed to have fled to Mexico. Jaime Araujo was held in custody in lieu of $5 million bail. He pleaded guilty to charges of conspiracy, narcotics violations and tax evasion on income in excess of $13 million. This is believed to be the largest personal income tax evasion case in history. Araujo was sentenced to 35 years in prison, to be served concurrently with a 15-year sentence with no parole. He was fined $1.2 million. In

November 1979, investigators seized 100 pounds of heroin, 49 pounds of morphine base and 30 pounds of cocaine from a residence maintained by the Araujo organization. Authorities believe this to be the largest seizure of drugs in the Western United States.

To Assistant U.S. Attorney Robert Perry's way of thinking, the cooperative interagency teamwork that made the Araujo case such a success for law enforcement is the kind of effort Federal agencies should put forward regularly. Only then can the big drug syndicates be immobilized and their leaders sent to jail. The Internal Revenue Service was especially helpful in the Arajuo inquiry, Perry testified, saying, "It is clear that without the joint participation of the many agencies involved, that we would have been unable to develop this hallmark prosecution. Cases such as the Araujo case show the enormous amounts of money generated by major narcotics organizations, and the sophisticated nature of these organizations. The development of financial evidence helps to identify the leaders of the organizations and is often the most effective law enforcement tool available. Financial information provides tremendous impact and results in appropriate sentences for major traffickers. In order to bring the full force of Government resources to bear against these major traffickers it is essential that financial information be emphasized and that IRS criminal investigators participate in such investigations" (p. 93).

Controlled Substances Units Praised, Criticized

Robert J. Perry was Chief of the Controlled Substances Unit of the U.S. Attorney's Office for the Central District of California in Los Angeles. He had an excellent record in initiating cases against syndicated narcotics sellers; the Valenzuela, Anderson, Godoy and Araujo cases all attest to that. The Controlled Substances Unit (CSU) in the Central District of California was found to be a well run program, well staffed and deserving of the good reputation it enjoyed. But not all CSU programs were so successful. In its evaluation of the Controlled Substances Units around the country, the U.S. General Accounting Office found some CSU programs to be effective (exhibit 17, p. 110). But others were not effective at all and were not living up to the hopes the Department of Justice held for them.

Established in February of 1975, the CSU program was to be a key element in the Government's effort to prosecute major international and interstate drug violators through conspiracy laws. The CSU's, established in 22 cities, were supposed to provide a core of experienced attorneys in each city who could devote the time and resources necessary to develop complex drug cases with the Drug Enforcement Administration. GAO was critical of the Department of Justice for not seeing to it that the CSU program was implemented properly in each city where it was set up. Instead, GAO said, the Department neglected the program. The result was that some U.S. Attorney's offices took the program seriously and tried to make it succeed, while other offices focused their attention on other matters and allowed the CSU to take a backseat. Consequently, Federal efforts against major drug syndicates did not have the benefit of the best available prosecutorial guidance.

AUDIT

A 1979 Department of Justice Internal Audit Report found that some Federal districts insisted upon well-qualified and experienced attorneys in their Controlled Substances Units, lawyers who were willing to remain with the program long enough to learn the ropes and contribute to the success of several cases. But other Federal districts assigned new personnel and made short term assignments. The Justice Department audit report found that CSU's did not always handle cases involving major interstate and international drug traffickers. In some districts, the CSU caseloads consisted of both big and small drug cases and, in some instances, even non narcotics cases. CSU attorneys were found to be receiving little supervision and only limited training in the legal techniques, methods and tools that are effective in developing major narcotics cases. Few CSU attorneys were experienced and trained sufficiently to utilize the conspiracy, Racketeer Influenced and Corrupt Organization (RICO) and continuing criminal enterprise (CCE) statutes, laws which are helpful in prosecutions against narcotics syndicates. The audit report also found a lack of coordination and communication among the various Controlled Substances Units around the country. Such teamwork is necessary for developing interstate and international conspiracy cases.

GAO's own inquiry found specific instances of the shortcomings cited by the Justice Department's audit report. In San Francisco, Assistant U.S. Attorneys and others associated with the Federal district there said CSU efforts had not been very effective in developing and prosecuting major drug conspiracy cases. Some recent improvements were noted, however. In Chicago, all types of drug cases were handled by the U.S. Attorney's narcotics unit, which was generally staffed by attorneys with little trial experience. Although some of the more complex drug cases were handled by attorneys outside the unit to take advantage of their experience, these lawyers were not assigned full-time to narcotics. In Miami, the Controlled Substances Unit placed little emphasis on major cases. Consequently, the Justice Department assigned two staff attorneys to work with DEA on investigations of several large scale drug syndicates.

While asserting that the Controlled Substances Unit program had not lived up to its potential, GAO was still hoping for improvements, as it said in its report, "Effective drug enforcement requires an unusually high degree of communication and coordination among agencies, and conspiracy cases against the top level drug financiers require, additionally, sophistication and a marshalling of available resources. CSU attorneys occupy the best position to accomplish this oversight and coordination through their early involvement in conspiracy case investigations. For this to happen, however, the parochialism and individual prosecution practices of U.S. Attorneys will have to be tempered, and the Justice Department's nationwide drug prosecution strategy strengthened."

IV. DEBATE OVER TAX REFORM ACT

Critics Say IRS Does Too Little To Combat Drug Trade

The General Accounting Office criticized the Drug Enforcement Administration for not being more proficient in conducting financial investigations of narcotics traffickers. Senator Sam Nunn, Chairman of the Subcommittee, asked DEA Administrator Peter Bensinger his views on GAO's criticism. While asserting that DEA has become competent in making conspiracy cases, Bensinger acknowledged that he would like to have agents with more capabilities in financial investigative skills, that some agents are proficient in it while others need more training, that DEA, which has fewer agents than the Capitol Hill Police Force has police, needs more resources and that the DEA record would be a lot better if his agency enjoyed a more cooperative "partnership with the investigative agency which has the most expertise, information and resources." By that Bensinger meant the Internal Revenue Service (p. 87).

Senator Nunn asked, "In other words, you are saying, IRS has the most financial expertise of any Federal agency?" "No question about it," Bensinger replied. Senator Nunn asked, "And if you are going to have any effective financial analysis, that is certainly the most efficient place to get it done?" "Absolutely," Bensinger replied. It was Bensinger's opinion that DEA's performance in doing financial investigation "would improve quantumly" if only IRS would cooperate more (p. 87).

Bensinger was not alone in his views about IRS. Witness after witness spoke in favor of having more participation by the Internal Revenue Service in Federal efforts to investigate, prosecute and immobilize the narcotics syndicates. Similarly, several witnesses—current officials of the Justice Department and former officials of Treasury and IRS—said IRS could make more of a contribution to drug investigations if its policymakers wanted the Service to. But IRS policy, heavily influenced by persons who apparently find police work unseemly, is to disengage the IRS as much as possible from traditional law enforcement efforts such as investigations of organized crime and drug groups, critics of the IRS said. The critics went on to say that the passage of the Tax Reform Act of 1976, with its limitations on the disclosure of IRS information to law enforcement, was made to order for those who wished to take IRS out of the crime field. The critics said that the legislation came along at a time when IRS officials, led by Commissioner Donald Alexander, believed the Service's single, overriding function was to bring about voluntary compliance of ordinary, law-abiding citizens with the internal revenue code. IRS deliberately seized on the Tax Reform Act as an excuse not to cooperate with other Federal investigative agencies, witnesses said. However, other witnesses—senior officials at Treasury and IRS—denied charges of IRS foot

dragging in the narcotics and organized crime field. They insisted that the IRS stands ready and willing to cooperate whenever and wherever called upon.

Tax Reform Act of 1976

The Tax Reform Act of 1976 was a comprehensive measure that affected many features of the nation's tax system. Two aspects of the act—the disclosure provisions and the summons provision—had special impact on law enforcement.

The disclosure provisions of the Tax Reform Act appear in Title 26 of the United States Code under Section 6103.[1] Section 6103(i) regulates the manner in which IRS may disclose information from tax returns and other sources to Federal agencies which are investigating non-tax crimes.

Section 6103(i)(1) is the court order requirement. To obtain tax returns and taxpayer return information, the Department of Justice or another Federal agency must seek a court order. The statute requires that the application for such a court order contain information to prove that (1) there is reasonable cause to believe, based on information believed to be reliable, that a specific criminal act has been committed; (2) there is reason to believe that, such return or return information is probative evidence of a matter in issue relating to the commission of such criminal act; and (3) the information sought to be disclosed cannot reasonably be obtained from any other source, unless it is determined that, notwithstanding the reasonable availability of the information from another source, the return or return information sought constitutes the most probative evidence of a matter in issue relating to the commission of such criminal act.

REQUEST

Section 6103(i)(2) is the agency request requirement. This has to do with information other than tax returns or taxpayer return information which is held by IRS. This information can be obtained by written request from the head of the requesting agency. The written request must give (1) the name and address of the taxpayer with respect to whom such return information relates; (2) the taxable period or periods to which the return information relates; (3) the statutory authority under which the proceeding or investigation is being conducted; and (4) the specific reason or reasons why such disclosure is or may be material to the proceeding or investigation.

Section 6103(i)(3) sets the procedures for IRS to provide non-tax criminal information to other agencies. Under this section, the Secretary of the Treasury may disclose return information other than return and taxpayer return information, which may constitute evidence of a violation of Federal criminal laws to the extent necessary to appraise the head of the appropriate Federal agency charged with the responsibility for enforcing such laws. The Treasury Secretary is not required to disclose such information but decides on a case-by-case basis.

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[1] See appendix p. 133.

Law enforcement officials level six major criticisms against the disclosure provisions. They say that (1) the statute makes it difficult to obtain IRS assistance in investigations that are worked jointly by IRS and another Federal agency; (2) the act generally prohibits IRS from disclosing what types of investigations it is working on; (3) the act generally prohibits IRS from disclosing financial information to any other Federal agency; (4) the act generally prohibits IRS from disclosing evidence it has of non-tax crimes to the appropriate Federal agency; (5) the act, coupled with IRS procedures and paperwork, causes unacceptable delays in obtaining any response from IRS; and (6) the disclosure provisions have a "Catch-22" [2] aspect in that they require agencies which seek information to make a preliminary showing to a court or to the IRS but at the same time prohibit IRS from giving another agency enough information to seek such a disclosure request.

The summons provision of the Tax Reform Act appears in Title 26 of the U.S. Code under Section 7609.[3] The statute changed the summons procedures as they apply to administrative summonses issued by the IRS to third parties for financial records of alleged tax evaders. The law requires that the taxpayer be notified that an IRS summons has been issued to a third party. The taxpayer then has the right to automatically stay the performance of that summons until IRS can take the issue to court. To obtain this automatic stay, the taxpayer does not have to advance any legal argument.

Both Justice Department and IRS officials are critical of the summons provision. They say it causes tax cases to be delayed as much as a year. They say many persons who invoke the automatic stays are criminals whose only wish is to delay proceedings in the hope that the passage of time will weaken the Government's case.

Justice Department Criticizes Tax Reform Act and IRS

For critics of the disclosure provisions of the Tax Reform Act, "The Case of the Trash Can" demonstrates the need for amending the statute (pp. 24–26). In Philadelphia, the Drug Enforcement Administration was investigating a man suspected of being an illegal drug chemist. The IRS was conducting its own investigation of the suspected chemist. IRS did not tell DEA because the Tax Reform Act prohibits such an exchange of information. But DEA found out IRS was on the case. DEA also learned that IRS agents had gone through the chemist's trash can and turned up drug formulas and other documentation suggesting the chemist was concocting drugs. The prosecutor in the DEA case subpenaed the IRS agent who had the contents of the trash can. But the Internal Revenue Service ruled that its own agent could not testify unless the prosecutor obtained a court order. Such an order is required according to the Tax Reform Act disclosure

[2] The term "Catch-22," which was used extensively by witnesseses testifying about the Tax Reform Act, is from the novel Catch-22 by Joseph Heller. The protagonist, Yossarian, fearing death, wishes to fly no more bombing missions. To be relieved of this duty, Yossarian must persuade his superiors that he is insane. But, Yossarian learns, his superiors consider it rational of him to seek to be grounded—and only logical of him to use the argument that he is insane. Only the insane would do otherwise. As Yossarian saw his dilemma, "If he flew them he was crazy and didn't have to; but if he didn't want to he was sane and had to." That was the Catch-22.

[3] See appendix p. 134.

provisions, IRS said. Unfortunately, the court order could not be obtained until completion of the suspected chemist's trial. The chemist was convicted anyway, without IRS assistance. But, according to Irvin B. Nathan, the Deputy Assistant Attorney General in the Criminal Division of the Justice Department, "The Case of the Trash Can" left Federal prosecutors with serious doubts about the Tax Reform Act.

INFORMATION

Nathan explained that the trash can illustration showed just how broadly the statute was written. He said the statute defines taxpayer return information as not simply the tax return and the required filings that accompany the return itself, but also "any information which comes from the taxpayer, from his books, from his records, from corporate records that he is required to keep, even whatever his representative or attorney would tell to the Service. That has the mask of confidentiality and cannot be provided to any other investigative agency" (p. 24). According to the IRS interpretation of the statute, the contents of the trash fit that broad definition.

Asked if the Justice Department ever did get hold of the trash, Nathan said, "we now have the trash and it is exactly worth that to us now that the case is over." Senator Cohen wanted to know why the Department had not asked for a delay to allow time for the court order. Nathan said the trial itself was to be over in no more than two weeks and that getting a court order is no simple task. The law requires that the heads of both agencies approve the transfer of information. He said that once the decision is made to seek a court order, the prosecutors have to draft a petition, have it approved by the Assistant Attorney General, then file it in Washington. If the petition is granted, it is then referred to the Internal Revenue Service, which, after examining the application, may decide it would adversely affect the IRS because it might reveal the identity of an informant or for other reasons. In any event, the IRS must make an analysis of the court order and, if it concludes the order would in no way disrupt its own investigative efforts, finally the order can be implemented and the information disclosed. The average length of time required to obtain a court order is 37 to 40 days (pp. 25, 26).

Nathan used the trash can case to support his criticism of the Tax Reform Act. The disclosure provisions of the law constitute a barrier to good police and prosecutorial work, Nathan said. Citing first the destructive impact on society of the illegal drug traffic and the large sums of money it generates, Nathan said an important cause of law enforcement's failure to bring big narcotics traffickers to justice is the Tax Reform Act. Its disclosure provisions make cooperation between investigating agencies very difficult, Nathan said. But Nathan, who is the second ranking official in the Criminal Division of the Justice Department, said the Tax Reform Act disclosure provisions, difficult as they are to live with, are made even more hard to handle by the Internal Revenue Service itself, which seems to be in no mood to cooperate (p. 29).

IRONY

Referring to the proven value of new tools in the war on drug traffickers such as the Bank Secrecy Act,[4] the Continuing Criminal Enterprise law and the Racketeer Influenced and Corrupt Organization statute, Nathan said it is ironic that the Congress should also have passed a confidentiality provision in the Tax Reform Act that has stood in the way of success in narcotics cases (p. 52). The disclosure provisions are even more of an irony, he said, in view of the fact that there was no evidence to support the fear that such confidentiality safeguards were even needed. Nathan said that when the act was passed in 1976 there were few, if any, complaints about abuses by prosecutors of tax information which they obtained and used in developing criminal cases (p. 39). As a legislative remedy of a problem that was not shown to exist, the law created problems of its own, Nathan said. "The statute, as enacted and interpreted by the [Internal Revenue] Service, given the penalties to which IRS personnel are subjected for improper disclosure, has made it extremely difficult for law enforcement officials working in such high financial crime areas as narcotics, organized crime, white collar crime and public corruption" (p. 52). Nathan said Federal prosecutors have told him that they believe the IRS seized on the Tax Reform Act's disclosure provisions as a justification for the IRS's desire to disengage itself from organized crime and narcotics investigations (p. 35).

The disclosure provisions of the tax law severely restricted the Government's ability to identify and prosecute narcotics financiers and to trace and seek forfeiture of their assets, Nathan said. No longer can Federal prosecutors and investigators work closely with IRS, Nathan said, adding, "This is extremely unfortunate because the Service agents are by training, experience and temperament among the best qualified of any in the Federal Government to assist in conducting financial investigations, and the information available to the Service is among the most important to assist in developing financial cases" (p. 52).

Nathan said the problems created by the disclosure provisions of the tax law are made worse by the IRS itself and its desire to move away from organized crime and narcotics investigations and to work more cases against the taxpaying public in general. Senator Cohen asked Nathan if there is a reluctance by IRS to commit substantial resources to narcotics and organized crime cases. Nathan said there is such a reluctance. He said the Tax Division and Criminal Division of the Justice Department want to be of assistance to IRS as it devises its long term strategy for criminal investigations. But, he said, IRS has no interest in entertaining any of the Justice Department's ideas or recommendations. "We stand ready to make that input," Nathan said. "We seek cooperation and coordination with the Service" (pp. 46–47).

NEGATIVE

Four negative effects on law enforcement flow from the Tax Reform Act, Nathan said. First, IRS cannot, in most instances, advise

[4] For discussion of the Bank Secrecy Act, see ch. VI.

the Justice Department of what cases it is working on. This leads to a lack of close cooperation and duplication of effort. The next negative result of the tax law is that it makes it unduly difficult for prosecutors and investigators from Justice to obtain financial information from IRS to assist in developing prosecutions against major criminals. Third, it is very difficult for IRS to give to other Federal agencies evidence concerning non-tax criminal violations which was obtained in the normal course of its investigations. Finally, Nathan said, in those limited circumstances where prosecutors can work with IRS the time delays involved tend to thwart the benefits that might otherwise have been achieved (pp. 52–53).

Nathan said the court order requirement works against good investigative effort in three ways. First, because IRS cannot tell Justice that it has useful information, the Department has no reason to request disclosure of the specific tax information at issue. Second, even if Justice suspects IRS has valuable information, there is an added requirement in the court order procedure that puts the requesting agency in a dilemma. That dilemma is seen in the fact that the law says before the court order can be obtained it must be shown that the tax information would demonstrate that a crime actually took place, that the tax information sought would provide evidence of the crime admissible in court and that this evidence is the best that is available. Such a requirement puts Justice Department officials in the Catch-22 situation. The law requires the requesting agency to have a significant amount of information about a tax return or another document it has never seen. The third problem in the court order requirement, Nathan said, is that it is a cumbersome, time consuming procedure that is not really needed. Calling the requirement "unnecessary, dilatory and inappropriate," Nathan said having to go through the involved preparation and processing of the documents needed for transfer ties up valuable resources and produces "delays which can in certain types of investigations prove fatal" (pp. 26–27).

VERDICTS

The prosecution of the Nicky Barnes heroin organization in Harlem was discussed in Chapter III of this report. It was cited as an example of how financial investigation can lead to the successful prosecution of a major drug syndicate when many other more direct attempts to immobilize the organization have failed. In the Nicky Barnes situation, Barnes himself was known to authorities to be a major violator. But proving it had not been possible until police used the financial investigation approach. The guilty verdicts constituted a well publicized victory for law enforcement as Nicky Barnes, one of the most notorious drug dealers in the nation, received a life sentence and several of his chief assistants were severely sentenced as well. But, Nathan told the Subcommittee, what was not so widely known was just how close the Government came to losing the Nicky Barnes case—and how the disclosure provisions of the Tax Reform Act were to blame (p. 27).

Nathan said Barnes was charged with violating the Continuing Criminal Enterprise statute which requires proof of substantial

amounts of income from narcotics. In April of 1977, prosecutors sought disclosure of the tax returns of Barnes and other principal defendants. Disclosure was sought under Section 6103(i)(1), which is the procedure to be followed in pursuit of a court ordered release of tax returns. Six months went by, the trial began—and the tax returns had not been turned over. Nathan said the trial was underway for one month when several of the returns, including Barnes', were finally given to prosecutors. Some returns never were given over. Even at the late date in the trial, the tax returns were of great value, showing for example, that Barnes reported more than $250,000 in miscellaneous income in one year alone. The prosecution was a success, Nathan said, but he warned, "If those tax returns had been delayed any longer, that conviction might never have been obtained" (p. 27).

CATCH-22

Nathan was especially troubled by the Catch-22 aspect of the Tax Reform Act, that feature of the disclosure provisions which demands that law enforcement officials have extensive knowledge about documentation they have never seen. In this exchange with Senator Nunn, Nathan discussed the problem this requirement poses for law enforcement agents:

> Senator NUNN. You first have to discover that they have that information [to enable the Department of Justice to seek a court order].
>
> NATHAN. Exactly.
>
> Senator NUNN. Which they can't tell you about.
>
> NATHAN. They can't tell us.
>
> Senator NUNN. Then the Justice Department, or DEA, or the FBI will, just out of the blue, have to find out from other sources that the IRS agent has been nosing around and found something in a narcotics suspect's trashcan.
>
> NATHAN. Yes. Of course, the IRS agents are precluded by statute and subject to both criminal and civil liability if they disclose the fact that they have information which they would like to turn over but which requires a court order or agency request (p. 26).

Nathan cited three instances in which IRS discovered evidence that a non-tax crime had been committed but, because of the Tax Reform Act, did not report it. One such case occurred when IRS analyzed records submitted by a taxpayer showing that a union official had accepted bribes, Nathan said. The second case he described had to do with IRS investigators who were reviewing a corporation's records. They found evidence that the corporation had paid off a public official. In a third instance, IRS agents, while going over the papers of a nightclub, came upon evidence indicating a narcotics transaction (pp. 25, 26).

These cases, and many more like them, demonstrate the difficulties the Tax Reform Act causes law enforcement officials, Nathan said. The ban on IRS simply telling the Drug Enforcement Administration that it has uncovered a drug crime, for example, is particularly trouble-

some, Nathan said, explaining that the court order requirements can't be met, first, "because IRS can't provide advance notice that it has useful information, another agency often has no reason to request disclosure of taxpayer information on any particular individual. Second, even if the agency suspected IRS possessed useful information—as we often do—the other agency may be in a Catch-22 situation of having to justify the need for the information without seeing what the information is. You have to not only justify it, you have to say that this information is probative information of a material fact in the case, and it is the best source to get that information. That is a difficult burden to carry. In fact, in some ways it is a heavier burden than to establish probable cause for a warrant to enter onto private premises to make a seizure" (pp. 26–27).

CAUTIOUS

Information supplied to IRS in a manner unrelated to a tax return is covered under Section 6103(i)(2) of the Tax Reform Act. Another agency may request such data if the agency head certifies that the evidence will be used solely in connection with an investigation or proceeding and state why it is material to the investigation. Nathan said IRS is "extraordinarily cautious" about complying with agencies which request information under this section of the law (p. 28).

He testified about one incident in which a DEA agent gave an IRS agent a list of persons in whom IRS might be interested. Later the DEA agent misplaced his own copy of the list. He asked the IRS man to give him a copy. The IRS agent refused, citing the Tax Reform Act as his reason. Nathan said that since the information had been supplied by a third party—the DEA agent—the IRS employee believed that a written request from the Assistant Attorney General was required. Nathan described an investigation in Cleveland in which the FBI asked IRS to examine film of documents it had photographed. FBI agents hoped the IRS would then join in the investigation. But, Nathan said, upon receipt of the film, IRS spokesmen said that it was a tax-related matter. IRS could not discuss the case or even return the film, Nathan said. In Arizona, the U.S. Attorney recently formed a special investigative task force to focus on white collar fraud. "Ideally, such a task force should include IRS participation," Nathan said, noting, however, that IRS, because of its reputation for not cooperating, is not serving on the multi-agency task force (p. 55).

TITLE 26

Problems stemming from the Tax Reform Act adversely affect those grand jury investigations in which prosecutors have been able to combine both tax and non-tax violations, Nathan said. He said that as a result of the Tax Reform Act IRS cannot participate in joint investigations until a "Title 26 grand jury request" is processed by the Department of Justice and the IRS. Before such a joint inquiry can begin, the Justice Department must provide justification and seek approval from IRS for each specific taxpayer to be investigated by the grand jury. Nathan said the Justice Department request must first

be approved by an IRS special agent. He passes the request to his supervisor, who, after his own review, sends it up to the chief of the Criminal Investigation Division. That chief, after his review, transmits the request to another chief, the chief counsel of IRS whose approval is needed before the matter can be referred back to the Tax Division of the Justice Department where the final decision is made. Nathan said the delays caused by such procedures can be "staggering" and in one case in Buffalo the frequent referrals took 13 months to complete (p. 30).

The Subcommittee Chief Counsel, Marty Steinberg, had more than ordinary interest in the Buffalo delay since it was he, as chief of the Buffalo strike force, who had initiated the grand jury request to begin with. Leaving Buffalo and joining the Subcommittee staff, Steinberg explained to IRS officials that the Subcommittee would be looking into grand jury request delays such as the one he left behind in Buffalo. The request was finally approved, one year and one month after it had been submitted (p. 42).

MAZE

Nathan talked about the injury such delays inflict on what could and should have been a strong investigation of organized criminals and drug traffickers. He said, "These are people who are not stationary. They are not standing still waiting to be indicted. They are international smugglers, moving at all times. They are likely not to be available when we need them. So we often are left in the situation of having to bring our non-tax case without having this approval from the IRS. We have had numerous instances where we put in requests for grand jury authorization for joint tax and non-tax counts, and we get the tax approval after we have already returned the indictment and after we are almost in trial in the non-tax case. As you can imagine, the prosecutors concluded that this effort to secure approval and go through all of this procedural maze is not worth the effort. Therefore, we don't often make, or we don't as frequently as we should, make the joint tax and non-tax case" (p. 30).

The Araujo case in Los Angeles, cited in Chapter III of this report, is referred to as illustrative of the good results that can come about when financial investigation is used against big drug syndicates. The Araujo case is especially useful in this context because IRS special agents were actively involved in the investigation, an example of the progress that can be achieved when the IRS works closely with the Justice Department and DEA. But, Nathan pointed out, it took eight months for the Justice Department to obtain IRS concurrence to conduct the joint investigation. Nathan mentioned another instance in which Justice initiated the request for a joint inquiry in March of 1979 and it still was being processed in December when Nathan testified, more than nine months later (p. 30).

Making the red tape for joint IRS-Justice Department investigation even more cumbersome, frustrating and lengthy is the added paperwork that must be begun should the inquiry turn up new suspects, Nathan said. The procedure calls for the original suspects to be identified. Then should new subjects emerge as the investigation proceeds, the entire process must be started again. "In a fast breaking in-

vestigation, it can be extremely harmful to have to go back to square one of the procedures," Nathan said. Sometimes prosecutors, faced with busy schedules, decide the process is too much trouble and don't bother to ask for joint investigations, Nathan said.

SIGNALS

The fact that some prosecutors have been put off by the red tape involved in asking for IRS help points to what Nathan felt is the most serious danger caused by the Tax Reform Act—not so much its technicalities and time consuming procedures, which are ample, but more the message the law signals to the law enforcement community, particularly the IRS. "The major problem that we have to focus on is the signal which the Tax Reform Act apparently has sent to the Service," Nathan said, adding that the message appears to be that the Service is to minimize "its role in non-tax law enforcement and devote itself almost exclusively to the voluntary tax collection system" (p. 23).

Nor are the Tax Reform Act's signals lost on prosecutors and other law enforcement officials outside IRS, Nathan said. Rather than complying with the elaborate procedures set forth in the statute, prosecutors have frequently gone without obtaining needed financial information already in possession of the IRS. Supportive of his view, Nathan said, are statistics showing a decline in the number of requests for tax information by Justice Department prosecutors. In 1975, the year before the Tax Reform Act was passed, there were 1,800 such requests; for a six-month period in fiscal 1979 there were only 124 such requests, Nathan testified.

More statistics support his point that the statute signalled IRS to go slow on everything but promoting the voluntary tax system—and IRS read the signal clearly, Nathan said. He said DEA provided IRS with the identity of 868 alleged Class I violators to be evaluated for criminal tax potential. Of the 868 subjects, 128 investigations were opened, 125 completed, 31 prosecutions recommended, nine indictments obtained and only six convictions. The six convictions represent less than a one-percent success rate. Nathan went on to say that since the Tax Reform Act had gone into effect in January of 1977 the organized crime strike force inventory of joint IRS-Justice Department cases had been cut in half, from a high of 600 investigations to slightly more than 300. He said IRS's own figures indicate that the Service devotes less than five percent of its criminal investigative resources to narcotics matters (p. 23).

CHILLING

Similarly, Robert J. Perry, the Assistant U.S. Attorney in Los Angeles who told the Subcommittee about the effectiveness of financial investigations in cases against major drug traffickers, was highly critical of the Tax Reform Act and what it had done to law enforcement (pp. 90–112). The act's disclosure provisions have had a "definite chilling effect on prosecutors," he said. Prosecutors are so put off by the law that they are reluctant to ask for IRS participation in a case,

Perry said, recalling that he prosecuted cases before the Tax Reform Act took effect and that those cases were productive, successful and a vivid demonstration to him of the value of IRS support. But since enactment of the new law, he said, "there are delays and I can cite you many examples in our office where we felt that the Tax Reform Act just caused us to jump through too many hoops and it was just too difficult to worry about" (p. 107).

Nathan told the Subcommittee that the Tax Reform Act has not only sharply curtailed the amount of information which IRS can give other agencies but it has also radically reduced the flow of information going to IRS as well. He said that a point that may be missed is that other law enforcement officials, recognizing how little assistance they are receiving from IRS, are returning the favor. Nathan explained, "It is simply a fact of life in agencies that the information flow cannot be a one-way street. If IRS can receive but not give back any information, if it can't tell other agencies what they are working on, who they are investigating, what they have found, then the other agencies simply do not want to cooperate and do not want to provide information to the Service" (p. 28).

The Federal organized crime strike forces, built on the premise of coordination among several agencies, are supposed to combine the Government's best resources and expertise to fight organized criminal groups, Nathan said. But, he pointed out, the IRS is almost no help at all as "IRS agents sit mute. They don't tell us who they are investigating, they won't tell us what information they have. They won't cooperate in the coordination of the effort of the strike force for the most part" (p. 29). On the strike force subject, Senator Chiles asked Nathan what the Tax Reform Act has done to the Justice Department's ability to allocate resources and plan investigations. Nathan replied that it is difficult to coordinate and plan and then try to bring together the resources of several law enforcement agencies when the IRS will not or cannot cooperate. "If we don't know what the IRS is doing and if they can't tell us how they will cooperate on our goals and objectives, then we are significantly impeded in our efforts," Nathan said (p. 41).

TREATIES

Nathan said the Tax Reform Act has had a negative impact on the willingness of other countries to cooperate with American authorities through mutual assistance treaties. These treaties are supposed to enable countries to exchange evidence of crimes. But the disclosure provisions have changed that. Nathan said the IRS, justifying its policy by referring to the Tax Reform Act, is not as helpful as it could be in negotiating such treaties. IRS now takes the position that it will not provide any foreign nation any information except for tax data to be used for tax prosecutions. As a result of this policy, Nathan said, the Netherlands and other countries which could provide the U.S. with financial data for use in non-tax cases have begun to respond as if they too were limited by the Tax Reform Act. These countries, Nathan said, now refuse to turn over evidence for non-tax cases; they will assist only in tax cases. IRS also insists that the Tax Reform Act requires foreign nations to deal only with the IRS and no other Amer-

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ican law enforcement agencies, Nathan said, adding that this insistence creates more obstacles to negotiating mutual assistance treaties (p. 32).

Under Section 6103(i)(3), the Secretary of the Treasury may disclose evidence of a non-tax violation to the appropriate Federal agency. This section does not apply to tax returns or taxpayer return information. Independent inquiry by the Subcommittee staff revealed that this section of the Tax Reform Act has generally failed to provide a sufficient mechanism to supply other agencies with non-tax criminal information for two reasons. First, since the Secretary is not obliged to turn over such information but instead decides on a case-by-case basis, there is no affirmative commitment on the part of IRS to provide this evidence. Second, severe criminal and civil penalties for improper disclosure under the Tax Reform Act discourages IRS officials from implementing this section of the law.

The staff finding regarding section 6103(i)(3) was endorsed by Nathan. He said that since the Tax Reform Act was enacted IRS has voluntarily turned over criminal information to the Justice Department only 25 times a year. Nathan is convinced the IRS holds back non-tax criminal information which the Justice Department could make good use of. One study by the General Accounting Office alone enabled Justice officials to learn of several non-tax criminal matters that IRS had never before told them about. Prior to the Tax Reform Act, Nathan said, the Justice Department had considered IRS non-tax criminal evidence voluntarily turned over to be crucial to its mission.

Quantifying a negative—that is, identifying the number of times that something had not happened—is not easy to do, Nathan said, and that is why no one will ever know the exact dimensions of the damage to law enforcement caused by the enactment of the Tax Reform Act. The number of good criminal cases that were not pursued because of the Tax Reform Act will never be known, but there were many of them and only criminals benefit from that kind of result, Nathan said.

In summary, it was Nathan's view that the Tax Reform Act, if only because of the adverse impact it has had on the Government's ability to do financial investigations, is the law most injurious to good police and prosecutorial work—and thus the law most in need of reform.

FBI Officials Testify on Tax Reform Act

Three men were associated with a photographic studio where young American and Mexican boys were thought to be posing for pornographic movies with homosexual themes. The Federal Bureau of Investigation investigated. Agents found that the men had received Federal funds under false pretenses, had made considerable financial investments and were involved in an international network for the distribution of obscene materials. There was also evidence that the three men were tied in with organized criminals. The case became complicated, requiring analysis of business records, mail order paperwork, money flow and personal expenditures. It was a case that would have benefited from IRS expertise in financial investigation. The FBI learned that IRS had already made inquiry into this pornographic

materials business; but IRS could not be of any assistance to the Bureau because of the Tax Reform Act.

The Subcommittee heard this account from Oliver B. Revell, Deputy Assistant Director of the FBI's Criminal Division. Of the pornography case, Revell testified, "Due to the fact that this is a complicated investigation involving a major national and international mail order pornographic business, numerous business records involving the flow of money, such as financial incomes, and expenditures could have greatly benefited the FBI's investigation. We have determined that the IRS previously conducted a separate investigation relative to this matter. However, IRS has been unable to furnish any information regarding the evidence or the individuals that they discovered involved in their previous case. Of course, this information would have saved us a tremendous amount of time, effort and money. There is no doubt whatsoever that this investigation could have been handled more expeditiously and in a more cost effective manner if the IRS was not restricted by the Tax Reform Act" (p. 247).

FUGITIVE

Since the Tax Reform Act went into effect in 1977, the FBI's joint investigations with the IRS have declined by 95 percent, Revell said. He said that in 1977 and 1978 when he was officer in charge of the Oklahoma office of the FBI, he and his agents did not receive a single piece of information from IRS.

At the request of the Subcommittee, the FBI surveyed its 11 largest offices to determine the impact of the Tax Reform Act. The survey was completed in early December of 1979. Revell said the findings of the survey were that the Tax Reform Act "hampers us in fulfilling our investigative responsibilities and has greatly diminished cooperation between the FBI and IRS" (p. 243).

Critical remarks from the FBI field offices were directed against the disclosure provisions of the law and against the manner in which IRS has chosen to interpret the law, Revell said. He said FBI personnel complain that the law has prevented the receipt of vital information that could have been the basis for criminal investigation. FBI agents said investigations to locate fugitives, many of whom are already felons, were made more difficult without the help of IRS. Explaining this point, Revell said, "Knowing the fugitive's last employer and residence, information that is often obtained on his tax returns, could well result in his apprehension." FBI officials were concerned about the fact that they could not obtain pertinent tax information when investigating major fraud, public corruption and organized crime cases. Revell said agents had found it difficult and sometimes impossible to trace illicit monies without the help of the IRS. Delays were also a problem, Revell said, pointing out that in major white collar crime cases, the issuance of search warrants and other investigative tools require timely and prompt access to information. Excessive delays, some as long as six to eight months, render these tools meaningless. FBI responses to the survey also indicated that the Tax Reform Act hampers effective prosecution of criminals. Revell said, "The IRS has very potent statutes interfaced with Title 18 statutes investigated by

the FBI. However, indictments using these statutes to strengthen Title 18 cases are seldom forthcoming because of information withheld by the IRS. This is a loss of a very favorable prosecutive tool" (pp. 243, 244).

KEYSTONE

Referring to task forces comprised of IRS and FBI personnel working with prosecuting attorneys, Revell said such joint investigations are a "very logical approach" to white collar and organized crime cases. But since IRS agents can no longer share their findings with anyone else, the task force concept has been all but abandoned, Revell said. In addition, the Tax Reform Act has virtually destroyed "agent-to-agent cooperation between FBI investigators and those of the IRS," Revell said, adding, ". . . we have always maintained a keystone to effective law enforcement is cooperation. This act has substantially reduced investigative cooperation between the FBI and IRS to the detriment of the public . . ." (p. 245).

Revell said the field office survey cited 70 separate instances in which the Tax Reform Act disclosure provisions were a hindrance to good investigative work. In one of these cases, a drug smuggler was charged with Federal narcotics violations. The FBI asked IRS for help several times. The Bureau was turned down each time. As a result, the stronger charges against the defendant had to be dropped. In another inquiry, the FBI was looking into bank fraud. The Bureau asked IRS for help. IRS delayed. FBI agents went out and obtained on their own records the IRS already had. IRS finally turned over the requested documents. "The IRS was eventually able to cooperate in the investigation of this matter," Revell said. "However, this information was of little use inasmuch as the information had already been obtained through the determined efforts of the Bureau agents while awaiting requested IRS information." Had the IRS cooperated promptly, "needless time, energy and money" could have been saved, Revell said. A $20 million real estate loan fraud that involved one bank on the verge of failure and a mortgage company in bankruptcy was linked to organized criminals. Investigating, the FBI found that it could proceed no further without IRS help—but IRS help was not forthcoming. So, Revell said, the investigation came to a halt. Seeking court approval for the IRS records would have taken too long, Revell said (pp. 245–246).

SURVEY

The FBI field survey revealed just how strictly and arbitrarily the IRS has chosen to interpret the Tax Reform Act. Revell told the Subcommittee about a mother whose son was a Government witness. Two men identifying themselves as being IRS agents asked the mother for the son's whereabouts. She told them. The FBI learned what she had done. Alarmed, they asked the IRS if the men were in fact IRS agents. The IRS, citing the Tax Reform Act, refused to either confirm or deny that the agents were authentic. "This has obvious ramifications for the safety of a very important Government witness," Revell said, adding that he would have thought simple common sense would have led the IRS to cooperate in this instance. "I don't see how that can be considered taxpayer information," he said (p. 247).

The Tax Reform Act even manages to extend itself into national security cases, Revell said. The FBI is currently investigating an American citizen suspected of selling secret information to the foreign intelligence agency of a hostile government. The FBI asked IRS for financial information on the suspect. But IRS delays in turning over the records make it impossible to go forward with the case. Meanwhile, the suspect is still free to continue his alleged dealings with the enemy. "The Tax Reform Act has hampered this and other espionage investigations to the extent that the procedure required to obtain IRS information necessary to an espionage investigation are extremely complicated and time consuming," Revell said (p. 248).

Cases involving political corruption are affected by the Tax Reform Act. Revell said the FBI spent many months investigating a State Assemblyman suspected of influencing the rezoning of property for his own gain. It turned out that the IRS had done the same inquiry. Revell said that if the FBI could have shared the information with IRS it could have saved the time of six agents working three months "to duplicate already existing investigative information in the files of another agency, namely, the IRS" (p. 248). Similarly, both the IRS and the FBI were investigating the Mayor of a city. But the IRS got there first, subpoenaing the Mayor's records, the same records the FBI wanted. The IRS refused to let FBI agents see the subpoenaed records. Without the records, the FBI had no choice but to end its investigation.

FRAUD

In his previous assignment as agent-in-charge of the Oklahoma office of the Bureau, Revell worked on investigations in oil fraud. An energy fraud unit was formed and inquiry was begun into alleged violations of energy statutes. The IRS would have been of considerable assistance to the energy fraud unit. But FBI officials, after consulting with the U.S. Attorney's Office and with IRS, decided they would be better off without waiting for the IRS to help. Some of the cases were threatened by the statute of limitations running out and other time considerations. Time was too important to use waiting around for Tax Reform Act procedures to be satisfied, Revell said. "So we proceeded separately on our investigation," Revell said. In one of the energy fraud cases, the FBI found possible unreported income by a major oil company. It was important to have the IRS in on this case because of the alleged tax evasion. The IRS did come in—six months after they were asked. "This delay not only hampered the investigation but required additional agent time to prepare an adequate briefing for the IRS agents entering the case some six months after we had initiated our inquiry," Revell said (p. 249).

The well publicized corruption in the U.S. General Services Administration would have been a logical target for IRS. But Justice Department officials, experienced in the delays caused by the Tax Reform Act, decided not to include the IRS in the investigations. Too many problems were anticipated in dealing with IRS, Revell said. An investigation of fraud in a Federal job training program led the FBI to conclude tax evasion had occurred. The IRS was alerted. But the IRS, restrained by the Tax Reform Act, would not say what it

intended to do and Revell admitted that he still did not know what ever came of the case (p. 249).

What other witnesses called the Catch-22 in the Tax Reform Act was criticized by Revell. This is the feature of the act requiring that agencies requesting data from IRS must have significant details about the desired information. But the IRS is precluded by law from giving out any such details. So how, witnesses asked, can we describe in detail information we have never seen and are forbidden from being briefed about? Revell put it this way: ". . . we are supposed to have, in order to obtain this [IRS] information, reasonable cause to believe that the information in the possession of IRS would assist our case." But, Revell said, "We do not know what they have. We do not know what they have obtained, we do not know even what investigations they are conducting so we are in no position to establish a reasonable cause to show the information they have in their possession affects our case." Revell said the disclosure provisions of the Tax Reform Act are more difficult to satisfy than are requirements investigators must meet preparatory to obtaining a search warrant (p. 250).

ONE-WAY

Another problem caused by the Tax Reform Act, Revell said, is that FBI agents are now precluded from discussing investigations with IRS personnel. Important information, essential to the opening and advancing of investigations, cannot be given by IRS to FBI agents, Revell said. Cooperation between FBI agents and IRS investigators has been destroyed, Revell said. FBI agents feel that the relationship with IRS is a one-way street, with the Bureau doing the giving and the Service doing the taking. There was a time, Revell said, when IRS was a charter member of task forces and other coordinated criminal investigative efforts—but those days are gone. Revell said IRS is rarely asked to participate in task forces anymore (pp. 244–245).

Revell talked about the Racketeer Influenced and Corrupt Organization statute. Known by its acronym RICO, this law has been an effective tool for Federal law enforcement against organized criminal groups. The RICO statute enables the Government to forfeit assets and property and shut down companies if they are found to be used in the commission of racketeering acts. Using RICO, the Government can convict a person and sentence him to prison and, simultaneously, immobilize his organization by seizing the business he ran and closing it. But, according to Revell, the Tax Reform Act has set back the Government's investigations required to develop a RICO violation. This is because of the lack of access to financial data held by IRS. Revell said this type of prosecution has suffered, particularly in the FBI's high priority areas such as organized crime, white collar crime, official corruption and foreign counter-intelligence (p. 251).

The IRS View from the Field

Senior Internal Revenue Service officials, speaking for the national office of the Service in Washington, D.C., were reluctant to admit that the Tax Reform Act and their own policy decisions had combined to bring about a diminished effort by IRS in organized crime and nar-

cotics investigations. As is seen later in this report, the IRS officials from Washington sought to assure the Subcommittee that narcotics investigations were being waged as aggressively as ever, and that IRS policy is to cooperate with other law enforcement agencies in bringing drug traffickers and organized criminals to justice. The views of the Washington witnesses contrasted sharply with the statements of three IRS officials who work outside Washington.

It is in the field where IRS special agents say they are most frustrated by the Tax Reform Act. Richard C. Wassenaar was the Assistant Regional Commissioner for the Criminal Investigation Division in IRS's western region. Headquartered in San Francisco, the region covers the 10 most western States. Wassenaar, a veteran of 16 years with IRS, said the feature of the Tax Reform Act which gave him and his special agents the most difficulty was the prohibition against telling other law enforcement agencies about the existence of information that would be of use to them in criminal investigations.

BRIBE

This prohibition may place the IRS investigators in the unlikely position of knowing about the existence of a crime, and of knowing who committed the crime, but being unable to report it, except within IRS. Such a situation was faced by Wassenaar. He said in one instance he came upon information that indicated that a certain policeman had received a bribe. He wanted to present this information to the local authorities. But the Tax Reform Act prohibited it. So he forwarded the information to IRS in Washington. The national office studied the issue and then informed Wassenaar that he was not to do anything with the information. Wassenaar said the policeman was never prosecuted. Wassenaar said he was sorry to say it but the policeman was still on the force. Wassenaar testified, "Senator, this is indeed very frustrating to a law enforcement officer who is engaged in the profession of enforcing the law, knowing in many situations that a violation has been committed but his hands are literally tied from enforcing or passing on the information that would enable the appropriate agencies to enforce the law" (p. 224).

Wassenaar's counterpart in the southwest region was John Rankin, a 17-year veteran of IRS. Rankin said he shared Wassenaar's concern over the Tax Reform Act and how it limits the ability of IRS special agents to assist other law enforcement agencies. Both Rankin and Wassenaar felt they should be able to legally inform another agency of the existence of information about crimes. Senator Nunn asked them what they would do if, in an extreme case, they found the taxpayer had received $50,000 as a down payment for the assassination of the President. Rankin said if he responded as the Tax Reform Act prescribes, he could do nothing more than tell his superiors in Washington. However, if there were immediacy to the information—if, in the extreme hypothetical situation, the assassination attempt was to occur shortly—Rankin said he might take some other action on his own but by doing so he would run the risk of breaking the law (pp. 221–222).

COURT ORDER

Rankin said he did not object to the need for obtaining a court order before IRS could turn over tax information to another agency. But what troubled him was the provision requiring that the requesting agency spell out for the judge considerable detail about information its own personnel had never seen. Wassenaar agreed, saying what he would like to see happen is an amendment to the Tax Reform Act which would provide some mechanism enabling IRS to go to a judge, tell him about the need to turn over certain information to the FBI, for example, and then petition the judge for the approval to initiate the transfer of data to the Bureau. Under existing law, how is the FBI expected to know what to ask for if the Bureau does not even know the information exists? Wassenaar asked (pp. 224–225).

Willard Cummings, Chief of the IRS Criminal Investigations Division in Austin, Texas, testified that there is a Catch-22 air to the problem of cooperating with other agencies. Other agencies cannot ask for information unless they are told about it—and it is against the law to tell them, he said. Cummings, who had been with IRS for 20 years, said the disclosure provisions demoralize law enforcement agents at IRS and elsewhere, because they take up so much time to comply with and because people are beginning to feel it is not worth the effort. This is especially true, he said, when speed is important, as it often is with FBI or DEA cases. The Bureau and DEA are "dealing with information that they need on a daily basis or real quick because of movement of drugs and that type of thing," Cummings said, pointing out that the disclosure provisions, even when they are utilized promptly, are at best cumbersome and time consuming (p. 228).

SYNDICATE

The Araujo case, already referred to in Chapter III of this report, involved a major narcotics syndicate in Los Angeles and Mexico. As a result of this case, a joint effort by the Justice Department, DEA, IRS and Customs, 17 persons were indicted, a $32 million drug organization was dismantled, several severe prison terms were handed out and about $28 million in additional taxes and penalties were levied. But, Wassenaar said, successful as that joint investigation was, a time delay caused by the Tax Reform Act enabled a principal figure in the Araujo case to flee to Mexico. Wassenaar said that some of the delays in responding to the disclosure provisions are not called for in the statute itself but are paperwork requirements laid on by IRS.

Rankin talked about the awkward role of IRS special agents attending organized crime strike force meetings. Attending these meetings are law enforcement agents from several agencies who are briefing one another on what cases they are working. All brief except the IRS people. They can only listen. They are not allowed to say anything about investigations they are pursuing or information they have developed. Rankin said that unless given court approval IRS personnel "can't actively participate in exchanging information with the strike force" (p. 234).

Wassenaar testified about a "sting" operation run by local police in which officers ran an undercover fencing business, buying stolen goods.

Considerable amounts of stolen property were recovered. Having no other way of returning the stolen property to its rightful owners, police went to the IRS with a partial solution. Since much of the property was identified with Social Security numbers, police hoped IRS could match the numbers with the identities and addresses of the owners so the property could be returned. IRS refused to help, saying the Tax Reform Act prohibited such actions (p. 223).

Senator Percy asked if Al Capone, who was finally brought to justice on tax charges, could be prosecuted on similar counts today. Rankin said no. ". . . from what I know about the facts of that situation," Rankin said, "that is the sort of case that takes an extensive coordinated effort by a number of different law enforcement agencies to be able to make the case. You have to have [an] exchange of information on the agent-to-agent basis. It would be extremely difficult to work that sort of case under the [disclosure] provisions of 6103" (p. 225).

PAPERWORK

Rankin also talked about the difficulties caused by the Tax Reform Act when it is to the Government's advantage to have the IRS in grand jury investigations. He said it is valuable to have IRS agents involved in the earliest stages of a complex financial investigation. He said that IRS cannot get involved without first overcoming complicated procedural requirements. These take time and resources and cause IRS to get into the case late—and such impediments are uncalled for in a strictly investigative endeavor, Rankin said. This red tape usually takes four to six months to complete (pp. 229–230).

The witnesses from IRS field installations said that while the Tax Reform Act may have cut back their participation in organized crime cases it has not reduced their level of paperwork. The new law has substantially increased red tape and bureaucratic procedures. The Tax Reform Act calls for twice the amount of paperwork than was required previously, Cummings said. Rankin said that so cumbersome are the paperwork requirements of the statute that agents must take time from their investigations to keep their forms filled out. He said agents have increased their paperwork time allocation by 20 to 25 percent to satisfy the Tax Reform Act (p. 234).

All three IRS field officials—Wassenaar, Rankin and Cummings—criticized the summons provision of the Tax Reform Act, pointing out that it causes substantial time delays, often weakens the Government's case and does nothing to enhance the rights of the suspected tax evader. Wassenaar explained how the provision operates: When a summons is served on a third-party recordkeeper, usually a bank, the taxpayer is also formally advised of what has happened. The taxpayer has the right to object to IRS. When the objection is filed, an automatic stay in the summons is implemented. Now it is up to IRS to take the matter to court. The taxpayer, using a variety of legal maneuvers, can cause the ensuing litigation to drag on for weeks, months and in some instances even years. Throughout this entire procedure, which may be repeated with each new summons, the taxpayer enjoys no new legal rights—but only gains the opportunity to slow down the case against himself, Wassenaar said (pp. 235–236).

33 MONTHS

Making this procedure even more time consuming, Rankin said, is the fact that when one set of documents is finally obtained, these new records often lead to IRS requiring more records. Once again, he said, the taxpayer has the right to invoke the stay mechanism and once again the court proceedings are begun and once again valuable time is lost. Wassenaar said delays caused by a stay last an average of nine months and enterprising defense attorneys have dragged them out for 33 months (p. 237).

Time works against the Government's case in favor of the alleged tax evader. Wassenaar said defense attorneys know this and conduct themselves accordingly. Witnesses move away or die or lose the precision of their earlier recollections. In one case cited by Wassenaar, IRS issued a summons for third-party records of a taxpayer. The taxpayer invoked the stay. IRS took him to court. The proceedings dragged on, month after month. Finally, in the 22nd month, the recordkeeper was directed to turn over the documents. Then the recordkeeper came forward to say that he never had the desired records in the first place. A delay of 22 months—and nothing to show for it (p. 238).

The three IRS field office witnesses proposed amending the summons provision. They said there should be a period following the summons in which the taxpayer can go to court and raise a legal issue as to why the summons should not be enforced. One study showed that by putting such an affirmative legal obligation on the taxpayer the delay problem could be significantly reduced. Wassenaar said that in more than 2,000 stays of summonses experienced in the Western region since the passage of the Tax Reform Act, in excess of 80 percent of the taxpayers that initiated the stays failed to pursue them in court. The conclusion, Wassenaar said, is that most taxpayers who use the automatic stay provision only do so to delay the investigation and rarely show up in court to argue any legal issue (p. 236).

GAO found that 75 percent of the summons proceedings pending in IRS's western region as of June 30, 1979 involved criminals or tax protesters (p. 309).

Compounding IRS's problems with the Tax Reform Act is the Freedom of Information Act. It too has been used to block or stay a summons, Wassenaar said. A common tactic of defense attorneys is to institute a Freedom of Information request upon issuance of a third-party recordkeeper summons. Wassenaar said that during the time the Freedom of Information request is in litigation, the summons enforcement request will not be processed (pp. 237–238).

Testimony of Elmer Staats and Richard Fogel

One of the more graphic illustrations of the problems caused by the Tax Reform Act was given by Elmer B. Staats, the Comptroller General of the United States and the head of the General Accounting Office. Staats described this situation: 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 will not discuss their individual cases as long as the prosecutor is in the room. 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. But if IRS decides to conduct the investigation, it does not so inform the strike force attorney (p. 326).

The strike force example was one of several Staats gave Senators to enable them to better appreciate the difficulties that arise from the Tax Reform Act's rule prohibiting 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. Such a restriction has impact on narcotics investigations as well.

GOALS

Focusing his remarks on the illicit drug trade in the U.S., Staats said Federal authorities have tried hard to reduce the flow of narcotics and some goals have been achieved. But, he said, the drug trade flourishes and the profits are enormous. Staats said the major barriers the Federal Government faces in trying to immobilize the big drug syndicates are (1) legal obstacles, (2) inadequate overall direction, and (3) changing priorities that prevent Federal agencies from fully using and coordinating their skills, jurisdictions and resources. Because of these problems in carrying out their mission, Federal agencies have had only limited success in immobilizing high-level traffickers and their organizations through conspiracy and financial investigation cases, Staats said (p. 322).

Special training and experience are needed for financial investigations, Staats said, and the Drug Enforcement Administration, at this time in its development, does not have that level of expertise generally. But, he said, the Internal Revenue Service does. However, the IRS has not been very effective in the drug area, Staats said. He explained that relatively few criminal investigations of drug traffickers have been initiated by IRS and most cases have not led to convictions (p. 323).

Staats said that although IRS has had some successes in drug efforts, its impact on reducing the nation's drug trafficking problem has been limited. Staats said these factors have inhibited IRS's ability in drug cases: 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. The Justice Department's "dual prosecution policy" provides little incentive for IRS to investigate drug-related tax cases.[5] IRS has limited its use of jeopardy and termination assessments as a means for getting at traffickers' assets. Currency and foreign bank account reports required by the 1970 Bank Secrecy Act have not been used effectively to identify major traffickers. IRS's ability to quickly obtain financial records from third parties has been impaired by the summons provisions of the 1976 Tax Reform Act. And IRS's ability to cooperate and coordinate with other law enforcement agencies has been reduced by the disclosure provisions of the 1976 Tax Reform (p. 324).

[5] For a discussion of the "dual prosecution" policy see page 108 of this report.

RESTRICTIONS

Staats said the Tax Reform Act of 1976 placed certain restrictions on IRS which limited its ability to work with other law enforcement agencies on drug cases. These restrictions result in IRS not being able always to disclose information about non-tax crimes. In addition, Staats said IRS cannot alert Justice attorneys to seek disclosure of criminal tax information. He said coordination between IRS and DEA has been slowed by the disclosure provisions.

In conducting their daily activities, IRS employees sometimes obtain information indicating that a taxpayer has committed a crime outside IRS's jurisdiction. Staats said that if they obtain the information from a third party they can disclose it to the appropriate Federal agency. However, Staats said, if that information is obtained from a taxpayer, the taxpayer's records, or the taxpayer's representative, IRS cannot alert the Attorney General or anyone else of the crime, regardless of how serious it is.

In response to questions from Senator Chiles, Staats said Congress in passing the Tax Reform Act disclosure provisions was "reacting to abuses and it undoubtedly weighed very heavily on the side of privacy in taking that action." But, Staats added, ". . . our investigations certainly support the view that we need to take another look at the Tax Reform Act of 1976 in order to be able to readdress what seems to be an imbalance now between the concerns of our privacy and the concerns about law enforcement. I think there is a tradeoff here that needs to be made and it is a very difficult tradeoff" (pp. 332–333).

REVIEW

Richard Fogel, Senior Associate Director of GAO in the Government Division, accompanied Staats before the Subcommittee. Fogel told Senators it was the clear intent of Congress in adopting the disclosure provisions that there be a third party—that is, the courts—to review the requests for IRS information to attest to their reasonableness. Fogel said, "And given the overwhelming intent of Congress to have that third party review because of documented evidence of past abuses by law enforcement agencies, and improper use of tax return information for other than legitimate law enforcement inquiries, we feel that the provision that was put in the 1976 act is still valid. If agencies come to the IRS, they still should get an *ex parte* court order making sure that the request is reasonable." The documentation for these abuses, he said, was recorded by the Senate Select Committee to Study Governmental Operations with respect to Intelligence Activities, also known as the Intelligence Committee.[6] Its Chairman was Senator Frank Church of Idaho (p. 333).

Past Abuses of Tax Privacy Are Discussed

In its report of April 26, 1976, the Intelligence Committee cited a number of instances in which IRS information was used as an instrument of domestic intelligence mainly by the Federal Bureau of

[6] Senate Report No. 94-755, 94th Congress, 2d session, Book III, pp. 835–920.

Investigation and the Central Intelligence Agency in the 1960's and early 1970's. The uses of the tax information referred to by the Intelligence Committee were in connection with efforts to gain information about political dissidents and persons and groups considered by those agencies to be possible threats to national security. In some cases, the Government attempted to use this information to discredit individuals or destabilize political groups which it considered to be subversive. Additionally, according to the Intelligence Committee, IRS during this same period initiated a number of audits on the basis of political considerations.

ABUSE

The major intent of the disclosure provisions of the Tax Reform Act of 1976 was to prevent this type of essentially political abuse of taxpayer information. On the other hand, the Senate Permanent Subcommittee on Investigations, in its examination of the Tax Reform Act of 1976, attempted to ascertain if there had been abuses in the criminal investigation and prosecution of major drug traffickers and other organized criminals. The preliminary finding of the Subcommittee was that abuses of taxpayer information in major drug and organized crime prosecutions were rare. Although the Subcommittee cannot state with certainty that no abuses occurred in the prosecution of organized crime and narcotics cases, the evidence of any abuse in this area was negligible. Witnesses before the Subcommittee, when asked if they knew of such tax privacy violations, replied that they knew of none.

Richard J. Davis, Assistant Secretary of the Treasury for Enforcement and Operations, was a prosecutor in the U.S. Attorney's Office for the Southern District of New York. He also was an attorney in the Watergate Special Prosecutor's Office, serving under Archibald Cox and Leon Jaworski. Davis said that he could not say there never were any instances of pre-Tax Reform Act abuse of a taxpayer's return by Federal prosecutors, but that he had not heard of any such abuses that would have been illegal or prevented once the disclosure provisions were adopted.

Senator Nunn asked Davis if there were any situations during the Watergate era that would have been addressed by the disclosure provisions of the Tax Reform Act. Davis said there was concern in the Congress during the Watergate era that some citizens' tax returns had been given to the White House and to other offices in the Government. Such actions were said to have been done "for political, as opposed to enforcement, purposes," Davis testified (p. 152).

"Wasn't that already illegal, though?" Senator Nunn asked. Davis replied, "I frankly do not know whether that would have been a crime. It certainly would have violated every regulation that I was aware of, although I must say under existing law, there are specific procedures which in a legitimate case, when there is a need to look at a tax return in connection with the prospective appointment, for example, that the White House can get access" (p. 152).

ASSAULT

Senator Nunn asked if it might have been a more direct assault on the problem of misuse of tax returns for Congress to have passed a very strong statute against misuse of tax returns. Davis agreed. "You don't have to destroy the whole apparatus of the Internal Revenue Service to get at that potential abuse, do you?" Senator Nunn asked. Davis said he did not think so (p. 152).

Irvin B. Nathan, the Deputy Assistant Attorney General in the Criminal Division of the Justice Department, said he recognized the legitimate concerns which led to the enactment of the disclosure provisions of the tax act. But, Nathan said, "I am aware of few, if any, complaints about abuses by prosecutors of tax information which they obtained and used in developing criminal cases" (p. 21).

Speaking about his own agency specifically, Peter B. Bensinger, Administrator of the Drug Enforcement Administration, told the Subcommittee he knew of no instance in which DEA had been charged with misusing tax information (p. 82).

The three witnesses from IRS who appeared before the Subcommittee as a panel said they knew of no instance where tax information had been used improperly by law enforcement officers and prosecutors in preparing criminal cases. John Rankin, Assistant Regional Commissioner for the Southeast Region of the Criminal Investigation Division, said that in his 18 years with the IRS he had not heard of any abuses of taxpayers' returns, before or after enactment of the Tax Reform Act. In a 16-year career with IRS, Richard Wassenaar, Rankin's counterpart in the Western Region, said he had no knowledge of such practices. Willard Cummings, Chief of the Criminal Investigation Division in Austin, Texas, said, "I am the old man, having 20 years with IRS and most of that time spent with the Criminal Division, involved in all types of organized crime activities, back into the 1960's and later years and in my experience I have never seen it used or intended to be abused, or intended to be misused by any other law enforcement official" (p. 235).

PRIVACY

In his criticism of the disclosure provisions of the Tax Reform Act, former Assistant Secretary of the Treasury David R. MacDonald said taxpayers' rights of privacy regarding their returns were protected before the disclosure provisions of the Tax Reform Act were passed. Appearing with MacDonald, John Olszewski, former Director of the IRS Criminal Investigation Division, said the tax return was always treated as "a very confidential, important document for that individual" (p. 277). He added, ". . . there is very little on the tax return that could help or would help the ordinary police agency, including the FBI. The only way it could be helpful to them is if they reported on the return, 'I earned my money from narcotics trafficking.' It would be an admission that they were engaged in an illegal activity. . . . If they are going to take the high risk of engaging in narcotics trafficking, which carries far greater penalties in the long run than income tax evasion, they sure as the devil aren't going to report that money on their tax returns" (p. 277).

The General Accounting Office witnesses believed there was good cause for the disclosure provisions. But even then there were no specific examples cited in which Federal prosecutors made improper use of a citizen's tax return. That point was demonstrated several times as Marty Steinberg, Chief Counsel of the Subcommittee, questioned Richard Fogel, Senior Associate Director in the Government Division of GAO. Their exchange follows:

> Mr. STEINBERG. Mr. Fogel, we were talking about the legislative history of the act and you will agree with me that the only abuses mentioned in the legislative history of the Tax Reform Act were the requests by the President [to] the Internal Revenue Service to provide him with some information. The other abuses that you have mentioned about information gathering in general, is there anything in the Tax Reform Act which prohibits the Internal Revenue Service from gathering information?
>
> Mr. FOGEL. No, there is not, Mr. Steinberg. That is the point I wanted to make. There is nothing that prohibits the Service today from mounting effective criminal tax investigations against anyone, including narcotics traffickers, and organized crime figures.
>
> The only point I was trying to make is that given the whole tenor of the times, with the disclosures on how information was being exchanged between IRS and the FBI, between IRS and the CIA, what the FBI was doing, what the CIA is doing, it is understandable why the disclosure restrictions were enacted. But it is important to point out that we believe very strongly that IRS has a lot of tools available to it right now to effectively go after narcotics traffickers for criminal tax law violations and that there are indeed problems with coordinating with DEA and Justice but there is nothing that precludes IRS from initiating that today.
>
> Mr. STEINBERG. If there is an abuse by a prosecutor or a Federal agent with respect to tax information he receives from the Internal Revenue Service, hasn't it always been a crime for a Federal agent or a prosecutor to disclose confidential information in his files for some ulterior motive, whether it be political or any other motive?
>
> Mr. FOGEL. I believe that is correct. I think it is also correct to emphasize, as one of the earlier witnesses did today, that the criminal and civil penalties imposed in the '76 Tax Reform Act had a chilling effect on those people that had to deal with this information. If my recollection is right, I think the criminal penalties were increased even in the '76 act.
>
> Mr. STEINBERG. The only point I am trying to make is we have had a number of agencies in here, the Justice Department, the DEA, the FBI, even IRS agents and each one of those agencies have been asked specifically to point to any particular abuse of a tax return or tax return information that they were given prior to the enactment of the Tax Reform Act and they said to their knowledge there was none. Are you aware of any specific such situations?

Mr. FOGEL. No. We are not.

Mr. STAATS. You are referring to prior to the 1976 act?

Mr. STEINBERG. Prior to the 1976 act.

Mr. FOGEL. What we are aware of is, I guess, there was a lot, if I could characterize it, loose exchanges of this information among a lot of Federal Government agencies that got people upset.

Mr. STEINBERG. I will only follow up with one more question along this line. Since the act's legislative history seems to be addressed to a President who could ask the Internal Revenue Service to go out and do something against his so-called enemies, does the Tax Reform Act today prevent a President from requesting a Commissioner of the Internal Revenue Service to investigate a person for income tax evasion?

Mr. FOGEL. I have to look at the detail of the act. I can't recall. I know there is a provision in the act that provides for the President to request the IRS to look at the tax returns of a person who is eligible for appointment and there is very strict documentation that has to be followed.

Mr. STEINBERG. That is not exactly the question. The question was not whether or not the President could look at the tax return information in his hands. The question is does the Tax Reform Act as it now stands prohibit a President from asking the Internal Revenue Service to go out and investigate political enemies he has?

Mr. FOGEL. No. I don't believe it does (pp. 337–339).

The Subcommittee also examined the "enemies list" phenomenon—that aspect of the Watergate scandals that had to do with the alleged use of White House power to damage a political opponent. As Senator Nunn pointed out, one of the reasons Congress passed the disclosure provisions of the Tax Reform Act was to prevent a situation in which a President or his immediate staff drafted an enemies list and then set out to develop adverse information on those persons through their tax returns. But as IRS Commissioner Jerome Kurtz said, that kind of behavior is not prevented by the Tax Reform Act, and if a President wanted to do that sort of thing his success or failure would have nothing to do with the Tax Reform Act but with IRS adherence to laws on the books long before Watergate. In short, it has been illegal for many years to make improper use of income tax returns whether by a Federal prosecutor, by IRS or by the President of the United States. This point—the need for the disclosure provisions of the Tax Reform Act in the first place—was discussed at length by Senator Nunn, Commissioner Kurtz and IRS Deputy Chief Counsel Lester Stein.

ENEMIES

Senator Nunn described a hypothetical situation in which a President of the United States drew up an enemies list. He asked the IRS to audit the tax returns of each person on the list. Senator Nunn wanted to know if the Tax Reform Act would in any way prohibit the President from giving the IRS such a directive. Commissioner Kurtz

replied that there was nothing in the Tax Reform Act's disclosure provisions that would prevent a President from doing that, nothing in the disclosure provisions that would make such a Presidential action a crime.

Senator Nunn posed a similar question to IRS Counsel Stein. Is there any language in the Tax Reform Act, Senator Nunn asked, that would make it illegal for the President to tell the IRS to investigate the tax situation of all Presidential aspirants? Stein's answer was no. Senator Nunn projected a hypothetical situation in which the President says to the IRS Commissioner, "Mr. Commissioner, you were appointed by my administration, I have seen these people that are bothering me, would you go and investigate them, 1, 2, 3, 4, 5, 6, 7, 8, 9, 10." Senator Nunn then asked Stein, "Is there anything in the TRA that makes that phone call a violation of the law?" No, Stein replied. (p. 461).

Questioning Kurtz again, Senator Nunn asked about the responsibility of the Commissioner should the President order IRS to investigate the President's rival. In this hypothetical circumstance, if the President said do it and Kurtz did it, would Kurtz have violated the Tax Reform Act? No, Kurtz said, pointing out, however, that in such an action other laws could be violated. Senator Nunn asked Kurtz what other crimes would be violated. Kurtz replied that the crimes would fall under Title 18, the criminal code and would have to do with the abuse of power by a Government official. Kurtz said these laws were there before the Tax Reform Act, even before Watergate (p. 462).

In summary, then, Senator Nunn said, the Tax Reform Act does not prevent or control or discourage or otherwise affect the drawing up of a Presidential enemies list. That is correct, Kurtz said.

CRS Study Cites Example From Watergate Era

During the Watergate period, there were several allegations that the Nixon Administration had tried to use IRS to achieve political gains, and to damage persons perceived to be political enemies.

This tactic was examined in a report issued on March 31, 1976, by the Congressional Research Service of the Library of Congress. Entitled, "Internal Revenue Service: History and Matters Dealing with Oversight of Its Practices and Procedures through 1974," (Exhibit 11, p. 110) the report cited a memorandum given by John Dean to the Senate Select Committee on Presidential Campaign Activities, known as the Watergate Committee. The memorandum, Dean said, was written by himself and John Caufield and it listed the problems the White House was having with IRS. The memorandum said:

> We have been unable to crack down on the multitude of tax exempt foundations that feed left wing political causes.
>
> We have been unable to obtain information in the possession of IRS regarding our political enemies.
>
> We have been unable to stimulate audits of persons who should be audited.

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> We have been unsuccessful in placing RN [Richard Nixon] supporters in the IRS bureaucracy. . . .
>
> In brief, the lack of key Republican bureaucrats at high levels precludes the initiation of policies which would be proper and politically advantageous. Practically every effort to proceed in sensitive areas is met with resistance, delay and the threat of derogatory exposure.

John Dean told the Watergate Committee of a list of persons at odds with the White House who comprised the "enemies list." The idea was that the White House could use the resources of the Federal Government to damage these "enemies." Johnnie M. Walters, the Commissioner of Internal Revenue from 1971 to 1973, said in an affidavit filed with the House Judiciary Committee that Dean called him to a White House meeting on September 11, 1972. At the meeting, Walters said, Dean gave him a list of persons and asked that IRS investigate them.

CONTRIBUTORS

The list was comprised of persons who were contributors to or worked on the campaign of Senator George McGovern of South Dakota, who at the time was the Democratic nominee for President. Walters told Dean that if he initiated such investigations it would be disastrous for IRS and the Administration. Walters said he later discussed Dean's request with Treasury Secretary George Schultz. Schultz agreed with Walters that no such investigations should be initiated. Later that month, Dean called Walters and asked what progress had been made. Again, Walters told Dean such a project would be inviting disaster. Walters and Schultz talked it over a second time and agreed to ignore the request.

On July 11, 1973, Walters turned over the list of the socalled enemies to the Joint Committee on Internal Revenue Taxation. The Committee was investigating allegations that IRS had taken enforcement action for political purposes. The Joint Committee examined the 1970 and 1971 tax returns of the 490 persons on the list. The Committee staff found no evidence that any returns were screened by IRS as a result of White House pressure. The Joint Committee staff also found no evidence that IRS had been unduly aggressive in its attempts to collect unpaid taxes from the so-called enemies.

A White House tape of September 25, 1972 recorded H. R. Haldeman and President Nixon talking about John Dean and Charles Colson, an assistant to the President, and their efforts to use the IRS against political enemies.

> HALDEMAN. Between times, he's [Dean's] doing, he's moving ruthlessly on the investigation of McGovern people, Kennedy stuff, and all that, too. I just don't know how much progress he's making cause I—
>
> President NIXON. The problem is that's kind of hard to find.
>
> HALDEMAN. Chuck [Colson], Chuck has gone through, you know, has worked on the list, and Dean's working the, the thing through IRS and, uh, in some cases, I think, some other

(unintelligible) things. He's—he turned out to be tougher than I thought he would, which is what—

President NIXON. Yeah.

Dean joined the meeting but nothing else shows up on the tape concerning IRS. However, both Dean and Haldeman testified that later, during the same meeting, there was a discussion about the unwillingness of IRS to pursue possible tax violations of political opponents. It was noted that this reluctance was because the IRS employed so many Democrats. Dean testified that the President seemed annoyed and said the Democrats had used this tool well and that after the 1972 election the Administration would place people who would be more responsive to the White House requirements.

HUGHES

In another instance of an attempt to use IRS to damage a political opponent, the Nixon White House tried to uncover irregularities in the tax returns of Lawrence F. O'Brien. He had been a close adviser to President John F. Kennedy, and was in 1972 the Chairman of the Democratic National Committee. John Ehrlichman told Treasury Secretary George Shultz that O'Brien reportedly had made a lot of money and had not properly reported it. Shultz told Internal Revenue Commissioner Walters. Walters recounted what happened next in his House Judiciary Committee affidavit.

IRS had initiated an investigation of the Howard Hughes organization in late 1971 or early 1972. IRS learned that the Hughes organization had paid large amounts of money to O'Brien and his associates. This information was included in the "sensitive case" reports concerning the Hughes investigation. Sensitive case reports were sent to Walters from the field each month to keep him and Secretary Shultz advised of IRS investigations or proceedings relating to prominent persons or sensitive matters.

Walters checked into O'Brien's returns and found that in 1970 and 1971 he had reported large amounts of income, had paid a small deficiency for one year and that the examinations were closed. Walters reported this information to Shultz. Shultz told Walters that Ehrlichman was not satisfied with the report on O'Brien. IRS conducted an interview with O'Brien in August of 1972. Walters said this interview would have been conducted anyway in connection with the Hughes inquiry but probably would have been postponed until after the election but, because of Ehrlichman's interest, it took place before the election. The report of the interview was given to Shultz. Shultz later told Walters that Ehrlichman still was not satisfied.

TACTICS

Later in August, Shultz, Walters and Roger Barth met to discuss the O'Brien case. Barth, Special Assistant to the Commissioner, had been placed in his job by the Nixon White House. The three men agreed there was nothing left to do in the O'Brien matter and that the case was closed. On a three-way extension, they called Ehrlichman and told him of their decision. Walters said Ehrlichman responded by telling him, "I'm goddamn tired of your foot dragging tactics."

In his testimony before the Watergate Committee, Ehrlichman confirmed that he had pushed the O'Brien case. He felt that IRS was delaying an audit of O'Brien until after the election. He was not satisfied with the reasons given for not conducting an audit immediately. Ehrlichman said he wanted IRS "to turn up something and send him [O'Brien] to jail before the election and unfortunately it didn't materialize."

The O'Brien case and others from the Watergate period led the Congressional Research Service to conclude in its report that, "The evidence has shown that with a few exceptions the IRS bureaucracy and its Commissioners withstood efforts to politicize it."

Former IRS Officials Testify on Tax Reform Act

The most frequently prosecuted violations of the tax laws are filing false tax returns, willful attempts to evade taxes and failure to file returns. The men and women who investigate the criminal violations of the tax laws are a force of 2,800 special agents. They work in the Criminal Investigation Division of IRS. The Criminal Investigation Division, or CID, was known as the Intelligence Division until 1973 when it was renamed. In the decentralized IRS organization, CID special agents are assigned to the seven regions, 58 districts and 10 service centers throughout the nation.

The Subcommittee called four former senior officials of the CID to testify. All veterans of many years in the Intelligence Division, the four former IRS officials were outspoken in their condemnation of what had become of the criminal investigation and intelligence gathering capability of the IRS. They were especially critical of the Tax Reform Act, both its disclosure provisions and its summons provision. But the IRS itself, uneasy with criminal tax investigators working on high level organized crime and drug cases, was already doing its best to undercut the Intelligence Division, they said, so that when the Tax Reform Act came on the scene its limitations and restraints were virtually welcomed with open arms by Service policymakers.

Eugene Peter Twardowicz, a veteran of 17 years with IRS intelligence, told the Subcommittee the Tax Reform Act had had a "devastating and debilitating" effect on criminal tax enforcement (p. 291). Twardowicz, who now works for the U.S. Attorney's Office in Baltimore as an investigator, was the lead IRS agent on the investigations that resulted in the prosecutions of Vice President Spiro T. Agnew and Maryland Governor Marvin Mandel. Neither the Agnew nor the Mandel case could have succeeded had the Government been forced to operate under the restrictions of the Tax Reform Act, Twardowicz said.

SMALL

Twardowicz said the tax statute curtailed the ability of IRS special agents to develop high level narcotics, organized crime and white collar crime cases. The limitations in the act are too severe, he said, pointing out that some agents have focused on smaller tax cases rather than aspire to make the big prosecutions because it is at that level where the Tax Reform Act can be the most frustrating.

Twardowicz said the summons provision of the Tax Reform Act is a major obstacle to successful prosecution of tax evaders. He said sophisticated tax cheats are the ones who use the summons provision, invoking the automatic stay mechanism to force delay after delay. The summons provision paralyzes IRS's ability to collect records, documents and other essential evidence, he said. These lengthy delays disrupt the rhythm and momentum of investigations, causing cases to linger for years, Twardowicz said. He said smalltime tax evaders—of the "ma and pa" variety—do not ordinarily invoke the stays so IRS agents are tempted to devote their time to investigating them. Meanwhile, the organized criminals and drug traffickers—the well-to-do violators who know the value of and can afford defense attorneys—invoke the automatic stay procedure at every opportunity. Rather than face that kind of frustration and delay, some IRS agents don't pursue the big tax evaders.

High level tax evaders now have the ability to delay proceedings and cause cases to drag on for years. "Records often lead to other important records and defendants who now have the ability to automatically stay and suspend IRS summons after each records request can effectively delay and impede investigations indefinitely," Twardowicz said (p. 291). He said procedures for disclosing pertinent information to other agencies have virtually stopped such exchanges from happening and have adversely affected law enforcement attempts to identify major suspects, collect evidence and pinpoint large sums of untaxed dollars controlled by criminal syndicates.

So confusing are some provisions of the Tax Reform Act that some special agents, fearful of the threat of civil penalties from violations of the law, now do investigations of small wage earners, Twardowicz said. "This category of violator, i.e., the average taxpayer, typically does not have the resources to delay and impede the progression of criminal cases as compared to an organized crime figure or a large scale narcotics trafficker," he said (p. 291).

THREATS

Twardowicz said that by 1978 the Tax Reform Act of 1976 was having a detrimental effect on his ability to conduct high level investigations. He said, "It was my firm belief that the investigative limitations imposed by the Tax Reform Act would effectively impede any legitimate effort or initiative to immobilize major criminal figures . . . " (p. 286). So, effective September 1978, Twardowicz quit and went to work for the U.S. Attorney's Office in Baltimore.

E. J. Vitkus, who retired from IRS in 1976 after a 26-year career, said the Tax Reform Act is jokingly referred to by IRS special agents as the "Tax Reform Act for Organized Crime." In its implementation, the act causes "daily frustration and friction" he said, citing one instance in which five IRS investigators were threatened with indictment by a U.S. Attorney because they would not disclose the whereabouts of a fugitive. "A peaceful solution" to the dispute was reached, he said, but only after IRS headquarters in Washington, D.C. stepped in with a new interpretation of the Tax Reform Act that persuaded the five that they could reveal the location of the

fugitive and still not be charged with violation of the law. Such disclosure problems will be avoided only when the law is amended, Vitkus said (pp. 300–301).

Vitkus urged the subcommittee to amend the summons provision of the law. As presently written, the summons procedures serve primarily to enable defense lawyers to achieve delay after delay, allowing pre-trail maneuvers to drag on for inordinate lengths of time, Vitkus said.

In Vitkus's experience, the problems at IRS preceded the Tax Reform Act. The trouble began in 1974 shortly after Donald Alexander was named Commissioner of IRS. Neither Alexander nor his chief associates sought to conceal their lack of enthusiasm for the work of the Intelligence Division, Vitkus said. Vitkus, who was Assistant Regional Commissioner for the southeast region with offices in Atlanta, said Alexander was looking for an excuse to undercut the Intelligence Division. Then allegations appeared in the Miami area news media that enabled Alexander to weaken the Intelligence Division, Vitkus said. The allegations, concerning an IRS Intelligence gathering project known as Operation Leperchaun, were that an IRS informant, Elsa Gutierrez, code name Carmen, had been directed to engage in sexual relations with several prominent Miami area men who were suspected of corruption and tax evasion. The central point of the Gutierrez story was the allegation that the IRS, under the guise of official work, was spying on the personal lives of American citizens. The story broke during the Watergate era when considerable doubt had been raised about the wisdom of Government covert operations.

PUNITIVE

The allegations signalled the end of the Intelligence Division as he had known it, Vitkus said. He said that even though a subsequent grand jury investigation proved the allegations against IRS groundless, the article did set in motion a series of punitive actions that destroyed morale and ultimately rendered the intelligence unit incapable of doing effective work in drugs and organized crime cases. An "in-house witchhunt" ensued, complete with what Vitkus termed "recriminations, abuse and humiliation" (p. 296).

The turmoil at IRS over the Miami allegations was not the fundamental cause of Alexander's actions in reducing the role of the Service in strike force and narcotics traffickers program activities, Vitkus said. The Commissioner had merely seized on the occasion of media charges, and the embarrassment they caused the Service, to weaken the Intelligence Division, Vitkus said. Alexander neither believed in nor had much confidence in his criminal investigative cadre. The media allegations "gave him the opportunity to accomplish his objectives," Vitkus said.

Vitkus said critics were caught up in Watergate fever. Vitkus said the same fears had caused similar overreactions at the Central Intelligence Agency and the Federal Bureau of Investigations. Like the CIA and the FBI, the IRS, at least as far as its intelligence unit was concerned, became a casualty of Watergate, Vitkus said.

Watergate hysteria, inflamed by the media allegations, led to the curtailing of valuable programs in which the IRS "paralyzed the strike

force and narcotics traffickers program." Vitkus said. All information gathering activities throughout the United States were stopped, Vitkus said. IRS internal inspectors "flooded the Miami area," Vitkus said, recalling that special agents were interrogated, intelligence files were broken into, unfounded rumors of additional alleged IRS abuses were allowed to spread throughout the Service, special agents with proven integrity were threatened with transfer, field managers were called to Washington for the sole purpose of seeing Commissioner Alexander testify before Congressional Committees and some agents were "abused and intimidated beyond belief," Vitkus said, adding, "Every executive conference became a forum to ridicule past practices in the Intelligence Division. Public affairs offices in IRS ground out endless mea culpas which can best be described as some form of self-flagellation. The Service became a living nightmare of frustration and intimidation" (p. 299).

JURY

The Subcommittee established that a Federal grand jury in Florida examined allegations against IRS personnel in intelligence gathering operations in the Miami area. The grand jury issued "No True Bill" which meant no probable cause existed to prosecute any IRS agents or their supervisors for any violation of Federal criminal statutes. In addition, the Senate Intelligence Committee examined operation Leprechaun. The Committee cited certain instances of inadequate internal controls in Leprechaun but concluded that "most of the allegations which comprised Operation Leprechaun were unfounded." [7]

Vitkus said the 26 years he spent at IRS convinced him that the Service would never be comfortable with the operation of an Intelligence Division or, as it is now called, a Criminal Investigation Division. For that reason, he recommended that the CID be removed from the IRS and made accountable directly to the Treasury Department. That way, Vitkus said, the CID's pre-eminent ability to do financial investigation would be sustained and put to good use, and at the same time the IRS could devote itself entirely to tax administration and need not concern itself with the question of how to manage criminal investigations. "The present structure subordinates criminal enforcement and leaves far too much to the likes and dislikes of individuals who have little or no criminal enforcement background," Vitkus said (p. 300). Moreover, he added, the mobility and scope of criminal activities cross political boundaries and call for a new operational structure such as putting the CID under Main Treasury.

Vitkus said that the other alternative is to leave the CID within IRS—but to give the Division the organizational authority to report directly to the IRS commissioner.

A strong endorsement of the now defunct narcotics traffickers program was given the Subcommittee by two more former officials. John J. Olszewski, who retired from IRS in 1975 after 26 years; and Lee Venable, a 28-year veteran who retired in 1978. Pointing to the immediate success of the narcotics traffickers program (NTP), they said

[7] P. 911, Intelligence Committee report.

that in the program's first year—1972—45 major narcotics dealers were convicted of tax evasion (p. 283). They provided seven examples of narcotics dealers who were convicted for tax evasion under NTP in the first two years. On January 29, 1972, Richard Barksdale was sentenced in Indianapolis, Indiana to 15 years in prison and was assessed a civil taxes penalty of $514,737. In Brooklyn, on September 5, 1972, Vincent C. Papa received a 12-year sentence and got a tax penalty of $158,554. Morris L. Williams, convicted on September 28, 1972, in Detroit, was sentenced to four and one-half years, penalized $111,146.39 and fined $5,000. Less than a month later in Detroit, on October 11, 1972, Lestar Ramsey received a 10-year sentence, a $5,000 fine and a penalty of $100,582.96. The largest of these civil tax penalties was levied on James Davis, Jr., in the amount of $1,777,344, following his conviction in Columbia, South Carolina court and his sentence of two years in prison and three years' probation. A $155,204 tax penalty was given Anthony Passero in Brooklyn on April 10, 1973 where he was given a 30-month prison term. And in Baltimore, on November 2, 1973, Gordon King was directed to pay $341,073 in civil taxes penalties and sentenced to six years' imprisonment (p. 284).

EXEMPTED

Olszewski, who was national director of the Intelligence Division from 1972 to 1975, rebutted the view, articulated at the time by IRS Commissioner Alexander, that the Service should not concentrate its tax enforcement effort on any specific group, but should instead focus on ordinary taxpayers. Alexander, for example, in a speech in 1974 in Honolulu before the American Bar Association, had said, "For the Internal Revenue Service to place a disproportionate emphasis on collecting one particular tax or enforcing the revenue laws for a particular group of people, in effect, puts the Service in a position of setting itself up as a judge between good and bad in our society. Clearly, under such circumstances, the IRS ceases to view all taxpayers as being equal before the law." To that Olszewski said, by not specifically going after criminals suspected of evading taxes, the IRS has created a "de facto tax exempt group—the narcotics financiers" (p. 284). Criminals frequently do not even file returns, he said.

Olszewski said drug trafficking is "one of the most heinous and corrupting activities in our society." He added, "Admittedly, the tax laws were not created to cure social ills. On the other hand, I don't believe Congress intended for the IRS to virtually ignore the taxability of the huge profits from an activity such as narcotics trafficking which creates the social ill" (p. 284).

Olszewski also pointed out that the IRS has devised an elaborate computerized formula that, with a high degree of reliability, can flag an irregularity or anomaly in an ordinary return. Then, in the normal course of events, once a return is flagged for the anomaly, an experienced analyst is called in to study the return to determine whether further inquiry is needed. However, Olszewski said, no such computerized early warning system is in place for criminals. "I know of no mathematical formula which can be computerized to identify a tax violator who is a narcotics trafficker or financier, as has been

devised for ordinary taxpayers who claim excessive deductions for contributions, medical expenses or exemptions" (p. 284).

EFFECTIVE

Venable, whose last job at IRS was from 1970 to 1976 as chief of the operations branch of the Intelligence Division, testified that he was continuously under pressure from his superiors outside the division to make intelligence gathering more cost effective. Venable said an investigations unit should not be judged on the basis of costs versus collections. His job in intelligence was to encourage compliance by investigating and bringing to justice major criminal tax evaders. The Intelligence Division was not supposed to collect taxes, he said, so why try to measure its effectiveness in terms of revenues collected (p. 281).

When the Miami area media revelations appeared alleging that IRS was spying on prominent Floridians' sex lives and drinking habits, Venable said, "disastrous" consequences followed. He said the intelligence gathering program was reduced and the centralized information dissemination effort discarded. The undercover agent group was disbanded. Rigid restrictions were placed on the use of informants, the result of which was that many valuable informants stopped cooperating. Restrictive measures were placed on the use of cars, weapons, radios, surveillance and surveillance equipment. Severe overtime restrictions were imposed on agents, effectively limiting work hours of criminal investigators from 9 AM to 5 PM, Venable said, adding, "Naturally, since criminals don't keep regular hours, the IRS intelligence and evidence gathering and ultimately the enforcement program suffered." Venable said these new policies were handed down from IRS headquarters to the field where regional commissioners and district directors "got the message" and placed a low priority on intelligence and investigative work (p. 282).

Venable said that another new development in the Criminal Investigation Division was that the division frequently no longer controlled its own files. This discouraged agents from filing crucial information—the identity of confidential informants, for example—because of the fear that the files were not secure, Venable said.

Venable was also critical of the IRS policy of delegating to the Drug Enforcement Administration in the Justice Department responsibility for identifying major narcotics traffickers. He said the policy sounds fine but in reality is inadequate. "The expertise of DEA lies in the area of interdicting the flow of hard drugs, not identifying and tracing complex movements of money to identify the true financier," he said (p. 282).

In summary, the four former IRS officials made the following six points as to why IRS should devote special attention to criminals. They said: (1) criminals earn their money illegally; (2) criminals not only evade taxes, they cause social problems; (3) they conceal their profits; (4) since criminals do not generally file returns, routine audit checks are of little value; (5) the amount of taxes they evade is substantially more than the tax evader who earns his money legally; and (6) special detection techniques are needed to determine if they underreported their taxes or did not file.

V. IRS ATTITUDE

DONALD ALEXANDER'S SPEECH IN HONOLULU

It was not only the Tax Reform Act of 1976 that led to the weakening of the Internal Revenue Service's involvement in criminal tax investigations of drug traffickers. Nor was it only the embarrassment caused by the allegations printed in the Miami area news media of IRS informant Elsa Gutierrez, code name Carmen, in Operation Leprechaun. As much as any other factor in the decline of the investigative resources of the Service was the attitude, held by some senior IRS policymakers, that criminal investigations did not belong at IRS, that it was risky, potentially embarrassing to use the tax statutes for collection of revenue from organized crime figures and drug traffickers. In short, the organized crime and drug trafficker investigative effort was an unwanted police function, an unneeded burden to the orderly administration of the tax laws. This attitude existed at IRS, according to the testimony of witnesses like E. J. Vitkus, Eugene Peter Twardowicz, John Olszewski and Lee Venable, former officials of IRS and longtime veterans of criminal tax investigation and intelligence gathering. Each of these men told the Subcommittee that they had seen firsthand this attitude manifest itself at IRS and seen firsthand the injurious effect it had on special agents' morale and effectiveness.

The statement that reflected best the attitude that troubled the law enforcement proponents at IRS was the text of a speech issued on August 14, 1974 by Commissioner Donald C. Alexander, who was addressing the annual convention of the tax section of the American Bar Association meeting in Honolulu (exhibit 38, pp. 496–507). To varying degrees, this speech supports many of the things Vitkus, Twardowicz, Olszewski and Venable said about the attitude of IRS management toward the Intelligence Division. One of the main points of Alexander's speech in Honolulu was the assertion that IRS has the mission of tax administration as its primary duty. Accordingly, IRS should not be asked to do more. Because for years IRS did its job so well, Alexander said, people assumed the Service could do much more. As a result, all sorts of non-tax responsibilities were handed to the IRS, functions which in his opinion did not really belong there. The result was that resources were strained, new problems arose and the Service's primary job of tax administration suffered, Alexander said.

MIXED

Alexander spoke of IRS's reputation for good work as being a mixed blessing. A good reputation, for all its value to a Government agency, can also bring about unwanted assignments. Alexander said he was tempted at times to plant a few trumped up stories in the media about

"how poorly we are doing." The idea of such a move would have been to make Congress think twice about giving IRS any new mission, Alexander said. In the past 15 years, he said, IRS had been given responsibilities in fire arms control laws, revenue sharing, the economic stabilization program, enforcement of Federal energy conservation activities and there was now serious discussion about IRS receiving the assignment of administering the proposed income maintenance program or, as it was known, the negative income tax for improving the nation's welfare system.

Surely, Alexander said, IRS did not have a monopoly on efficiency in Government. In turn, the road in search of competent administrators for Government programs should not always lead to IRS. Alexander said he wished "the other Federal planners and executives would leave us alone and quit trying to give us additional responsibilities, particularly in the non-tax area." Even before his appointment as IRS Commissioner, Alexander had been apprehensive about the growing numbers of non-tax functions which had been given to the Service. "My experience as Commissioner quickly showed me that my concern was well placed," Alexander said, "and I began to take steps to ameliorate this situation."

The steps he took included turning back to the Bureau of Alcohol, Tobacco and Firearms the firearms control functions and pulling out of several energy-related duties. These and other non-tax responsibilities behind him, Alexander was then able to plan for the return of more than 1,000 experienced revenue agents to the field and the auditing of tax returns. In a similar vein, Alexander referred to the "social and political turmoil" of the 1960's and early 1970's when "the forces of hardline law and order" encouraged the use of IRS for criminal law enforcement. "IRS participation in the organized crime drive of the Justice Department and in federally-led strike forces in the major cities around the country were the first manifestations of this movement," Alexander said. "Following that, there came the narcotics traffickers program," he added. From these programs, Alexander said, from the "adoption of this general philosophy," IRS then created a section whose function was to investigate the financial affairs "of a variety of right and left wing organizations" whose potential activities could lead to violence, Alexander said. In his prepared remarks, he did not, however, demonstrate why IRS's role in organized crime inquiry should result in the Service then going into investigations of right and left wing political groups. Alexander terminated the investigation of extreme political groups because these organizations' "activities, legal or illegal . . . had little direct relationship to the administration of the tax laws."

PROTESTERS

Alexander also stopped the practice of special agents in the field who were spending many hours investigating anti-Vietnam War protesters who selectively refused to pay certain percentages of their Federal tax. The protesters hoped that this tactic would disrupt revenue collection procedures. This was a time consuming pursuit for IRS personnel to be involved in, resulted in small revenue collections and it was far outweighed by the cost of the manhours invested. Alexander

added, ". . . the definition of tax administration was permitted to stray from its proper emphasis. If our tax administration is either permitted or encouraged to respond selectively to such sociopolitical phenomena as are likely to crop up from time to time in our pluralistic nation, or if it permits itself to be used as a selective tool which places criminal enforcement or other criteria before revenue collection and enforcement, we may be jeopardizing our traditional tax administration processes, both from the standpoint of the most effective use of our resources and from the standpoint of the public's faith in an impartial, non-political tax system."

His perception of organized crime investigations being on a par with inquiries into political groups showed up several times in Alexander's speech. Talking about IRS's long standing policy of attaining publicity for criminal tax cases in order to "make an example of the offender" and thereby encourage compliance by the rest of society, Alexander again lumped into one category organized crime, narcotics trafficking and political dissent. He explained that the publicity approach had its pitfalls. " . . . this policy, like those resulting in an excessive emphasis upon drug dealers or anti-war protesters, could have the effect of directing a disproportionate share of the Service's enforcement efforts and resources toward a relatively small segment of our total population. This might mean that certain other portions of our society would escape their obligations. Both aspects, in my view would seem inappropriate from the standpoint of a fair and impartial administration of the nation's tax laws," Alexander said.

LAWBREAKER

Alexander went on to say, "As regards our intelligence operations, the overall emphasis of our criminal enforcement activities has been shifted away from special enforcement programs such as narcotics traffickers and strike forces, and have been aimed more directly toward the taxpaying public in general. This shift in emphasis has enabled us to achieve greater occupational and geographic coverage and our criminal tax sanctions are more equitably applied—reaching the broadest possible spectrum of society within our resource limitations. I believe that our revised enforcement policy not only achieves this goal, but more fully meets the intent of Congress in that our resources are being used for the enforcement of tax statutes, rather than as alternative methods for the prosecution of laws normally enforced by other Federal or local agencies." Nowhere in his speech did Alexander refer to the fact that some major organized criminals and narcotic traffickers enjoy sizable income from their illegal enterprises and often they do not pay taxes on this income.

Alexander warned that in trying to limit the work of the IRS to tax administration and little else he might be fighting a losing battle. He felt he might fail in his effort to "redefine tax administration" because his position was based on principle and "principles and ideals have been losing more and more battles to pragmatism and expediency in recent years."

But, Alexander said, he would continue to work to redefine tax administration his way. He would see to it, for example, that all IRS

involvement in anti-narcotics and strike force activities would have to measure up against "revenue and professional criteria" which are guidelines for use of all IRS resources. In the future, Alexander said, law enforcement would have to "compete openly and equally for resources against our regular tax administration activities."

INSIGHT

A paragraph from the Commissioner's speech provided insight into his thinking. It follows: "For the Internal Revenue Service to place a disproportionate emphasis on collecting one particular tax or enforcing the revenue laws for a particular group of people, in effect, puts the Service in a position of setting itself up as a judge between good and bad in our society. Clearly, under such circumstances, the IRS ceases to view all taxpayers as being equal before the law. Such practices by the Service, however, rightly viewed and supported by other forces of the Federal executive, by Members of Congress, or even by a large portion of the population in general, can only serve to the detriment of the integrity of the tax administration system. Selective enforcement of tax laws, designed to come down hard on drug dealers or syndicated crime, for example, may be applauded in many quarters, but it promotes the view that the tax system is a tool to be wielded for policy purposes, and not an impartial component of a democratic mechanism which applies equally to all of us. I need not tell you here this afternoon that the Service is already having some public image problems in that respect."

The Impact of the New IRS Policy

The policy articulated in the Alexander speech was a significant change from the previous IRS approach to law enforcement and tax collection. David R. MacDonald, who was Assistant Secretary of the Treasury for Enforcement, Operations and Tariff Affairs when the Alexander policy took hold, testified what he saw happen. "When I first arrived at the Treasury Department in 1974," he said, "I found a distinct change in the policy of IRS with respect to criminal enforcement. IRS's new management team was withdrawing itself from any emphasis on law enforcement. They substantially decreased their commitment to narcotics and organized crime and instead aimed their program at the average taxpayer" (p. 260).

MacDonald said this change in policy was strictly an in-house affair, with no advice sought from Congress. MacDonald said the decision was made with no apparent justification, such as a study, but seemed to be made by and for IRS without reference to anything else. MacDonald said he favored IRS's former policy of "tough law enforcement towards high-placed criminals." He said that policy was effective and no evidence was ever presented to him to justify why it was being abandoned (p. 260).

MacDonald said his own experience in tax matters had convinced him that a valuable method of encouraging compliance among ordinary taxpayers is to prosecute wealthy mobsters for tax evasion. Such cases receive wide publicity, he said, and serve two useful purposes.

First, the average American, seeing a mobster convicted of tax evasion, concludes that if a shrewd and ruthless hoodlum cannot beat IRS then he can't either. And second, ordinary taxpayers find consolation in paying their taxes voluntarily if they see someone who tried to circumvent the law get caught. Nothing so effectively promotes compliance as does the sight of a bigtime tax cheat going to jail, MacDonald said.

EQUALS

Donald Alexander's desire for an "impartial" tax collection system could not be faulted, according to Irvin B. Nathan, Deputy Assistant Attorney General in the Criminal Division of the Justice Department. But, while the revenue collector ought to be impartial, fair and collect from everybody, he should not be so impartial that he treats all tax evaders as equals. "Of course, we want impartial tax collection," Nathan said, "but we also want increased emphasis put on those criminals engaging in high profit crimes, crimes that involve a tremendous amount of money and, of course, involve the dangerous substances of narcotics" (p. 41).

The policy spelled out by Donald Alexander in Honolulu did not expire when he stepped down as Commissioner in 1977. Nathan said the men and women at the top in IRS still believe as Alexander did. Jerome Kurtz, who succeeded Alexander as Commissioner, testified before the Subcommittee that IRS should not be overly attentive to organized criminals and drug financiers. ". . . there would be risks to the voluntary compliance system if a disproportionate amount of our criminal enforcement resources were directed against any one particular sector of our society, with the effect of ignoring tax crimes in other sectors," Kurtz said. "We simply do not have enough information to know with certainty how the compliance of otherwise respectable citizens earning their income from legal sources would be affected if we concentrated the bulk of our criminal investigative resources against racketeers or narcotics traffickers." Kurtz said IRS is conducting research into why people comply with the voluntary tax system. But until more information is available, Kurtz said, IRS would rather have ample investigative capability to pursue tax evasion in legal enterprises and not allow the investigative programs to become unbalanced with a tilt toward illegally earned income (p. 378)

The Testimony of David R. MacDonald

Criticism of IRS' attitude toward law enforcement came from David R. MacDonald, who served from 1974 to 1976 as Assistant Secretary of the Treasury for Enforcement, Operations and Tariff Affairs. MacDonald, who went on to become the Undersecretary of the Navy from 1976 to 1977, now practices law in Chicago. His Assistant Secretary position at Treasury made him the senior adviser to the Secretary of the Treasury on law enforcement matters. In addition, he had supervision over the law enforcement work of the Secret Service, the Customs Service and the Bureau of Alcohol, Tobacco and Firearms. He did not supervise the Internal Revenue Service law enforcement function. While IRS was the only component of Treasury law enforcement

activities he did not supervise, MacDonald did have the responsibility to advise the Secretary concerning IRS's enforcement policy and procedures.

MacDonald said IRS' record in bringing racketeers like Al Capone and Frank Costello to justice is one that the Service can take pride in. IRS, he said, by its successes in the organized crime and narcotics field has taken important strides forward in persuading the average taxpayer that "the organization that can bring major hoodlums to justice can easily catch ordinary tax cheaters." IRS' vigilance regarding gang leaders is also valuable in a voluntary tax system like this nation's because it serves to assure honest taxpayers that no one will long get away with flouting the tax law, MacDonald said (p. 260).

ENFORCEMENT

MacDonald sought to show the Subcommittee how IRS' role in enforcement differed from but still complemented the work of other Federal agencies. ". . . in areas such as organized crime and narcotics trafficking many agencies could attack the actual crime in progress and thus apprehend the lower and middle echelon criminal. However, it also became quite clear to me, through my position in the Treasury Department, that to attack the people who gave orders and made the most ill-gotten gains, complex financial investigations were a necessity. The organized crime leader or the narcotics financier may never involve himself in the day to day criminal affairs of his criminal enterprise. In fact, this high echelon criminal usually spends substantial time, energy and resources in insulating himself from the people who actually commit the crime. This is why IRS was such an integral and necessary part of the Government's overall efforts in law enforcement. Their expertise, ability finanical information, combined with the hard criminal intelligence of other Federal agencies, enabled the Government to go up the line and convict drug kingpins and highly placed mob officials" (p. 260).

The general public feels about taxes and the IRS much the way he does, MacDonald said, calling to the attention of Senators a 1966 study sponsored by IRS and the Justice Department and conducted by the University of Michigan. The study clearly shows, MacDonald said, that the public wants criminals to pay their rightful taxes and expects the Government to focus sufficient resources on prosecuting tax evaders—and forcing them to pay what they owe (p. 261).

It became apparent to MacDonald early in his tour at Treasury that IRS management did not share his views about the need to demonstrate to the public that everybody, including mobsters, had better pay his taxes. Senior IRS managers "substantially decreased their commitment to narcotics and organized crime and, instead, aimed their program at the average taxpayer," MacDonald testified. He said he was never shown a study or research effort to support IRS policy in this regard. It was done more or less "by bureaucratic fiat," which made it doubly troubling to him because it was done without anyone informing Congress. In fact, MacDonald said, specific appropriated monies earmarked by Congress for the principal illicit drug effort, the Narcotics Traffickers Program, were diverted by IRS and spent for something else (p. 260).

DISRUPT

The Narcotics Traffickers Program (NTP) was established at President Nixon's direction in 1971 to disrupt the narcotics distribution system through intensive tax investigations of middle and upper echelon drug dealers. The decision to dismantle the NTP dealt a severe blow to the ability of the IRS to make good use of its resources in the narcotics field. MacDonald said he asked IRS officials for an explanation of why they had begun to draw back from NTP. It was explained to him, he testified, that the lack of cost effectiveness of NTP was their reason for not getting behind the program. Anyway, IRS officials told him, the targeted cases under the NTP were not tax related. MacDonald said senior IRS officials told him the money allocated to the NTP could be better spent in other IRS programs (pp. 260, 261).

As Assistant Secretary of the Department, MacDonald directed studies into the IRS argument about NTP. He said the studies put the lie to their assertions about NTP. He cited figures showing that in fiscal year 1974 IRS office auditors examined 1,495,000 returns, most of them from low and middle income taxpayers engaged in legal activities. Additional taxes and penalties recommended totalled $335.3 million—or $230 per return. During the same year, he said, the IRS examined 2,030 cases under the Narcotics Traffickers Program and recommended civil assessments and penalties totalling $69.5 million—$34,236 per case (p. 261).

MacDonald said the problem was IRS' ineffective collection system, not the Narcotics Traffickers Program. MacDonald said that "the IRS staff did not vigorously follow-up and collect assessments in narcotics cases. In many cases, narcotics traffickers with experienced lawyers and accountants made assets harder to find. In many cases, IRS civil collection staff took so long to attempt to collect that traffickers disposed of their assets or hid them effectively. This lack of effectiveness of IRS collection was a problem which IRS should have addressed to increase these collections, rather than to criticize the NTP. The assessments were monumental under the program. It was up to IRS to collect them. I should add that it is much easier for IRS to collect an assessment against an average taxpayer of a couple of hundred dollars than it is to find and collect the assets of a major narcotics trafficker" (p. 262).

CIVIL

MacDonald said the IRS civil enforcement effort was continuing to concentrate on the "little guy." MacDonald went on to say that one reason for the focus on ordinary taxpayers is that, unlike honest people, "criminals do not willingly cooperate with the tax authorities. They do not even file returns in many instances," It was his understanding, MacDonald said, that as many as 25 percent of the NTP cases involved persons who had not even bothered to file income tax returns (p. 261).

Officials shaping IRS policy in the crime field next told MacDonald that IRS should be an impartial tax administrator and not aim at any particular group of persons, even if they are narcotics traffickers or

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organized criminals. That contention was found to be the heart of the prevailing IRS philosophy at the time the Service was disengaging from the drug and organized crime field. The principal consideration here seemed to be that all taxpayers should be treated equally. No one should become the target for inquiry. MacDonald disagreed, saying that to ignore criminals while focusing on ordinary citizens was not equal either; it made ordinary citizens the target (pp. 265, 266).

The next criticism of IRS' role in narcotics and organized crime investigations had to do with the authority to terminate tax years and make jeopardy assessments. MacDonald said he was told there was deep concern at IRS over the possibility that this authority would be misused or abused. When IRS uses its authority to terminate tax years and to make jeopardy assessments, revenue agents step into a person's business and declare that his tax year has ended, estimate his profits, levy a tax and then seize it. This tactic is applied in instances of blatant disregard of tax liability and when it is clear that the targeted entrepreneur has no intention of paying his taxes. MacDonald said IRS agents had used this authority against drug dealers under the Narcotics Traffickers Program. These actions resulted in assessments and seizures totalling $140 million in fiscal year 1973, MacDonald said. By fiscal year 1975, with the new IRS policy in place, jeopardy assessments came to only $3 million in the NTP program, MacDonald said. He said rarely did anyone contest a jeopardy assessment. In 4,000 instances of this technique, he said, there were only eight or nine adverse court actions (p. 261).

TOO COSTLY

Trying to persuade IRS to strongly support the NTP rather than to undercut it, MacDonald cited statistics which demonstrated its value as a revenue collector. To the IRS assertion that NTP was too costly, MacDonald pointed out that IRS had distorted the figures to prove its case. IRS was saying the NTP cost $53 million and brought in only $34 million. MacDonald said $32 million in costs of the Intelligence Division of IRS were charged to NTP. That was inappropriate, MacDonald said, explaining that only collection programs are evaluated on the basis of revenues made versus costs. "The activities of the Intelligence Division are not directly related to revenue collections," he said, "its principal purpose is to encourage voluntary compliance with the self-assessment system." MacDonald went on to say, "Moreover, seizures of cash and property totalling some $33 million were not added to the amounts of assessments actually collected which was $34.5 million by IRS management. This would effectively double the revenue figures. In addition, total assessments of over $231 million were due and owing at the time IRS prepared its figures and no credit was given to the NTP for moneys that would be collected in the future as a result of the program" (p. 262).

The Dismantling of the Narcotics Traffickers Program

The Narcotics Traffickers Program was established at the Internal Revenue Service in 1971 at the direction of President Nixon. Its purpose was to disrupt the narcotics distribution system through inten-

sive tax investigation of middle and upper echelon drug dealers. One of the methods used in the NTP program was to declare a known narcotics violator's tax year terminated, levy a tax and then seize it. By 1975, the NTP had been dismantled.

According to the GAO report of October 25, 1979, the decision to abandon the Narcotics Traffickers Program was made by IRS Commissioner Donald Alexander, who believed that "IRS exceeded its cash-seizing authority and because of the program's low revenue yield." Alexander also felt the public's trust in the IRS as an impartial administrator of the tax laws is vital and could be jeopardized when IRS is assigned missions whose primary objectives are not tax-related (exhibit 17, p. 110).

David R. MacDonald, who was Assistant Secretary of the Treasury at the time, did not share Alexander's views. Pointing out that the neglect of programs like NTP and organized crime strike forces appeared to him to be violations of Title 26, U.S. Code, Section 7601 which directs the IRS to pursue all persons who are not paying their taxes, MacDonald said these decisions were reflections of the Watergate era when intelligence gathering projects were suspect, no matter how responsibly they were managed and carried out. "That was a time when any effort to single out any group or individual, even a convicted felon, was immediately identified as the formulation of an enemies list," MacDonald testified. "It was much easier in 1974 simply to respond to Congressional and press criticism by refusing to investigate anyone whose probable liability for taxes was not spewed out of a computer or placed in the IRS' hand on a silver platter by an unsolicited informant" (pp. 258, 265).

JEOPARDY

Elmer B. Staats, the Comptroller General, testified on changes that had occurred in the Narcotics Traffickers Program prior to its dismantling. Before fiscal year 1972, he said, IRS made relatively few jeopardy and termination assessments. However, in response to President Nixon's announcement to expand efforts in combatting drug abuse in July 1971, and with the creation of the ensuing Narcotics Traffickers Program, many jeopardy and termination assessments were made against drug financiers and traffickers (p. 310).

In March 1974, Commissioner Alexander announced that IRS would revise 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 of 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 criminal history of the taxpayer, Staats said, adding that these new instructions were to assure that only cases with substantial and documentable tax violations were included in the program (p. 310). What Staats did not point out was that this revised policy on jeopardy and termination assessments had the effect of diluting the anti-drug campaign of IRS and that this diminution of the narcotics program paralleled the worst days of Watergate for President Nixon. A President preoccupied with

his own political survival did not object when a principal weapon in the Narcotics Traffickers Program was blunted.

PREMISES

Staats went on to say that Congress amended the law in 1976 to afford taxpayers subjected to jeopardy and termination assessments quicker judicial remedy than had been available previously. 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. Staats said the change in law, the IRS revised policy and the Court's decision combined to bring about a sharp decline in the use of jeopardy and termination assessments. Total jeopardy assessments numbered 298 in fiscal year 1972. There were 526 of them in fiscal 1974 but only 69 in fiscal 1979. Staats said IRS made 5,311 total termination assessments from 1972 to 1974 but only 756 during the next five years (pp. 310, 311).

Staats concluded by saying there was "definite evidence" that IRS had abused its jeopardy assessment powers in the early and mid-1970's. He said statistics indicate that IRS has all but abandoned the jeopardy and termination assessment route as a tool in civil enforcement of the tax laws. Staats said, "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" (p. 311).

In 1976 President Ford directed IRS to again establish a tax program aimed at high-level drug traffickers. This program was to replace the Narcotics Traffickers Program. DEA and IRS signed a memorandum of understanding. Then, IRS embarked on its new High-Level Drug Dealers Tax Enforcement Project. Staats testified that the Tax Reform Act slowed implementation of the IRS-DEA agreement. The pact was signed in July of 1976 but when the disclosure provisions of the Tax Reform Act went into effect the following January doubts were raised about the legality of the agreement, particularly as it affected the transfer of information from IRS to DEA, Staats said. He said it took nearly a year for DEA and IRS to work out a procedure for exchanging information that seemed to be legal under the terms of the Tax Reform Act (p. 309).

RESULTS

The House Select Committee on Narcotics Abuse and Control reported that the High Level Drug Dealers Tax Enforcement Project actually provides no greater emphasis on narcotics traffickers than any other taxpayer group (exhibit 8, p. 110). Staats agreed. He testified that the IRS-DEA agreement "has produced few tangible results."

Former Assistant Treasury Secretary David R. MacDonald was of a similar mind, saying, "The agreement with DEA was an uncontrollable, unmonitorable arrangement which appeared to be nothing more than an agreement for DEA to refer cases where the violator appeared not to have paid his taxes" (p. 269). MacDonald said that the "agreement" placed narcotics traffickers in the tax fraud program. He said the agreement did not devote specific personnel or resources

to a separate program. He said that in 1974 IRS had more than 900 people working on NTP. The new agreement did not allocate any specific personnel or resources, MacDonald said, adding that the agreement, in fact, stressed the point that IRS was only a support agency, working to a "limited extent" with DEA. Conversely, President Ford had intended a re-emphasis of NTP. MacDonald said that the President "intended that IRS should have its own major responsibilities in the Administration's anti-narcotic program." The IRS' participation was viewed as making a positive effort to identify suspected major narcotics traffickers who appear to have violated the Federal tax laws. With the destruction of the NTP and the only replacement being the IRS-DEA agreement, IRS no longer had a program capable of initiating efforts against narcotics traffickers (p. 264).

IRS Estimates of Unreported Income

The Internal Revenue Service decides how much investigative resources to devote to criminal cases on the basis of its assessment of the amount of income taxes that are deliberately evaded. The IRS said in a September 1979 report, "Estimates of Income Unreported on Individual Income Tax Returns," that $6 billion to $9 billion in taxes was not paid on $25 billion to $35 billion of unreported individual income from illicit narcotics, gambling and prostitution in 1978. For the same year, IRS said, $13 billion to $17 billion in taxes were not paid on legitimately earned but unreported income totalling $75 billion to $100 billion (p. 368).

The IRS did not have very much confidence in its estimates. The report acknowledged that some of the estimates were less reliable than others and that the figures on illegal income were especially approximate. The Commissioner of Internal Revenue, Jerome Kurtz, qualified even further, telling the House Subcommittee on Commerce, Consumer and Monetary Affairs that "all of the figures in this report should be taken as the group's best estimates based on available information—not as facts" (p. 368).

The same House Subcommittee, which is chaired by Congressman Benjamin Rosenthal of New York and which is part of the House Government Operations Committee, held hearings on September 5 and 6, 1979, on "Subterranean or Underground Economy." The Rosenthal Subcommittee reported that the IRS estimates were even more approximate than Kurtz had cautioned. The House panel concluded that IRS understated by at least 50 percent the total annual income from drug trafficking. The House Subcommittee said IRS estimates of illegal source income were "dramatically understated" in both organized crime and white collar crime.

OMISSIONS

The House Subcommittee said IRS estimates omit entire categories of potentially unreported income. Instead of giving a total legal and illegal unreported income estimate of $100 billion to $135 billion, IRS could have more accurately issued an approximation of $250 billion, the House Subcommittee said (exhibits, 12, 13 p. 110).

Similarly, a report, "Offshore Banking—Issues with Respect to Criminal Use," prepared by former and present Stanford University Law School professors for submission to the Ford Foundation (exhibit 33, p. 473), said the IRS estimates were not agreed to by everyone at IRS. The estimates were heatedly debated within IRS and then reduced by half before they were made public, the report said.

Elmer B. Staats, the Comptroller General of the United States and head of the General Accounting Office, told Senators that the IRS estimates of income earned from illegal sources are probably understated (p. 307).

The staff of the Senate Permanent Subcommittee on Investigations made its own evaluation of the IRS estimates. Jack Key, the Subcommittee's Chief Intelligence Officer, testified that the illegal source unreported income estimates by IRS are "grossly understated." Key, whose 17 years in law enforcement include 10 years with the organized crime strike force in Miami and seven years with Florida State and local authorities, said the staff arrived at its illegal source income estimates using data from the Joint Economic Committee of Congress, the Congressional Research Service of the Library of Congress, the U.S. Chamber of Commerce, the Advisory Committee on Intergovernmental Relations, the General Accounting Office and other sources. Key said the Subcommittee staff estimate for illegal source income was $121.2 billion to $168.2 billion. Key said the staff's estimates were on the low side (p. 369).

RETAIL

Key said IRS estimates seemed to have ignored or cut in half projections made by the National Narcotics Intelligence Consumer Committee. The NNICC, composed of Government agencies involved in drug investigations, estimated gross retail sales of more than $40 billion in illegal drugs alone. The Internal Revenue Service had to know about the NNICC estimate since it is a member of the organization (pp. 372–373).

Testifying before the Senate Permanent Subcommittee on Investigations, Internal Revenue Commissioner Jerome Kurtz said unreported income from illegal drugs was about $20 billion—about one-half of the estimate of NNICC. Kurtz explained, "Others have estimated gross retail sales of over $40 billion of illegal drugs. Without getting into details of methodology or data, the point is that the drug trade is enormously profitable and that only a minuscule amount of income of dealers and financiers is reported for Federal income tax purposes" (p. 375).

The Subcommittee examined closely this $20 billion difference in drug trade estimates that Kurtz attributed to "methodology or data." While everyone would agree with Kurtz that the drug trade is enormously profitable and that only a minuscle amount of drug income is ever reported, it is important for the Government to have as accurate a picture as possible of the size of this illicit business. Arriving at a reliable estimate of the volume of untaxed dollars is important because such a figure is used by IRS in allocating investigative resources for the purpose of taxing that illicit income. With a low estimate, IRS expends less effort to trace tax evaders than might be

applied if the estimate were higher. In addition, the size of the illicit drug business, measured in dollars, gives Congress an idea of the dimensions of the narcotics trade and an indication of how effectively the executive branch is dealing with the problem.

Subcommittee staff investigator Key said IRS estimates are out of touch with what other responsible authorities consider to be the volume of unreported income derived from illegal activities. He said that IRS figures are so unreal that if its report were to be filed at the Library of Congress it might more appropriately be indexed as fiction (p. 374).

Senator Nunn asked Kurtz how IRS decides to allocate investigative resources. Kurtz said this decision is made through "a combination of intuition, judgment, experience, demands, requests from the field". Senator Nunn asked Kurtz if the findings of the Rosenthal Subcommittee in the House of Representatives would have any influence on IRS' decisions regarding the allocation of resources. Kurtz said the Rosenthal Subcommittee findings would have no impact on the decision-making process at IRS (pp. 392–393).

DATA

Kurtz went on to say the IRS estimates of untaxed legal and illegal income are the best the Service could do under the circumstances. He said the estimates were as accurate as they could be and when IRS officials felt they could not be accurate, owing to unreliable data or a lack of data, no estimates were made. Kurtz said IRS made very clear that some of the estimates were incomplete. He said that nothing in the estimates was put there for political reasons. He said IRS had never before tried to approximate the total amount of unreported income and that the next time IRS undertook a task like this it hoped to issue a more comprehensive, complete report (p. 393).

As for the difference of $20 billion between IRS' estimate of unreported income from drug sales and the estimate by the National Narcotics Intelligence Consumer Committee, Kurtz said there is no real discrepancy. The $20 billion difference vanishes, he said, when deductions and other appropriate adjustments are made to reflect the distinction between money that is earned from drug sales and that which is taxable. Kurtz was saying that, as in all businesses, the drug trade, if it were being taxed as any other enterprise, would be able to deduct the costs of doing business and realize other deductions. Only then would a taxable figure be arrived at. And that figure is $20 billion less than the figure calculated by the NNICC. Kurtz said, in effect, that IRS is right in its estimate—and so is NNICC (p. 394).

Kurtz added that IRS had begun with a gross figure similar to the NNICC estimate. But, he explained, "gross income is not taxable under the law. . . ." Then, he said, "we backed down to take out deductions, to take out payments made abroad, to take out some estimates of the income that was already reported, to take out estimates of the income attributable to people who are not taxpayers. Some of this income goes to people who are students, very low income, et cetera, who, if they reported the income, would not owe any taxes."

Kurtz said the NNICC estimate and the IRS estimate "are completely reconcilable taking into account the definitional differences of gross sales and taxable income" (p. 394).

STUDY

Kurtz was asked about the private study, prepared for the Ford Foundation, which asserted that IRS went through an intense internal debate over the untaxed income estimates and then cut them in half before making them public. Replying that he knew nothing of this alleged internal debate, he said he would have subordinates look into this allegation and report back to the Subcommittee (p. 396).

A memorandum, dated December 31, 1979, was forwarded to the Subcommittee. The memorandum was based on information from the three IRS staff members who led the study of unreported income, Howie Wilson, Berdj Kenadjian, and Jim Swarztwelder, and was signed by Russell Dyke, the Assistant Commissioner of IRS for Planning and Research. Dyke said there was no pressure on the study group to minimize or reduce the estimates (pp. 396–397).

1976 Criticisms of Donald Alexander

Internal Revenue Commissioner Donald Alexander was criticized for taking IRS special agents out of investigations of drug traffickers. He also came under fire for disengaging his personnel from political corruption and white collar crime cases.

On January 6, 1976, a full year before the Tax Reform Act was implemented, Jonathan L. Goldstein, United States Attorney for New Jersey, said IRS investigators had proven themselves to be of indispensable value in a succession of corruption prosecutions involving 13 political figures in New Jersey over a period of six years. Addressing a tax conference at Seton Hall University in South Orange, New Jersey, Goldstein said that in light of so many successful prosecutions—none of which would have been possible without IRS assistance—he found it ironic and incredible that Alexander had decided to remove IRS from similar investigations in the future (exhibit 24, pp. 354–356).

While Goldstein was complaining about the IRS disengagement from white collar crime and political bribery cases, his remarks sounded similar to those comments heard from officials concerned about the IRS absence from major narcotics prosecutions. Goldstein said the only successful methods of investigating political bribery cases is precise, detailed and skillful analysis of financial records. He said these records, which can be obtained only by grand jury subpoena, must be analyzed—and no one can do that better than IRS. Therefore, to take these skilled analysts out of political bribery cases is thoughtless and unsatisfactory and the only alternative is for the Government to enlist the assistance of certified public accountant firms which would try to fill in for the missing IRS, Goldstein said.

SHIFT

Goldstein said that Alexander "by administrative fiat" jeopardized the Government's ability to conduct public corruption investigations.

He said that by withdrawing IRS from investigations of sophisticated political corruption cases, Alexander had removed the most effective weapon the Government can wield, IRS accounting agents.

Alexander tried to justify his shift of policy on the premise that crimes such as extortion and bribery do not result in violations of the tax laws, Goldstein said. Goldstein added that the premise is a false one, that in each instance of extortion or bribery there is an accompanying Federal income tax crime. He said that when an illegal cash payment is made the crimes of bribery, extortion and tax violations occur simultaneously. This fact alone demonstrates that there is no justifiable reason for IRS agents to be withdrawn from corruption investigations, he said.

It is important that the public perceive that all segments of society fairly and lawfully share in the payment of Federal income taxes, Goldstein said. The withdrawal of IRS from official bribery and white collar crime cases will be observed by the public and will result in an erosion of the people's confidence in their government, Goldstein said.

Decline of Special Enforcement Program

The Internal Revenue Service conducts investigations of two kinds of tax crime. Those violations committed by taxpayers who work in legitimate pursuits are investigated under the general enforcement program. IRS devotes about 75 percent of its investigative resources to this kind of investigation. The remaining 25 percent goes into the special enforcement program whose function is to pursue organized criminals, drug traffickers and financiers and other persons who earn large incomes illegally and who invariably do not pay taxes on these proceeds and who frequently do not even file tax returns.

Five percent of the total investigative effort goes to investigations of person in the drug trade. The remaining 20 percent is used for inquiry into organized criminals and other violators whose illicit gains are not primarily from the sale of narcotics. For the purposes of this report, then, IRS expenditures, by percentages, for investigations into tax violations are:

—75 percent for investigation of taxpayers who earn their income in lawful work. This is under the category of general enforcement program.

—5 percent for investigation of persons in the drug trade. This is under the category of special enforcement program.

—20 percent for investigation of criminals not primarily in drugs. This also is part of the special enforcement program.

IRS' allocation of personnel and other resources to the special enforcement program was criticized by Deputy Assistant Attorney General Irvin B. Nathan. He said that prior to the Tax Reform Act of 1976 IRS had a much stronger investment in drug and organized crime cases than it does today. He said IRS worked with the Justice Department in more than 600 organized crime prosecutions providing the Department with especially valuable assistance in the area of financial investigation. But once the statute was enacted the figure of 600 cases dropped to 300. Nathan blamed the Tax Reform Act and a diminished commitment by IRS to the special enforcement program

for the decrease. He said it was not the result of a manpower shortage (p. 53).

BLINDERS

It is not simply a lack of commitment that is to blame for IRS' reduced role in drug and organized crime investigations. And it is not all the fault of the Tax Reform Act. The problem is that IRS policymakers do not want to cooperate. They have put on "blinders," are oblivious to what is going on in society and are unpersuaded of the value of using the revenue laws and IRS investigative skills to immobilize drug syndicates and imprison their leaders. That is the view of Peter B. Bensinger, the Administrator of the Drug Enforcement Administration.

Bensigner told the Subcommittee that IRS' lack of enthusiasm for its own special enforcement program can be likened to a situation in which the nation's police forces spend most of their time on petty theft cases and neglect to investigate armed robberies and murders. Bensinger said IRS policy leaves much to be desired when it ignores the billions and billions of untaxed dollars in the drug trade. He said the loss to society—the "thousands of injuries and overdose deaths"—is enormous and IRS is to be criticized for not doing its part to address the drug menace (p. 83).

Bensinger said IRS policy regarding its special enforcement program is misguided and demonstrates a false sense of priorities. He said IRS apparently prefers to investigate ordinary taxpayers earning between $15,000 and $25,000 rather than persons who are making millions of dollars in illegal activities (p. 83).

Richard Fogel, Senior Associate Director of GAO in the Government Division, said that while the illicit narcotics trade in the U.S. has increased, the Internal Revenue Service has reduced its allocation of resources to investigate drug traffickers under its special enforcement program (pp. 351, 352).

Subcommittee Questions IRS Statistics

Testifying before the Subcommittee, IRS witnesses insisted they were devoting sufficient resources to high level narcotics investigations. For example, on six occasions, IRS witnesses told Senators that the IRS had obtained convictions against 22 high level drug dealers in fiscal year 1979. The Subcommittee sought to identify those 22 high level narcotics convictions claimed by IRS. Irvin B. Nathan, speaking for the Justice Department, could not identify the cases. Puzzled by his and his Department's lack of knowledge of the 22 cases, Nathan pointed out that no prosecutions can occur without Justice supplying the prosecutor. IRS witnesses, including Commissioner Jerome Kurtz, testified that they did not have the information on the 22 cases in the hearing room but that they would provide this data to the Subcommittee later. Kurtz and his colleagues gave the Subcommittee this assurance on December 14, 1979.

IRS did not immediately supply the requested information. Senator Nunn wrote to Internal Revenue Commissioner Kurtz on January 24, 1980 and again requested the information. No response was forthcoming. The Subcommittee told IRS that printing deadlines

required that the hearing record be formally closed by Friday, March 7, 1980. On that date, the Subcommittee received a letter from Kurtz. He said IRS had changed its position now and would not provide the Subcommittee with information regarding the 22 high level narcotics convictions. The reason, Kurtz said, was that these drug cases "may not be a matter of public record and therefore not properly disclosable." (Exhibit 37, p. 496.)

22 CASES

In addition, in that same letter, dated March 6, 1980, Kurtz clarified his own testimony before the Subcommittee. During his appearance before the Subcommittee the previous December, Kurtz testified that demonstrative of IRS's positive approach to narcotics investigations was the fact that in fiscal 1979 the Service had "achieved 22 convictions of high level drug financiers and traffickers." (p. 376) Kurtz said in his letter that the convictions he had testified about might not have been of high level drug dealers after all. ". . . I am advised," Kurtz wrote, "that in several instances the classification of the cases as a high level narcotics trafficker was questionable." (Exhibit 37, p. 496.)

Because trials and the convictions that flow from them are public record, the Subcommittee continued to try to obtain information from IRS that would identify the 22 cases. Responding to the Subcommittee's interest, Thomas J. Clancy, Director of the IRS Criminal Investigation Division, wrote to Senator Nunn on March 28, 1980 to further discuss the 22 cases. Clancy said the Tax Reform Act disclosure provisions prohibited IRS from identifying any person convicted of a tax crime as being a drug dealer. However, Clancy attached to his letter an 80-foot long computer printout that contained the name of every person convicted in fiscal year 1979, of a Federal tax crime. To make use of the printout, the Subcommittee would have had to go through all IRS convictions in fiscal '79, determine which of those were narcotics-related and then which were the 22 high level narcotics cases. There were about 1,622 persons convicted of tax crimes in that 12-month period. The Subcommittee staff estimated that to make the analysis Clancy proposed would require several investigators working fulltime more than a year. Senator Nunn, the chairman, chose not to undertake this task.

Accordingly, on March 31, 1980, Senator Nunn instructed Marty Steinberg, Subcommittee Chief Counsel, to write Clancy to say that nothing in the Tax Reform Act of 1976 prohibited IRS from giving the Subcommittee specific information as to who were the 22 high level narcotics traffickers convicted as a result of IRS investigations in fiscal year 1979. In his letter to Clancy, Steinberg pointed out that these cases were a matter of public record. The computer printout, Steinberg said, would not satisfy the Subcommittee's request.

The explanation for IRS's reluctance to cooperate in supporting the sworn testimony may be found elsewhere in Clancy's letter of March 28 to Senator Nunn. Clancy admitted the figures IRS initially submitted—that is, that 22 high level narcotics convictions had been obtained in fiscal year 1979—were not accurate. He said that some

of the 22 convictions did not even involve narcotics and others in the list of 22 were "weak speaking solely in terms of the narcotics connection." [1]

The Missing Organized Crime Prosecutions

The Subcommittee also questioned IRS statistics in connection with the Service's participation in organized crime strike forces. The strike forces were established in the nation's urban centers in the early 1960's. Comprised of drug, revenue and FBI agents, representatives of other agencies, Justice Department investigators and prosecutors, the strike forces combined the law enforcement resources of the Federal Government for what frequently resulted in successful prosecutions of organized criminals, drug traffickers, interstate gambling leaders and other persons involved in serious violations. Because of its proven expertise in financial investigations, the IRS was an integral part of most strike force operations.

IRS reduced its participation in strike forces by about 50 percent, since passage of the Tax Reform Act, according to a March 12, 1979 report by the General Accounting Office. IRS tried to dispute the GAO figures, pointing to a chart, prepared by IRS, which purported to show that IRS's work in organized crime had not declined at all. What had actually happened, IRS said, was that fewer tax-related cases were being made through strike forces—and that IRS was continuing to pursue organized criminals outside the strike forces.

The Department of Justice disputed IRS on this point. Deputy Assistant Attorney General Irvin B. Nathan said the GAO figures were correct, that IRS had substantially reduced its role in organized crime strike forces.

STATISTICS

The Subcommittee sought to identify those organized crime cases which IRS claimed to have been involved in but which do not show up in strike force statistics.

The Subcommittee asked for an explanation from IRS Commissioner Jerome Kurtz. He said that beginning in fiscal year 1977 IRS initiated "a greater number" of its organized crime cases outside the strike forces (p. 377). But, as Nathan had pointed out, even cases outside the strike forces had to be prosecuted by Justice Department prosecutors and the Department could not locate the prosecutions Kurtz had reference to (p. 35). Kurtz could not further enlighten the Subcommittee on this question.

ACTIVE

Senator Percy referred again to the March 1979 GAO report which cited IRS' decline in strike force work. In that report IRS claimed it was still active in organized crime cases at the same level but that these investigations were outside the strike forces. Senator Percy noted that Justice Department spokesmen cannot locate or otherwise identify these organized crime cases and asked Clancy to explain this discrepancy. Clancy said he could not explain it (pp. 437–438).

[1] See Appendix pp. 138–140 for Clancy's letter of March 28, 1980 and Steinberg's letter of March 31, 1980.

Marty Steinberg, the Subcommittee's Chief Counsel, asked Clancy if he would supply for the hearing record those organized crime cases which IRS worked but which the Justice Department could not locate. Clancy said he would supply that information for the hearing record. That was on December 14, 1979. A month went by and Clancy did not supply the information. Still trying to locate the cases, Senator Nunn again requested the information in his letter to Commissioner Kurtz on January 24, 1980. This was the same letter in which the identities of the convicted drug traffickers were sought. The next response was the March 6, letter from Kurtz. It was in that letter that IRS changed its position, saying it would not now provide the Subcommittee with the names of the organized crime figures or the 22 high level drug traffickers. The reason, Kurtz said, was that these cases involving high level drug traffickers and organized crime figures "may not be a matter of public record and therefore not properly discloseable." (Exhibit 37; p. 496.)

In his March 31, 1980, letter to Clancy, Subcommittee Chief Counsel Steinberg, acting under the direction of Senator Nunn, challenged the IRS refusal to turn over the requested information. Steinberg said the Subcommittee did not want confidential or otherwise sensitive information. All it needed was the names of the organized crime figures and high level narcotics dealers who had been convicted of tax charges in fiscal year 1979. This was public record data, not covered in any way by the disclosure provisions of the Tax Reform Act, Steinberg said.

OVERSIGHT

As part of its oversight responsibility, the Subcommittee must have pertinent information on how IRS allocates its resources, particularly regarding organized crime and major narcotics investigations, Steinberg said. The Subcommittee has no other way of making a comprehensive evaluation of the effectiveness of IRS in its Special Enforcement Program, SEP, Steinberg said.

Steinberg asked Clancy to have IRS lawyers give the Subcommittee a written opinion on why the disclosure provisions of the Tax Reform Act prevent IRS from giving the Subcommittee this public record information. "I do not believe that a logical and rational interpretation of [the disclosure provisions] leads to the conclusion that the names of persons convicted in public forums, in particular IRS programs, should be withheld from the Subcommittee," Steinberg wrote.

IRS Intelligence Gathering Program Was Reduced

Members of the Subcommittee asked Irvin B. Nathan of the Justice Department to comment on IRS intelligence gathering. Nathan confessed that he knew very little of what the IRS did in gathering intelligence. He said the screen erected around IRS by the Tax Reform Act enabled the Service to function alone, telling outsiders like himself very little of what went on inside (p. 34). But two longtime IRS senior officials—John Olszewski and Leroy G. Venable—could talk from first hand experience about the IRS intelligence gathering program. What they said indicated IRS intelligence has suffered a fate similar to what happened to most other aspects of the special enforce-

ment program. That is to say, the intelligence function has been cut back (p. 282).

Olszewski, former Director of the Criminal Investigation Division of IRS, and Venable, former Chief of the Operations Branch of the CID, said that in the late 1960's and early 1970's IRS had a substantial information gathering intelligence system. The system, they said, was directed towards tax violations but also included background information on people under investigation. The intelligence effort was succeeding, developing information that led to major tax cases, they said (p. 281).

MISTAKES

But from 1974 on, Olszewski and Venable said, IRS policymakers clamped down on intelligence activities. Isolated instances in which mistakes were made were blown out of proportion by IRS executives. Rather than solve an individual problem in the intelligence field, they chose instead to deemphasize the entire intelligence effort. Using "cost-effectiveness" as their justification, IRS policymakers reduced the investment in intelligence and, as a result, the whole special enforcement program suffered, Olszewski and Venable said (p. 282).

Similarly, former Assistant Treasury Secretary David R. MacDonald witnessed the same decline in intelligence at IRS. He said intelligence gathering was even abandoned entirely for a time and then started up again but with such restrictions that the program was rendered useless (p. 265).

MacDonald said that because of its lack of information gathering capability IRS is, in effect, prohibiting its agents from actively looking for tax violations. Without an adequate centralized information gathering system, investigations will be opened only if referred by other agencies, he said. Moreover, if no return is filed—which is frequently the case with major mobsters—and if there is no complaint from others, then there is little likelihood that anyone engaged in an illegal occupation will ever be bothered by IRS, MacDonald said (p. 265).

Watergate scandals were causing several agencies to be sensitive on the subject of intelligence in 1974. IRS was no exception, MacDonald said. But, he added, concern over Watergate did not justify IRS' decision to take the path of least resistance and gather no intelligence at all. (p. 265).

John Gunner, who worked on GAO's examination of IRS' criminal investigative programs, testified that the Service moved away from its centralized system of filing intelligence. IRS selected the less efficient decentralized system, Gunner said, because of criticism leveled by critics such as the Senate Select Committee to Study Governmental Operations with respect to Intelligence Activities, chaired by Senator Frank Church of Idaho (p. 265).

Quality of Cases Reportedly Has Declined

Once IRS completes its investigation of an alleged criminal tax violation, the Service makes a judgment as to whether or not the case can be prosecuted. If the judgment is yes, prosecution is called for,

then the case is referred to the Tax Division of the Justice Department. The Department is responsible for prosecuting Federal crimes. Deputy Assistant Attorney General Irvin B. Nathan said the Justice Department declines to prosecute an increasing number of IRS cases. Now declining at the rate of 18 to 19 percent of the IRS referrals, the Department of Justice feels that IRS is not sending over very substantial cases in all too many instances, Nathan said. "The cases that we have declined are simply not quality cases," Nathan said. "They do not involve significant taxpayers. The Tax Division does not believe it will have a significant impact on the tax collection system if those individuals are prosecuted" (p. 36).

Nathan said that frequently the IRS refers tax cases of the "ma and pa" variety; that is, cases which involve people who do not make much money and who are accused of trying to cheat the Government out of even smaller amounts. The "ma and pa" cases will show up more often at IRS, he said, because the overwhelming majority of its investigative effort is directed at that lower level of violator. Conversely, five percent of IRS' investigative capability is used against drug traffickers, Nathan said (p. 36).

The Decision To Refer a Case To Justice

Prior to the enactment of the Tax Reform Act of 1976, the Department of Justice and the IRS shared the responsibility of deciding whether or not an organized crime or major narcotics case had merit. But now, according to Deputy Assistant Attorney General Nathan, IRS has delegated unto itself the sole responsibility for deciding whether a criminal case should be reviewed by Justice.

In pre-Tax Reform Act years, Nathan said, IRS would do an organized crime or drug inquiry and then decide if the case was or was not strong enough to be prosecuted. If the decision was the case was strong, it would be referred to the Tax Division. If the case was found to be lacking, it was still sent to Justice, not to the Tax Division, but to the Criminal Division. The idea was that prosecutors in the Criminal Division might be able to add information they had to the case, making it more likely to be successfully prosecuted. Or. Nathan said, it was hoped that at the minimum the Criminal Division might find something of value in the case that could be used in a non-tax investigation. The inquiry could be of use to prosecutors working outside the tax realm. But in 1977, when the Tax Reform Act went into effect, IRS refused to let Justice see those cases which IRS had decided should not be prosecuted, Nathan said.

Later a compromise of sorts was worked out. Nathan said IRS agreed to refer the files to the Justice Department—but only when there were only five months remaining before the statute of limitations would expire. This was not satisfactory, Nathan said, because it gave the Department so little time to put together its own case if one were called for. By the fall of 1979, the IRS had decided even the compromise procedure would not do and it decided not to turn over to Justice files on any cases it had decided should not be prosecuted—and it did not matter who the subjects of the case were, major drug traffickers or not. "So at present, we have no knowledge of the cases

in which IRS has decided not to proceed with prosecution," Nathan said. At another point in his testimony, Nathan summarized the frustration Federal prosecutors feel when trying to find out what IRS is up to in law enforcement activities. "We simply can't get through the screen of the Tax Reform Act to know what the Internal Revenue Service internally is doing," Nathan said (p. 42).

A "Balanced" Tax Collection System

An "impartial" tax collection system was advocated by former Commissioner Donald Alexander and other senior executives at IRS. But others believe that an "impartial" system is one in which ordinary taxpayers are the principal targets because they file returns and submit readily to scrutiny. Mobsters, on the other hand, hire attorneys to help them resist IRS audit and in many instances don't even file returns to begin with.

The "impartial" system, in fact, gives "a distinct advantage" to the criminal, according to former Assistant Treasury Secretary David R. MacDonald. He said that major crime figures know that when IRS intelligence gathering projects are abandoned they will benefit because no special efforts will be made by the Government to look into their tax status.

Instead of the so-called impartial tax collection system, IRS' goal should be a balanced system, MacDonald said. The collecting of taxes from those earning illegal income is just as much a part of tax administration as is the collecting of taxes from those earning legal income, MacDonald said. It is more difficult to get mobsters to pay their taxes, he said, but that is no reason to give up the cause.

A similar view was expressed by John Olszewski and Leroy Venable, both veterans of many years in criminal tax investigations. They said that by concentrating its enforcement efforts on general taxpayers, IRS ignores "the big money men" engaged in highly profitable illegal activities. They said what is called for is a "balanced enforcement program," (p. 284), one that encourages compliance by both law-abiding citizens and criminals.

A Proposal To Reorganize IRS

There is no one in the senior executive level of IRS who has sole responsibility to represent criminal investigations and intelligence gathering. Investigative matters are handled by the Assistant Commissioner for Compliance. Several witnesses have advocated that a separate position of Assistant Commissioner for Investigations be created. This would give the criminal investigations function a greater voice in IRS policy, advocates say.

Jerome Kurtz, the IRS Commissioner, told the Subcommittee he had never heard the suggestion that such an assistant commissioner be created. He said he opposed the idea. Kurtz said the interests of the criminal investigators are well represented by the Assistant Commissioner for Compliance, Singleton Wolfe, who carried out his responsibilities "with vigor" (p. 413).

Elmer B. Staats, Comptroller General of the United States, said it may be that no such Assistant Commissioner position exists be-

cause this aspect of IRS duties "is of a low priority." Another GAO spokesman, Daniel Harris, who worked on the examination of the IRS criminal investigations capability, said a previous inquiry he had done at the FBI led him to conclude that better headquarters management was called for. The same need exists at IRS, he said. At the FBI, he said, once the GAO report came out, the Bureau imposed improved leadership at the national office, thereby solving the problem administratively. Harris said it is necessary that similar action be taken at IRS so that the criminal investigations division is able to report directly to the Commissioner. Harris called for a direct line of command from the CID to the Commissioner, with no one in between (pp. 344–345).

The same point was made by John Olszewski and Leroy Venable. They said criminal enforcement had little representation at the senior executive level at IRS. They said criminal enforcement procedures and policies are set by people with little or no background in criminal investigations (p. 282).

A similar problem afflicts IRS nationwide. While Kurtz opposed the idea that more criminal investigative voices were needed at the Assistant Commissioner level, IRS Deputy Chief Counsel Lester Stein did acknowledge that of the 58 regional directors throughout the country only three or four have criminal investigations backgrounds.

E. J. Vitkus, former Assistant Regional Commissioner in the Atlanta office, said no amount of reorganization within IRS would achieve the desired goal of the CID having its voice heard at national headquarters. The only solution, he said, is to take the criminal investigations division out of IRS altogether and reconstruct it in the Treasury Department. There it would report directly to the Treasury Secretary, he said.

The Statement of Senator Lowell Weicker

Senator Lowell P. Weicker, Jr., of Connecticut, who was a member of the Senate Watergate Committee, said in a statement submitted for the hearing record, the disclosure provisions of the tax law are needed, are workable, do not stand in the way of good law enforcement and if problems have resulted from them for prosecutors and investigators it is because the Internal Revenue Service has used them as an excuse to be deliberately uncooperative.

It is not surprising to find witnesses like Deputy Assistant Attorney General Irvin B. Nathan, DEA Administrator Peter Bensinger and Assistant U.S. Attorney Robert Perry to have spoken out against the disclosure provisions, Senator Weicker said. "Charged with the responsibility of enforcing criminal laws, it is understandable that these men are most concerned with the efficiencies of enforcement," Senator Weicker said. "However, we, as legislators, must strike the necessary balance between privacy rights of the citizens and the rights of government to enforce laws." (p. 357).

Until the Tax Reform Act was implemented in 1977, tax returns were made available to such diverse agencies as the Department of Defense, the Federal Trade Commission, the Interior Department, the

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Tennessee Valley Authority and the Veterans Administration, Senator Weicker said. He said that Justice Department officials had access to tax return information if it was deemed to be necessary for their work. "The wide latitude created by pre-1977 procedures gave Federal officials the freedom both to rummage through income tax returns for statistical data obtainable from other sources and to abuse audit procedures in order to harm enemies and help friends," Senator Weicker said (p. 357).

LIST

Past abuses of tax return disclosure included the "well publicized Nixon White House hit list" (p. 357) and the use of tax return information on occupational groups for political purposes, Senator Weicker said.

American citizens voluntarily file tax returns—"This baring of the soul" (p. 357)—for revenue purposes only, Senator Weicker said, stressing that taxpayers do not accommodate their government in this task for scientific, sociological, political, statistical or non-tax law enforcement purposes. Taxpayers who lose faith in their government's ability to keep their returns secret will be less willing to report honestly, Senator Weicker said, warning, "If taxpayers become convinced that confidential data they submit each year is being used for political purposes, how long will it be before cheating is commonplace? Widespread cheating would be beyond the capacity of our 13,000 revenue agents to control and our entire system of voluntary self-assessment would collapse."

Senator Weicker said the disclosure provisions of the Tax Reform Act, particularly the requirement that a court order must be obtained for the inspection of a return, are needed if a proper balance is to be maintained between the privacy rights of citizens and the duties of law enforcement agencies. He said that the fact that major narcotics cases had been made recently—the Araujo trial in California, for example—shows that successful prosecutions are possible under the disclosure provisions of the act. ". . . in testimony before this very Subcommittee within the past week, it has been demonstrated that cooperative efforts between IRS and other agencies are not proscribed by the act, and indeed if such barriers do exist they are artificially imposed by the attitude taken by IRS to joining in such cooperative efforts," Senator Weicker said (p. 358).

TOOLS

Senator Weicker also suggested that if the Justice Department had more expertise in financial investigative work it could more effectively attack "major corporate white collar or organized criminal activity by using the legal tools already available to it" (p. 359). Senator Weicker interpreted the decline in prosecutors' requests for tax information as reflective of the fact that they are unwilling to do the preparation necessary to make such requests "or it is an indication that prior to the passage of the Tax Reform Act the multitude of the requests for such information without judicial scrutiny, were simply unwarranted" (p. 359).

In the Nicky Barnes trial—another major courtroom victory won under the new disclosure provisions—the Justice Department felt the case would have been lost had there been further delays in receiving returns requested from IRS six months earlier, Senator Weicker said. But whose fault was the delay? he asked. "The reason for the delay is obvious," he went on. "It was because of the artificial, bureaucratic procedures that IRS has established since passage of the Tax Reform Act which have hampered the flow of critical information, even when the provisions of the Tax Reform Act have been complied with. This seems to be IRS' calculated way of saying, in effect, that it wants to remove itself from participation with other agencies in criminal investigations" (p. 349). Senator Weicker said all the Justice Department's criticism of the disclosure provisions of the Tax Reform Act are misdirected. The law is not the problem, Senator Weicker said, explaining that the real problem is the way IRS has interpreted the law. He said Congress should make it clear to IRS that the Service will be expected to stop using the Tax Reform Act as an excuse to avoid working with other agencies in law enforcement. IRS should be made to start cooperating, Senator Weicker said.

The IRS View From Washington, D.C.

Three IRS officials from the field—John Rankin of Dallas, Richard Wassenaar of San Francisco and Willard Cummings of Austin, Texas—testified before the Subcommittee about the problems they encountered with the disclosure and summons provisions of the Tax Reform Act. Following their testimony, Senators sought the views of IRS officials at the national office in Washington. Testifying were Jerome Kurtz, Commissioner of Internal Revenue; Singleton Wolfe, the Assistant Commissioner for Compliance; Lester Stein, the Deputy Chief Counsel; and Tom Clancy, the Chief of the Criminal Investigation Division. The Subcommittee wanted to know from these men how they felt about the Tax Reform Act. It was clear that they were far less troubled by the disclosure provisions of the statute than were their agents in the field. Senators also wanted to know if IRS policymakers were allocating sufficient resources to drug investigations. The witnesses said IRS spent sufficient resources for narcotics investigations.

Kurtz said five percent of IRS' criminal tax investigative effort is directed at narcotics traffickers; and overall a total of 30 percent goes into the combined areas of narcotics, organized crime strike forces, gambling and the like. Kurtz warned against devoting too many special agents to the special enforcement program aimed at organized criminals. He said there "would be risks to the voluntary compliance system if a disproportionate amount of our criminal enforcement resources were directed against any one particular sector of our society, with the effect of ignoring tax crimes in other sectors." Kurtz said he did not know how honest citizens would comply with the tax laws if they felt that the bulk of IRS resources were used in pursuit of organized crime. He said IRS ideally should have "an appropriate presence in all areas." In deciding how to allocate resources, Kurtz said "management makes hard choices" because the number of tax crimes will always exceed IRS' capability to investigate (p. 378).

COOPERATION

Kurtz said IRS is cooperating with DEA and other law enforcement agencies. He said he understood the need to respond promptly to disclosure requests and said IRS is trying to speed up its procedures in this area (p. 379).

Admitting some shortcomings at IRS, Kurtz referred to "a weak point" in his administration of the disclosure provisions. Special agents who do come across evidence of non-tax crime in financial records are encouraged to report this information to the IRS national office where a decision is made as to whether or not to pass the data to the appropriate law enforcement agency, Kurtz said. But unfortunately, even though they are able to do this, IRS field personnel are not doing it and, Kurtz said, the Service will be devoting more time to educating special agents on what they can and should do under the Tax Reform Act (pp. 380, 452). As noted earlier in this report on page 51, IRS Assistant Regional Commissioner Richard C. Wassenaar testified about just such an instance. He said he had evidence that a policeman had accepted a bribe. He wanted to alert local authorities. The national office of IRS told him to tell no one about the alleged bribe. Wassenaar said the policeman is still on the force (pp. 222, 223).

When Kurtz testified that it would take more time for IRS to educate special agents as to how they could work more productively within the constraints of the Tax Reform Act, Senator Nunn countered by saying it had taken IRS and the Treasury Department more than seven years to disseminate one single form called for by the Bank Secrecy Act. Senator Nunn added, "The discouraging thing is it has been three years since the law passed and I understand the reaction out in the field but when we look at the other precedents, we have heard that it took IRS and Treasury seven years to get one form, Form 4789. We have a whole generation of young people that are out there exposed to drugs now, and with the tremendous increase in drug traffic, we just simply can't wait that long" (p. 452).

VALUES

Kurtz acknowledged that the protections of taxpayer privacy contained in the Tax Reform Act do restrict the sharing of information among law enforcement agencies and do make the process more cumbersome. But, Kurtz said, the legislative judgment behind the Tax Reform Act was aimed at balancing the "competing values" of privacy and law enforcement. "Effective criminal law enforcement is an important public objective," Kurtz said. "But we must also protect our citizens' reasonable expectation of privacy with respect to their tax affairs." Kurtz said the disclosure provisions of the Tax Reform Act are not perfect but they should not be amended without taking into account the effect of such changes on fairness and privacy. He said IRS is working with other agencies to try to formulate changes in the law that would improve law enforcement effectiveness and not sacrifice "legitimate privacy interests and considerations of fundamental fairness" (p. 80).

Kurtz said IRS did not in 1979 devote as many resources to narcotics investigations as it did in 1974. But, he said, much of the in-

CONTINUED

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vestigative work in 1974 was directed at relatively low level narcotics dealers. Today the IRS focuses on Class I and Class II traffickers, those drug dealers rated as the biggest by DEA, Kurtz said. Kurtz insisted IRS has not reduced its commitment to taxing the profits from narcotics transactions, nor is the Service any less willing to cooperate with DEA (pp. 385, 412).

Kurtz said IRS was investing less resources into its narcotics investigations but, at the same time, was obtaining improved results by going after higher level traffickers. Senator Nunn said the best information he could gather from experts in law enforcement is that it requires more of an investment of time and resources to investigate high level trafficking. Kurtz agreed, saying that it does cost more to pursue major traffickers but, he added, "there are many fewer cases." Senator Nunn said, "You are saying you are shifting your program, going after high level people and cutting agent man years down by two thirds. Those two, I submit, are totally incompatible. I don't think it is possible for anybody in law enforcement to agree you can do both of those at the same time. As a matter of opinion, it contradicts everything I have ever heard about law enforcement, the difference between going after the little people and the big people" (p. 412).

CRITICISMS

One of the criticisms against criminal intelligence gathering and investigation was that these programs are not cost effective. In his 1974 speech in Honolulu, former IRS Commissioner Donald Alexander said that in the future IRS involvement in anti-narcotics and strike force activities would have to measure up against the "revenue and professional criteria" which are guidelines for the use of all IRS resources. Alexander said law enforcement work would have "to compete openly and equally for resources against our regular tax administration activities." David R. MacDonald, who was Assistant Secretary of the Treasury when the Narcotics Traffickers Program was dismantled by Alexander, told the Subcommittee that the NTP was not considered to be cost effective and that was the reason the critics of the program used to justify cutting it back. In light of these assertions, Senator Chiles asked Kurtz if he felt IRS criminal tax enforcement programs were cost effective. Kurtz said criminal enforcement should not be judged in terms of direct revenue yield. Its cost effectiveness he said, is not seen in terms of new dollars collected but by how it affects and encourages overall compliance. "In all probability, the criminal enforcement effort is less cost effective than the civil audits of tax returns, but it has a different impact on taxpayers' willingness to comply with the tax laws," Kurtz said. He said narcotics traffickers make large amounts of money and rarely pay taxes on it and that funds spent investigating drug promoters is well spent even if the taxes reclaimed do not pay the cost of the investigation in every instance. Ordinary taxpayers are favorably impressed by the ability of IRS to convict underworld figures, he said (p. 389).

Singleton Wolfe, Assistant IRS Commissioner for Compliance, said the Service participates in joint criminal investigations less often today than it did in the mid-Seventies. The Tax Reform Act limited the

ability of IRS to work with the Justice Department, he said, adding that the number of jeopardy assessments has also declined. Criminal investigations come under the jurisdiction of Wolfe in the IRS chain of command.

OVERTIME

Tom Clancy, Chief of the Criminal Investigation Division, said there were restrictions on the use of automobiles, on overtime pay and on the use of informants in recent years and acknowledged that his division did have a morale problem during the Watergate era but that those days were behind the division now. "Today we are pretty far along with post-Watergate, with the Privacy Act, Freedom of Information, Tax Reform Act, plus the additional guidelines that have been established to provide the guidance to our agents of what they can and should be doing," Clancy said (p. 414). It was Clancy's intention to have the Subcommittee understand that morale was high in the CID and his special agents were satisfied with the management and guidelines they work under.

The witnesses from the national office of IRS brought with them statistics and other data that they offered as evidence that they were managing organized crime and narcotics traffickers investigative programs that were sufficient to meet the problem. But their statistics were often incomplete and vague, or they could not be reconciled with data the Subcommittee had already received from other sources. For example, the General Accounting Office reported that IRS makes little effort to coordinate the information gathering activities conducted in its 58 district offices. This failure contributes to a lack of national direction and control in criminal investigation matters, GAO said. Senator Nunn asked Clancy and Wolfe to respond to that criticism. Neither of them responded directly to the question. Commissioner Kurtz did not respond directly either but he did say, "Let me say the criminal function of the Internal Revenue Service is one that is integrally related to overall compliance activities. It serves the end, not only of investigating criminals, as such, but also has a very fundamental role in encouraging compliance by everyone. It is clearly closely related to the overall job of tax compliance" (p. 431).

That response, coupled with the whole tenor of the testimony by Wolfe, Kurtz, and Clancy that there were no problems at IRS in the criminal inquiry field, led Senator Chiles to say, "I guess really what we are getting at as much as anything else, and we can go around the Maypole a long ways, that everything we get from IRS agents, from U.S. Attorneys, from the Justice Department, from DEA, from Customs, from everything is that there has been a deemphasis in IRS in criminal enforcement in the Criminal Division. You can give us all kinds of facts, statistics—it is hard for us to play that kind of game with you—but the proof of it, I think, is in the morale of the people you have got yourself in the Criminal Division. They don't feel like they are an elite part of the Service now. They don't feel that they are treated as being one of the major important parts of the Service and if we get that perception and if all law enforcement people have that perception, I would certainly think that people that are out there as drug

traffickers are going to have that perception too. And I think our concern, more than anything else, is how do we reverse that"? (p. 431).

"I don't know the answer to it," Kurtz replied. He added, "I think there may be a morale problem in the criminal law investigation enforcement community generally in all of the criminal areas—one that I think was greater and is probably coming more under control—and not limited to criminal investigators within the Internal Revenue Service" (p. 431).

DECISION

Senator Nunn asked who made the decision to reduce investigations by IRS in organized crime and narcotics. Kurtz said he did not know. Wolfe said the decision was made in about 1974. He said, "I think when the programs were changed they said we would go into the higher echelon cases. I don't know if there was any decision made just to cut the number of resources and I don't know of any case that we had come up involving narcotics, or organized crime, that we have not worked for lack of resources.

"Basically, we said we would work any of those cases that meet our standards without any concern as to whether they exceeded a given level or did not reach that level. Of course, I think the Tax Reform Act has decreased their participation in the strike force area, certainly, and the fact that . . . some of the strike forces have been cut back . . . but not to my knowledge do I know of any instance that we have failed to work a narcotics case that was in the upper echelon that came to our attention or that we have uncovered through our own efforts" (p. 445).

Throughout the hearings witnesses discussed the Tax Reform Act's disclosure provisions. Particular attention was focused on the requirement of the statute wherein the requesting agency must be able to describe in some detail the tax return or tax information being sought. Yet the IRS is prohibited by law from telling anyone anything about the information. Therefore, the requesting agency is expected to have information about documents it has never seen. This dilemma came to be known during the hearings as the Catch–22 situation caused by the Tax Reform Act.

CHALLENGE

The challenge of trying to describe a document without ever seeing it or being briefed on it—or even knowing it exists—was discussed by Richard Fogel of the General Accounting Office. Fogel's comments, in this exchange with Subcommittee Chief Counsel Marty Steinberg, were reflective of the general view of most witnesses regarding the Catch–22 dilemma:

> Mr. STEINBERG. Let me ask you this, in following up on the Catch–22 situation. Under either the court order route or the agency request route, certain information has to be given to the court or to the IRS to receive back from the IRS information. Is that correct?
>
> Mr. FOGEL. Yes.
>
> Mr. STEINBERG. And yet, the prosecutor, or any other Federal agency, cannot see that information or be told about it in

order to meet the test of the court or the IRS to receive that information?

Mr. FOGEL. That is correct.

Mr. STEINBERG. Is that the Catch–22 situation we are talking about?

Mr. FOGEL. Yes, and again, that is why we think it is very appropriate to begin exploring how the law could be changed to eliminate that type of problem (p. 341).

Jerome Kurtz, the Commissioner of Internal Revenue, told Senators that the law reads the way it does because the Congress meant for it to read that way. If there is a Catch–22 in the statute, that's what Congress wanted, he said. In that regard, Subcommittee Chief Counsel Steinberg and Kurtz had the following discussion:

Mr. STEINBERG. . . . Every witness before this panel . . . has stated that in their dealings with the act, they face the Catch–22 situation of attempting to obtain information from the IRS without knowing what information they need to obtain.

Mr. KURTZ. It is exactly right. It is not Catch–22 at all. It is the explicit policy of the act. . . . Catch–22 to me . . . implies a nonsensical situation. . . . It is a deliberate policy judgment (p. 459).

VI. BANK SECRECY ACT AND OTHER LAWS AND POLICIES AFFECTING DRUG CASES

Bank Secrecy Act Was Not Fully Enforced

In a small town north of Los Angeles, a man opened an account in a bank with a $500 cash deposit. A month later the man returned to the bank. He carried a cardboard box. Inside the box was $2 million in cash. The man explained that the money was from Mexico. He said he feared that the peso was about to be devalued. He wanted his money in dollars and he wanted his dollars in American banks.

For two years, members of the Araujo heroin syndicate made cash deposits in the name of Pedro de la Cruz Alvarez in Southern California banks. Thirty-nine cash deposits ranging in size from $90,000 to $860,000 were made totalling more than $15 million.

These two actual cases, related to the Subcommittee by the U.S. Attorney's Office in Los Angeles, were precisely the kind of bank transactions that are covered by the Bank Secrecy Act, the 1970 statute which requires banks to report to the Government when someone deposits $10,000 or more in cash. But in both these instances the Bank Secrecy Act failed, not because the banks did not file the required forms—in both cases they did—but because the Government did not make proper distribution of the information.

$2 MILLION

Federal prosecutors did find out about the transactions, though. The U.S. Attorney's Office in Los Angeles learned of the $2 million cash deposit from the wife of one of its prosecutors. She heard about it from someone in a shopping center. Regarding the Araujo heroin gang's 39 deposits, Federal prosecutors, already investigating the heroin organization, were alerted through procedures established by the Bank Secrecy Act—but not until two years had gone by and all 39 deposits had been made and more than $12 million of the $15 million had been transferred to Mexico. During that two-year period, the currency reports would have been of great value to investigators. Until they received the reports, there were doubts that the case would succeed. Also during that period one of the principals in the Araujo gang fled the United States and never was brought to justice.

The Subcommittee tried to find out why in these cases and in many others the Bank Secrecy Act has not lived up to expectations in its nine-year life. The Bank Secrecy Act, formally known as the Currency and Foreign Transactions Reporting Act of 1971 (31 U.S.C. 1051 et. seq.), was enacted to provide Federal investigators with certain financial reports for use in criminal, tax and regulatory inquiries. Two provisions of the statute have special importance for narcotics investigations. The first provision says that banks must file reports with

the Internal Revenue Service on unusual financial transactions of $10,000 or more. These filings are done on form number 4789 and consequently are called 4789 reports. The statute also requires that form number 4790 must be filed with the U.S. Customs Service by any person or business entity that transports, mails or ships $5,000 or more in currency or other monetary instruments into or out of the United States.

While the Bank Secrecy Act became law in 1970, Treasury Department officials acknowledged to the Subcommittee that it was not until 1979—nine years later—that the Department started to set up the procedures for the use and dissemination of forms 4789 and 4790.

CURRENCY

Richard J. Davis, the Assistant Secretary of the Treasury for Enforcement and Operations, testified that his Department is worried about the fact that so few successful prosecutions have been made under the Bank Secrecy Act. One problem was the failure of the Treasury Department to adequately assemble, analyze and distribute currency reports, Davis said. He said that the "exemption list" was abused by persons and entities who claimed and received them but were not entitled to being excepted from the law. Davis said the act allows exemptions to be given to certain businesses which transact substantial numbers of currency transactions daily. The abuse occurred when businesses were placed on the exemption list which were fronts for organized criminals. Davis said banks and other financial houses were giving these exemptions and had become lax in seeing to it that the enterprises were legitimate. Now, he said, the rules for exemptions are tighter and banks must report to Treasury on their exemptions. The Department may direct the bank to take away the exemption in specific instances, Davis said. He did admit, however, that background inquiry on businesses on the exemption list has not been thorough enough. Nor, he said, is there any routine check with State, local and Federal law enforcement agencies on the persons involved in the businesses.

Senator Chiles suggested that Treasury publish periodically its exemption list and circulate it to local law enforcement agencies so that they could assist in identifying businesses which are on the exemption list and are serving as fronts for organized criminals. Acknowledging the additional paperwork requirements created by more comprehensive background checks on exempt companies, Senator Chiles said Treasury should place more of the burden on the banks for attesting to the legitimacy of the firms and their principals. Senator Chiles said those banks which do not take seriously their responsibilities under the Bank Secrecy Act should be made to understand that their continued failure will be publicized by the Government. "I notice that they are tremendously concerned about adverse publicity," Senator Chiles said. "The mere fact that we were starting to hold hearings in regard to banks caused a tremor to go through the banking community in South Florida—more than a tremor, it was shock waves . . . when Treasury and when this Subcommittee first started looking into the bank transactions caused a tremendous amount of concern.

PUBLICITY

"If they have some understanding that they could get some bad publicity out of this, where they are dealing in a cavalier fashion with people who are bringing in laundry bags full of money, that they should have every reason to believe, and to know, that those aren't coming from proper persons. I think you would find that would be one of the best safeguards you could have.

"I don't want to tar them if legitimately they wouldn't have known about these transactions. But where they are being sort of greedy or selfish in taking those deposits, knowing that it is tainted money, they have got to know there is a downhill side on that" (p. 155).

More cooperation from the banks was also called for by Irvin B. Nathan, Deputy Assistant Attorney General in the Criminal Division of the Justice Department. He said the banks need to work harder at compliance with the requirement that they report all cash transactions of $10,000 or more. There had been few prosecutions for noncompliance, he said, but should neglect of the law become widespread there was no way Justice could cope with it alone. What is needed, he said, is more enthusiasm on the part of the banks to recognize the problem the Bank Secrecy Act was designed to solve and to help the Government solve it. "We simply cannot have a situation where legitimate businessmen turn their backs on the issue," Nathan said. "We need them to come forward and provide information and stop assisting with their eyes closed or with blinders on to this problem. We need closer supervision by the bank regulatory agencies to make sure there is compliance with the Bank Secrecy Act. Maybe there should be some amendments that would require reporting with respect to wire transfers as much as with respect to cash deposits because, of course, the narcotics financiers who are becoming increasingly sophisticated, simply transfer their funds by wire from banks in this country to other banks in this country and also to foreign banks" (p. 32).

GANG

The Araujo heroin gang prosecution is a good example of what positive results can spring from sound financial investigation backed up by spirited cooperation among Justice Department, Drug Enforcement Administration, Customs and IRS investigators. But, according to the man who prosecuted the Araujo gang, the case also had serious difficulties that were frustrating because they could have been avoided. Robert Perry, the Assistant U.S. Attorney in Los Angeles who headed the narcotics prosecution, told the Subcommittee about the two-year delay in obtaining currency reports on the gang members' $15 million deposits in the fictitious name of Pedro de la Cruz Alvarez. Nonetheless, the reports were better late than never, Perry said, attesting to the great value of currency reports in any case based on financial investigation. He said the inquiry was bogged down until the reports arrived. "I would say that we had our investigation very definitely stalled and we really weren't going very far," Perry said. "We had some stale informants who were growing staler, and it was just a very difficult case, and it looked like we were going to have

to move on to other things and then we learned about the money and we got IRS involved and we were able to make the case" (p. 111).

Perry recommended creation of a system whereby currency transaction reports would be made part of an overall intelligence filing system. That way, he said, investigators could more readily identify, cross reference and match known criminals and their activities with suspicious bank transactions. Perry said that in order to receive a currency report from the Treasury Department he must request the report in the name of the person who made the deposit. Perry said that in the Araujo case this procedure would never have led him to the gang members because their accounts were in the name of Pedro de la Cruz Alvarez. Therefore, Perry concluded, an analysis unit should be formed to flag all suspicious currency reports for referral to the appropriate Federal investigative office.

DEPOSITS

David R. MacDonald, former Assistant Secretary of the Treasury, said Internal Revenue Service authorities could have made effective use of the forms 4789 and 4790 regarding large cash deposits and transfer of large sums in and out of the country. He said these forms could have been of value to IRS in tracking down foreign bank accounts held secretly by Americans. But IRS chose instead not to make the most of this tool. Moreover, he said, IRS and other Treasury Department components were not as willing as they should have been to help other law enforcement agencies use the new statute and the documentation it generated. "IRS would not cooperate in our effort to make this information available as Congress had intended," MacDonald said. "This caused years of delays in dissemination of vital information which could have been used to track down narcotics traffickers and organized crime figures" (p. 264).

Also critical of IRS in this regard were two former senior IRS intelligence officials, John Olszewski and Lee Venable. They testified that IRS collected thousands of 4789 forms regarding bank cash deposits of $10,000 or more but did nothing with them but let them pile up unstudied in service centers. They said that from their own personal experience many of these transactions could have provided important leads to the identities and activities of major narcotics traffickers and organized crime figures. They said this documentation would have been especially valuable to investigators trying to track down the financial routes criminals used to transport their illicit money.

Elmer B. Staats, the Comptroller General of the United States, recalled a General Accounting Office study of April 1979 in which IRS was criticized for not developing a compliance program to ensure that required currency forms were filed. GAO said IRS had not only failed to enforce the law, it had neglected to make good use of those forms it did receive.

SEIZURES

Nathan and Davis said the Bank Secrecy Act should be amended to enable the Government to give cash rewards to persons who volunteer information that leads to currency seizures. They said Govern-

ment needs to provide incentives to encourage people to enlist in the drive against narcotics traffickers and financiers. They said the rewards would cost the taxpayer nothing because they would be taken from the currency seized.

A second amendment to the Bank Secrecy Act was recommended by Nathan and Davis. They proposed writing new language for the statute in which the authority of the U.S. Customs is spelled out specifically regarding searches of persons suspected of carrying currency and monetary instruments over the $5,000 limit in and out of the country. As the statute reads now, it is unlawful to enter or leave the United States without filing a form revealing the transport of that sum of money. But, while Customs officials have the constitutional right to search travelers suspected of carrying contraband such as jewels and drugs, there is debate over whether they may use this authority to search for currency or monetary instruments. The statute as presently written calls for a search warrant preparatory to the Customs search.

The Bank Secrecy Act needs to be amended in one other way, Nathan and Davis said. Section 231(a) of Title 31 should be changed to include attempts to import or export $5,000 or more without filing the required form, they said, pointing out this dilemma faced by Customs authorities: Federal courts have held that the law defines the crime of transporting currency without reporting it as being committed when the violator actually leaves the United States. Thus, authorities must stand by and let the violator actually leave the country—only then has he committed the crime. But once he has left the United States the currency carrier is outside American jurisdiction. He cannot be arrested by American authorities. Nathan and Davis said the dilemma is easily avoided by making it a crime to attempt to import or export unreported currency and monetary instruments. Then—once the law is changed to include the attempt—a person who tries to clear Customs at an American airport, for example, and is found to have more than $5,000 hidden in his luggage would have violated the law without actually boarding the aircraft. At this writing, legislation is pending before the Congress that would amend the Bank Secrecy Act by making it illegal to attempt to violate the statute.

Subcommittee Examines Bail Policy

The Subcommittee received testimony about the effects of low bail requirements on DEA's efforts to immobilize major narcotics traffickers.

Jimmy Chagra was a reputed narcotics dealer of considerable wealth. Just how wealthy he was was apparently not known, at least not to the judge who allowed Chagra to remain free on a $500,000 bail following his conviction on a drug charge. Chagra, deciding he would rather forfeit a half million dollars than go to jail, jumped bail. According to Peter B. Bensinger, Administrator of the Drug Enforcement Administration, the Chagra case is a good example of why judges should set higher bail for narcotics traffickers. "For the trafficker with thousands or even millions in cash at his disposal, bail is merely another business expense," Bensinger testified. "For Jimmy

Chagra in Texas, it was a ticket to freedom after being convicted" (p. 66).

The Chagra case is one of many instances of how bail presents little difficulty to major drug traffickers. Bensinger cited two more examples. In the first, two men were arrested, charged with manufacturing PCP, and released on bail. While on trial for that charge, the same two men were arrested and charged with conspiring to manufacture PCP. Enough material to make ten pounds of PCP was seized at the time of their second arrest. In the second example, a man was arrested on drug charges and released on bail. While out on bail, he was arrested in another State and charged with conspiring to smuggle 58 pounds of cocaine from Bolivia to the United States.

FELONS

Bensinger said accused drug violators often return to the illicit drug business before trial. He said some drug traffickers, who already are convicted felons, are being released on low bail amounts or on personal recognizance. Bensinger said that many drug traffickers simply do not show up in court for their trials. Often the bail violators leave the country.

A 1977 DEA study cited by Bensinger showed that 71 percent of DEA's serious defendants were released on bails of $10,000 or less. More than half of these defendants were free on bond for seven months to a year. The DEA survey indicated that there were wide regional discrepancies in average bail amounts for the same drug offense. It was also shown that nearly half of the charged drug traffickers were recidivists or foreigners in this country illegally. "There is a clear need for reform of the bail system," Bensinger said, "The current system does not work" (p. 66).

A similar view was given by the House Select Committee on Narcotics Abuse and Control in a 1977 report. The Committee said that current law allows major traffickers to be released to the community and a significant number of these go right back to their illegal drug activities; or they become fugitives. (Exhibit 5, p. 110.)

The U.S. Attorney's Office for the Central District of California reported that 40 percent of all narcotics violators in the district jumped bail and forfeited bond from 1976 to 1979. (Exhibit 17, p. 110.)

The Bail Reform Act of 1966 (18 U.S.C. 3146 *et seq.*) was passed to assure that criminal defendants, regardless of their financial status, are not needlessly detained awaiting trial. Under the Act, the judge is to take into consideration whether or not bail will insure "the appearance of the person as required." The Bail Reform Act does not address the issue of whether, pending trial, the defendant is likely to commit criminal acts, such as narcotics trafficking and pose a "danger to the community." In another section, 18 U.S.C. 3148, the Act provides that in capital offenses—those crimes punishable by death—the judge may refuse bail on grounds that the defendant's continued freedom may threaten people. Drug violations are not capital offenses.

That section also provides that defendants in capital cases and defendants convicted of criminal acts but awaiting sentencing or the outcome of an appeal may be released on bail but only if the judge feels that the defendant will appear in court and poses no danger to any other person or the community. If the judge decides the opposite is true, the defendant can be held without bail. Where the danger to the community rationale is used to detain a convicted drug offender awaiting appeal, there must be substantial evidence that the community would be threatened by the defendant's release.

According to Irvin B. Nathan, Deputy Assistant Attorney General in the Criminal Division of the Justice Department, one way to accommodate the provisions of the Bail Reform Act, and at the same time strongly encourage the defendant to show up for his trial is to make bond so high that even bigtime drug traffickers will think twice about posting or jumping bail. According to Nathan, that is one of the advantages to making financial investigations into major drug syndicates. Nathan testified that frequently judges set low bail because they are not aware of the large amounts of cash the defendant is alleged to be dealing in. "I don't think that often we have provided enough information to the courts as to the magnitude of the problem, both with respect to that individual and the problem to the community generally," Nathan said. "I think we could enhance our ability to do that if we had before the court tax violations as well as in which we were given an opportunity to demonstrate the amount of money that is available and the likelihood that these individuals can meet the high bail and go out and continue to traffic" (p. 47).

As early as 1973, the U.S. General Accounting Office warned that drug traffickers too often were being released on bail for long periods of time and were engaging in illegal narcotics transactions. Again in October of 1979, a GAO report raised the bail issue, pointing out the low bails and bail-jumping traffickers have weakened the effect of drug enforcement. In this 1979 report, GAO noted that to offset the problem, it had been proposed that the Federal bail statute be amended to enable judges setting pretrial bail in all serious, noncapital cases to consider whether a defendant released on bail would pose a danger to the community.

GAO recommended that the Congress consider amending the Bail Reform Act of 1966 to enable judges to consider the likelihood of the defendent's participation in drug trafficking in the factors that go into the decision to set bail. GAO concluded, "The bail law itself has hampered immobilization efforts. The Bail Reform Act . . . allows many alleged drug traffickers to be released before trial, providing them the opportunity to traffic in drugs."

Sentencing Policy Is Reviewed

The Controlled Substances Act of 1970 provides a maximum penalty of 15 years' imprisonment per count for first offenses and 30 years' imprisonment per count for second offenses. Judges rarely give sentences that tough, however. And, just as he had urged reform in the Bail Reform Act of 1966, Drug Enforcement Administrator Peter B. Ben-

singer also testified in support of longer sentences for drug violators. "I think that drug traffickers weigh the risks involved when considering whether or not to set forth on a particular venture," Bensinger testified. "The present structure of the Controlled Substances Act does not send a strong enough signal to the trafficker of large quantities of marijuana. The Act in its present form makes it plain to the trafficker that a great risk lies in dealing in heroin, but not in marijuana" (p. 66). Bensinger recommended that penalties for marijuana trafficking be increased. He said marijuana trafficking is "big business" and sentences should reflect the seriousness of the offense. He noted that recently judges had given stiffer sentences when the marijuana violations were found to be connected with large cash seizures.

Jim Smith, the Florida Attorney General, also asked the Subcommittee to consider increasing Federal drug sentences. Violators know Federal penalties are mild compared to laws in those States, like Florida, which have adopted tougher sentencing. ". . . our law enforcement people complain that criminal prosecutions for narcotics violations under Federal laws result in slap-on-the-wrist sentences of a few years," Smith testified. "When Sheriff Frank Wanika of Lee County arrested a group of smugglers on Fine Island in cooperation with Customs agents, the defendants pleaded to go into Federal custody because of the more lenient sentencing laws" (p. 164).

STUDY

A study by DEA of 919 defendants whose Federal court dispositions were reported in 1976 disclosed that 24 percent of the convicted serious offenders—those found to be trafficking in, distributing drugs—received probation. Sixty-one percent of those convicted of serious offenses received sentences of three years or less. And 81 percent received sentences of six years or less. The study found that actual time served averaged 43.2 percent of the sentence imposed.

The General Accounting Office found that court statistics reveal that drug violators are usually not incarcerated for long sentences. "This continues to negate the deterrent effect of prosecution," GAO said, citing its own 1973 survey that showed most convicted narcotics violators were receiving sentences of five years or less. "There was a tendency in these cases to impose short periods of incarceration even though the cases involved major traffickers who profited substantially from their crimes," GAO said. A second survey, this one done at GAO's request by the Administrative Office of the U.S. Courts, showed that of 2,143 serious offenders sentenced in fiscal year 1977, 20 percent received probation, 28 percent received three years or less, 21 percent got three to five years and 30 percent were sentenced to five years or more. GAO noted that most narcotics convicts are eligible for parole after serving one-third of their sentence.

Justice Department's "Dual Prosecution" Policy

The "dual prosecution" policy of the Justice Department says, in general, that a person will not be tried for two similar and related but separate crimes stemming out of the same series of actions. In effect, the policy requires that all offenses arising out of a single transaction,

such as drug trafficking and evading taxes on the ensuing profits, will be tried together—or, in the absence of trying them together, the first prosecution will be sufficient. For example, a major narcotics trafficker, the subject of a comprehensive tax evasion case, might also have been charged with a misdemeanor violation of simple possession of a small amount of illicit narcotics. While the Internal Revenue Service works up the much more serious tax case, the man is tried on the misdemeanor. He is convicted and given a light sentence. Meanwhile, the IRS completes its tax evasion investigation and refers it to the Tax Division of the Justice Department for prosecution. Justice declines prosecution on the tax evasion charges because of its "dual prosecution" policy. Critics of that policy say it subverts the notion of even-handed justice, it is inefficient and wasteful of Government resources and it gives major drug dealers an advantage they don't deserve. Criminals should be charged with both crimes when both crimes are serious; or, when one offense is minor and the other serious, the more serious charge should be prosecuted, critics say.

One such critic is Richard C. Wassenaar, Assistant Regional Commissioner of the IRS' Criminal Investigation Division for the Western region. He testified, "I guess I find it difficult to find the substantial narcotics trafficker who is not guilty of some other kind of misdemeanor. If the conviction of those misdemeanors is, in fact, going to prevent us from prosecuting them on felony charges, then perhaps we are in the wrong business" (p. 240).

Oliver B. Revell, Deputy Assistant Director of the FBI's Criminal Division, had a similar view. He pointed out that the "dual prosecution" policy, coupled with the Tax Reform Act's requirement of little or no exchange of information between IRS and prosecutors, resulted in organized criminals being charged with one set of offenses while another series of tax charges is being readied by IRS. What happens, Revell said, is that IRS often has no reason to proceed criminally against those criminals who are breaking other laws along with their tax violations. "A very important area of criminal law enforcement" has ben cut off, Revell said (p. 245).

REVIEWS

The Comptroller General of the United States, Elmer Staats, testified that GAO has examined the dual prosecution policy and found it unsatisfactory. He said time delays and duplicative legal reviews affect all criminal tax cases. These delays have a particular impact on IRS' drug-related investigations because narcotics violators are often arrested and convicted on drug charges before IRS can fully develop the related tax case for prosecution, Staats said. He said that when the drug charges are tried first, the Justice Department usually declines to prosecute for criminal tax fraud. "In such instances," Staats said, "IRS has wasted scarce investigative resources and the drug dealers' resources remain intact" (p. 310).

The General Accounting Office cited two illustrations of how the dual prosecution policy works to the disadvantage of comprehensive, balanced law enforcement. In the first case, a person who had failed to report at least $150,000 during a two-year period was sentenced to one

year in prison on a narcotics misdemeanor. IRS attorneys did not forward this case to Justice for review because the person was already in prison and the dual prosecution policy would have precluded another trial. In the second example, the Justice Department declined to prosecute a major narcotics violator on criminal tax charges because he pled guilty to a felony indictment count carrying a maximum sentence of five years in prison. Subsequently, the subject was sentenced to five years' probation. "IRS' investigation proved useless from a criminal tax standpoint, although civil actions may result," Staats said (p. 310).

About these cases and the Justice Department's dual prosecution policy in general, Staats said, "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" (p. 310).

Subcommittee Studies Posse Comitatus Statute

During the hearings, several witnesses discussed the ways in which the United States Armed Services could assist Federal drug enforcement in combatting the drug traffic. But, they said, such assistance has been limited by the current interpretation of the Posse Comitatus statute, 18, U.S.C. 1385. The statute was designed to preclude the use of Federal troops to enforce civilian law. The Posse Comitatus statute, adopted after the Civil War, makes it unlawful to deploy "any part" of the armed services "as a posse comitatus or otherwise to execute the laws" except in those instances specifically authorized by the Constitution or Congress. A fine of up to $10,000 or a sentence of up to two years, or both, can be imposed on violators of this law.

Robert Asack, Director of Air Control for the U.S. Customs Service, told the Subcommittee that often radar and other electronic detection equipment used by civilian law enforcement agencies is not sophisticated enough to track the movements of drugs as they are shipped along and across and near the U.S. border. Traffickers frequently ship drugs in modern aircraft and fast moving ocean vessels. Asack said military installations along the border are often far better equipped to note the movement of drugs than are civilian authorities. The military has permitted drug enforcement officials to have access to radar equipment which has been of assistance in identifying some smugglers. However, Asack testified, whenever military personnel who routinely use radar to monitor U.S. borders get information on a drug smuggler they do not generally pass this information along to law enforcement. He recommended that the law be amended to clearly allow military personnel to serve this function (pp. 136, 137).

PRINCIPLE

Richard J. Davis, Assistant Secretary for Enforcement and Operations of the Department of the Treasury, also addressed the issue of posse comitatus in his testimony. Davis noted that the general principle of military non-involvement in civilian affairs was a sound one, and

that efforts to modify this doctrine should be undertaken with caution. He would "however, like to see an expansion in specific areas of cooperation with the Coast Guard, and in general would like some modifications to be made in the support area" (pp. 136, 137).

Florida Attorney General Jim Smith said military assistance would be a major step forward in controlling the flow of smuggled drugs into his State. Smith said he does not favor the use of military resources in civil law enforcement except in "the most dire circumstances." But, he said, so serious is the drug problem in Florida that such extreme circumstances exist now. Smith recommended changing the law in such a manner as to allow the transfer of information obtained in military surveillance to civilian authorities (pp. 165–166). He said the services routinely electronically gather information about aircraft and ship movements and this data would be of considerable value to civilian authorities.

The House Select Committee on Narcotics Abuse and Control commissioned the Congressional Research Service of the Library of Congress in 1977 to do a study of the application of the Posse Comitatus statute to the use of the military in the enforcement of narcotics laws.[1] According to that study Congress enacted the Posse Comitatus statute in response to various alleged abuses of the use of military force in civilian matters following the Civil War. The original intent of the statute was to prevent the use of soldiers to assist the local marshal in carrying out his work. Senators and Congressmen also objected to the use of troops to collect taxes, maintain order during strikes and influence elections by intimidating voters. The Congress wanted to insure that civilians would not be subjected to military law and discipline. The law was supposed to prevent the military from being used to carry out a court order, process or other lawful command of a civilian government. The Congress intended that the only proper role for the armed services was to suppress forces too powerful for civilian authorities to overcome, the research study reported.

RULINGS

Since its enactment, the statute has been interpreted by various court decisions including *Wrynn* v. *U.S.*, 200 F. Supp. 457 (E.D., N.Y. 1961); *U.S.* v. *Walden*, 490 F2d 372 (4th Cir. 1974); *U.S.* v. *Casper*, 541 F2d 1275 (8th Cir. 1976); *U.S.* v. *McArthur*, 419 F. Supp. 186 (D. N.D. 1076); *U.S.* v. *Red Feather*, 392 F. Supp. 368 (D.S.D. 1974); *U.S.* v. *Jaremillo*, 380 F. Supp. 1375 (D. Neb. 1974), 510 F2d 808 (8th Cir. 1975). The most recent event which revived interest in the statute was the situation at Wounded Knee, South Dakota, where various members of Indian tribes demonstrated and troops were used in various ways to assist Federal law enforcement in dealing with the situation.

In its study of Posse Comitatus, the Congressional Research Service said the statute clearly prohibits the use of military personnel to perform authoritative acts such as making arrests, searches, seizures or custodial interrogations on civilan offenders within the civilian

[1] "Use of Military against Drug Smugglers in Southwestern United States," Congressional Research Service, Library of Congres, Apr. 14, 1977.

community. Similarly, the statute prohibits the use of military personnel as informants, undercover agents or non-custodial interrogators in a civilian criminal investigation that does not involve potential military defendants or is not intended to lead to any official action by the armed forces.

However, court rulings on how the Posse Comitatus statute applies to "indirect" military assistance to law enforcement have varied substantially. The legislative history of the statute has provided courts virtually no guidance as to whether or not purely support services might be legally provided. Consequently, cases have had to be resolved on an ad hoc basis without a consistent informing principle, and have frequently been contradictory, the CRS study said.

RADAR

There is no case on the books which definitively answers the question whether the military may or may not provide to drug enforcement officials such things as information gathered from radar and other sources; the loan of military equipment and facilities; or the services of the military to provide training and expert advice. These are the areas where cooperation is currently being sought. However, the legality of engaging in these cooperative efforts is tied to an interpretation of an inconclusive body of case law, the CRS study said.

The military has interpreted the law as allowing it to supply some forms of equipment for use by drug enforcement officials. But for the most part, the armed services have not ventured further into providing other forms of support services to drug enforcement. The CRS study concluded that the military's caution in entering this area may well be justified. Given the broad language of the Posse Comitatus statute and the case law as it stands today, the most probable result of a case challenging the use of military support services in apprehending a drug offender would be a finding that such military support was in violation of the Posse Comitatus statute, the Congressional Research Service concluded.

VII. FINDINGS AND CONCLUSIONS

This report concerns how Federal law enforcement can more effectively investigate and prosecute major drug dealers and their syndicates. The Subcommittee recognizes that law enforcement is not the only solution to the drug problem. There is great demand for illicit drugs in this country. Until demand subsides the problem will still exist.

However, it is also apparent that the availability of illicit drugs has reached epidemic proportions. Law enforcement cannot reduce demand. But it can do a better job of controlling the supply of drugs being sold. To that extent, it should be a deep embarrassment to the United States Government that this Nation is literally awash in illicit drugs. Heroin, cocaine, marijuana and all varieties of synthetic drugs are available to anyone who wishes to buy. The richest nation in history is also the most dependent on drugs—and the least capable of controlling their importation, distribution and use.

The U.S. General Accounting Office in October of 1979 gave a description of how widespread the drug trade is. Since 1973, GAO said, 450,000 to 500,000 persons have used heroin daily. In 1977, about 1.7 million persons used heroin occasionally. About 7,800 persons died in 1977 as a result of drug use. About 19 percent of property crimes are heroin-related. The use of the hallucinogen PCP has nearly doubled from 1978 to 1979 and surpassed the use of LSD. PCP is regarded by many experts as potentially the most harmful of the commonly used drugs. Cocaine and marijuana have moved from the fad stage and have become accepted by an increasing number of American people. Their use often begins by boys and girls as young as 12 years old. In 1977, it was reported that cocaine was being used by sixth graders in some schools.

PERCENTAGE

GAO said the public uses marijuana more than any other psychoactive drug. About 43 million Americans have tried marijuana, and its use has been rising steadily in the last 10 years. Marijuana use is on the increase in the armed forces. The percentage of young people using marijuana on a daily basis is increasing and is now approaching nine percent among high school seniors nationwide. Average monthly use of marijuana is estimated at one person in 25 for 12 and 13 year olds; and one in seven for 14 and 15 year olds. The American market consumes between 60,000 and 91,000 pounds of marijuana a day, resulting in an outlay of between $13 billion and $21 billion a year. GAO said the enormous profits of drug trafficking attract many profit seekers who see, and often realize, opportunities in the narcotics trade that far outweigh those offered by legitimate businesses.

The drug traffic is so large that the amount of money it generates is beyond most people's comprehension. The National Narcotics Intel-

ligence Consumer Committee, an organization of Federal agencies working to control drugs, estimated that the retail value of illicit drugs in the United States is between $44 billion and $63 billion. By comparison, the Department of Commerce estimates that American consumers spent $50.3 billion for the purchase of new cars in 1978.

There is no question then, that the drug problem is massive. To bring it under control, the Federal Government must mount a comprehensive campaign, using all the resources available to it. Above all, those components of the executive branch involved in drug enforcement—the Justice Department, the Drug Enforcement Administration, the Federal Bureau of Investigation, the Customs Service, the Internal Revenue Service—must work in close and willing harmony. There is no time for interagency rivalries or bickering. The American people have no patience for excuses and explanations as to why Federal efforts cannot substantially reduce the drug trade.

HARMONY

Insofar as the IRS is concerned, the desired harmony does not exist. The IRS should be a principal participant in Federal drug investigations. IRS is not involved to the extent it should be. Moreover, its limited participation in Government drug control efforts is declining. There are two major reasons why IRS is not participating. First, some IRS policymakers do not wish for IRS to play an active role in investigations of organized criminals and drug traffickers. Second, the disclosure provisions of the Tax Reform Act of 1976 frequently prohibit and discourage IRS involvement in investigations of organized criminals and major drug syndicates.

In all too many instances, IRS has stopped working with the Justice Department, DEA, the FBI, and other Government components as they seek to forge a coherent strategy to control the drug traffic. Such a strategy cannot be built or implemented without IRS. This is because the most effective method of disrupting the big drug syndicates is through financial investigation—and financial investigation is a form of inquiry which the IRS can do better than any other Federal agency. For the Federal Government to conduct complex financial investigations of major drug syndicates and not use the IRS is comparable to a baseball team not using its best players for the championship game.

Financial investigation includes tracing the movement of funds, analyzing business transactions, studying investment patterns, comparing lifestyles with income and, in general, establishing evidence of criminal conduct through evaluation of how alleged drug dealers conduct their financial affairs. By training, temperament, and on-the-job experience, IRS special agents are the best the Government can field to conduct financial investigations.

The Tax Reform Act of 1976 was a comprehensive tax bill that, among other things, tightened the rules governing the disclosure by IRS of tax returns, tax information, and non-tax data. The disclosure provisions were enacted in the wake of Watergate. Based on proven and alleged abuses, they were intended to enhance the privacy of tax returns and prevent their being used for political purposes.

REQUIREMENTS

According to the disclosure provisions of the statute, the Justice Department and other law enforcement components may obtain a tax return or taxpayer return information for investigation of non-tax crimes such as drug trafficking by securing an *ex parte* court order. Before the court order is granted, the judge must be satisfied that three requirements have been met. First, it must be shown that there is reasonable cause to believe that a crime has been committed. Second, it must be shown that there is reason to believe that the tax information being sought is probative evidence of the commission of the crime. Third, it must be shown that the information cannot be obtained from another source and is the most probative evidence available.

Satisfying all three requirements can be difficult. It is sometimes impossible. The requesting agency often is placed in the position of having to know the details of documentation it has never seen or been briefed on. Justice Department officials call this dilemma their "Catch-22" problem. Prosecutors ask, "How can we be expected to describe in such detail tax documents we have never seen or been told about?" The answer is they should not be expected to do the impossible.

The disclosure provisions and the way they have been applied have had an adverse effect upon law enforcement and have reduced cooperative work between IRS and other agencies. The disclosure provisions make it difficult to obtain IRS assistance, even in cases that were initiated jointly by IRS and the Justice Department. The disclosure provisions, as interpreted by IRS, prohibit it from telling other agencies what cases it is working. This leads to unfortunate situations in which IRS investigators, assigned to organized crime strike forces, sit by silently while other Federal agents try to coordinate their efforts. Everybody cooperates—except the IRS people. Morale suffers. Some U.S. Attorney's offices, impatient with the Tax Reform Act and with IRS recalcitrance, have begun to exclude IRS from joint projects. Even when the statute's requirements are met and tax returns are disclosed, the bureaucratic delay consumes so much time that the value of the evidence obtained is diminished, if not lost altogether. In addition, the demonstrated expertise that IRS brings to financial investigations is lost to other law enforcement agencies. It is as if IRS were not only a separate agency but were also part of a separate government, serving purposes and goals having little to do with this Government's avowed resolve to control the drug traffic.

SUBPOENA

In the "Case of the Trash Can," the problems caused by the disclosure provisions were clearly demonstrated. DEA was working on a drug inquiry in Philadelphia. Drug agents learned that IRS was on the case too, and that one of its investigators had found a trash can with evidence that would have been valuable to the DEA case. The Federal prosecutor in the DEA case subpoenaed the IRS investigator. IRS refused to allow the investigator to respond to the subpoena, arguing that under its interpretation of the Tax Reform Act, a court order was required. The law has been interpreted to mean

that tax return information includes almost anything that comes from the taxpayer in the way of documentation. By the time the prosecutor was given the evidence from the trash can, the trial had ended, the suspect had been convicted anyway and many Justice Department attorneys were wondering about the value and intent of a law that prohibits the most elementary cooperation between IRS and other agencies.

The disclosure provisions have been interpreted in a strict manner by IRS. One DEA agent gave an IRS man a list of persons whose activities might be of interest in future tax cases. The DEA agent misplaced his own copy of the list. He asked the IRS man for a copy. The IRS investigator refused, saying the list was now a tax matter and the Tax Reform Act precluded him from sharing it with anyone, including the agency which gave it to him. Similarly, an FBI agent asked IRS to examine and copy evidence he had developed and then return it to him. IRS took the information but refused to return it, citing the disclosure provisions of the Tax Reform Act. These examples demonstrate the folly caused by the disclosure provisions.

IRS investigators often come upon non-tax criminal information in the normal course of their work. No longer can IRS automatically turn this information over to the appropriate law enforcement agency. It cannot even alert the appropriate agency to request the information. The decision is left in the hands of the Secretary of the Treasury, who, acting upon the advice of IRS, may or may not decide to pass on the information to the appropriate agency. One IRS agent came upon evidence indicating that a policeman had accepted a bribe. Since he could not tell the local authorities, he asked IRS national office headquarters in Washington what to do. His directions were as follows: Do nothing, tell no one. The IRS investigator said he did as he was told, and the policeman is still on the force. The hypothetical situation in which an IRS investigator learns of a planned attempt to assassinate the President of the United States came up at the hearings. IRS field agents said they would probably alert appropriate authorities if they learned of such an attempt—but, they said, to do so would make them violators of the Tax Reform Act.

PETITION

There is a procedure through which another agency may request non-tax information from IRS. The head of the requesting agency may petition the Department of the Treasury Secretary. But it is unlikely that the request will ever be made because there is no adequate procedure through which DEA, for example, can be informed that such non-tax information is available and IRS is under no directive to trigger the procedure. Justice Department officials believe that IRS withholds information indicating non-tax criminal conduct. It is the Subcommittee's view that IRS should be obliged to report information of this kind to appropriate law enforcement agencies. Anyone who has knowledge about the commission of a crime should report it. All American citizens have this civic responsibility. No less should be expected of IRS.

The disclosure provisions of the Tax Reform Act have sent a strong signal to the law enforcement community, at the Federal and State

levels, that the Internal Revenue Service no longer will play an important role in organized crime and major drug investigations. As a result, IRS participation in organized crime strike forces, in grand jury investigations and in other joint projects has declined. Passage of the disclosure provisions has served to give moral backing to those policymakers at IRS who do not believe that it is the task of the Service to cooperate in investigations of criminals. It is the Subcommittee's view that criminals' profits are taxable and ought to be taxed. In addition, it is the Subcommittee's view that IRS should cooperate with other law enforcement agencies responsible for investigating and prosecuting drug traffickers and other organized criminals and that it should not hide behind the disclosure provisions of the Tax Reform Act of 1976 to avoid doing so.

SUMMONS

In addition to its disclosure provisions, the Tax Reform Act contains another section detrimental to good law enforcement. This section has to do with administrative summons served by the Internal Revenue Service on third-party recordkeepers of suspected tax evaders. Usually these recordkeepers are banks. The summons provision of the statute enables the taxpayer to invoke an automatic stay to stop the performance of the summons until the matter is pursued in court by IRS. Instead of stay, a more appropriate word would be delay—because delay is all, in fact, that is achieved. Each automatic stay has resulted in a delay of an average of nine months. One stay stopped a tax proceeding for 33 months. In one region of IRS, in more than 80 percent of these cases, the taxpayer did not even contest the summons when it came to court.

The beneficiaries of the new summons procedures are often tax criminals whose only interest is to enable their attorneys to invoke the stay in order to gain time. The passage of time works to their advantage. Witnesses move away or die or their memories fade. Government has enough trouble bringing tax evaders to justice. It should not have to contend with the contrived situation in which delays can be triggered for no other reason than that such a mechanism is available.

Commensurate with the problems caused by the disclosure and summons provisions of the Tax Reform Act are the difficulties created by the IRS and the idea, held by some of its policymakers, that working with other law enforcement agencies is unseemly and should be avoided whenever possible. Some officials in the IRS hierarchy believe that its mission is to collect taxes primarily from law-abiding citizens—and that drug traffickers and organized crime figures who earn taxable income illegally and do not pay taxes on it should receive no special attention.

PROHIBITION

The most celebrated instance of a person who committed crimes and paid insufficient taxes on his profits was Al Capone, the notorious Chicago mobster of the Prohibition era. In the *Sullivan* decision of 1926, the United States Supreme Court ruled that a person who lived outside the law in his income-producing activities was still account-

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able to the law when it came to taxes. With that decision, the Government began moving against mobsters who had heretofore managed to evade conviction for their non-tax crimes. The *Capone* case is the most famous example of a criminal whose very success in crime and the huge profits he earned from it, led to his undoing. The more money he made, the more taxes he owed—and the more taxes he owed, the more vulnerable he was to prosecution for tax evasion.

Capone's imprisonment for tax evasion was not the first example of how effective the Internal Revenue Code can be in bringing otherwise uncatchable criminals to justice. Nor was it the last. Well known and powerful criminals like Frank Costello in 1957 and Joseph (Doc) Stacher in 1964 were convicted of tax evasion, along with many more hoodlums of similar renown. Even in the case of a non-tax crime, IRS can be of assistance. The Nicky Barnes case is an example. In Harlem, Barnes headed one of the biggest heroin syndicates in the country. His tax returns showed he claimed $250,000 in miscellaneous income. That and other data led to his conviction, a life prison sentence for him and long prison terms for his chief accomplices. It should be noted, however, that in the Barnes case the Tax Reform Act's disclosure provisions prevented his tax returns from being turned over in a timely fashion. Had the delay been much longer, Justice Department officials say, this important case might have been lost.

It is the Subcommittee's view that the tax laws, as well as the investigative resources of the IRS, are a valuable tool for law enforcement against organized criminals and drug traffickers. This tool is especially useful against major drug dealers and their syndicates. Nowhere in criminal activities is the potential greater for massive profits quickly gained than it is in the drug trade. As with Capone, the bigger the illicit profits, the more vulnerable the criminal to charges of tax evasion. And as with Nicky Barnes, even when the violator tries to satisfy the income tax law, the more difficult it is for him to conceal the criminal nature of his livelihood. It would be regrettable if the tax tool continued to decline in use in criminal investigations. This tool should be used with proper concern for the rights of the accused. That goes without saying. But it is the Subcommittee's finding that in recent years IRS has not done enough to use this valuable tax tool in investigations of organized criminals and major drug traffickers.

NATIONAL INTEREST

Investigation of the tax status of criminals is not unseemly work. It is difficult but it is also valuable, productive work. It is in the national interest. It may well be the most effective means of curtailing the growing drug problem. In light of the Government's obvious inability to prevent illicit drugs from being smuggled into the United States, the tax route, combined with financial investigation, constitutes a crucial available vehicle for immobilizing the big drug syndicates.

Justice Department spokesmen and other officials experienced in drug prosecutions place great stock in the value of IRS investigative capabilities. IRS criminal tax investigators are heroes everywhere but in their own agency. The law enforcement community has respect and admiration for the investigative skills of IRS personnel. Similarly,

mobsters themselves have a grudging respect for IRS. F. Harvey Bonadonna of Kansas City, Missouri, son of an organized crime figure who gave evidence against his father's accomplices, said he had noticed that in recent years the IRS was no longer investigating mobsters. Testifying before the Subcommittee on the subject of mob violence, Bonadonna said he was puzzled as to why IRS was less interested in the tax returns of organized criminals since the tax laws were the ones most feared by criminals. "I don't know what you, Senator Percy, or you, Mr. Chairman Nunn, can do about this," Bonadonna said, "[but] if you can motivate the IRS into getting facts accurately and investigating organized crime figures and making them prove where they are getting the money that they are spending [and] where they are getting the money they are losing at the gaming tables you would put the fear of God in them [and] you could put a damper on an organization overnight if you started this again." Bonadonna added that organized criminals "are more scared of the Internal Revenue Service than they are of the FBI." [1]

Other criminal investigators admit to their own shortcomings in the area of financial investigation, a discipline so critical to the success of prosecutions of the major drug syndicates. It may be that one day other Federal agents will have improved ability to put together solid financial investigation cases. But that day is not here yet. What is here is the most monumental drug problem in history. If the present leadership at IRS is unwilling to join in efforts to combat the drug problem, then it is time for new leadership with a different philosophy.

RESOURCES

The difficulty in enlisting IRS support in the war on drugs lies partly with the Tax Reform Act and partly with the Service itself. The Subcommittee finds the IRS allocates insufficient resources to its participation in organized crime strike forces and other joint projects with the Justice Department and its components. The Subcommittee finds IRS has not met its responsibilities to collect taxes from persons whose income is illegally earned. In bringing major narcotics dealers and other organized criminals to justice, IRS will be carrying out its duties more equitably, it will be helping in the Government's effort to control drug trafficking and it will be restoring the faith of the American people in the fairness of their tax system. Nothing so encourages voluntary compliance by law-abiding taxpayers than the sight of a big time mobster going to jail for tax evasion.

The Subcommittee makes the following additional findings:

(1) "We have been unable to obtain information in the possession of IRS regarding our political enemies." That statement is from a memorandum written at the Nixon White House by John Dean and an associate. It is language reflective of the Watergate era and it has no place in American Government and politics. But, regrettably, there were attempts by politically-inspired people like Dean to use IRS to damage persons perceived to be enemies of the President. There

[1] Hearings before the Senate Permanent Subcommittee on Investigations, "Organized Crime and Use of Violence," May 1, 1980, stenographic transcript, pp. 389–392, 411.

was also evidence that the FBI and the IRS had cooperated—sometimes officially other times informally—to use tax returns and tax information to embarrass and discredit political dissidents.

Congress felt steps should be taken to avoid a replay of these abuses of taxpayer privacy. Accordingly, the disclosure provisions of the Tax Reform Act were adopted. While the disclosure provisions did not address the problems created by a President who orders the IRS to audit his political enemies, the new statute did limit access to tax returns and tax information. The disclosure provisions, however, had another result. The provisions have placed undue restraints on the ability of Federal prosecutions to make use of tax returns and tax data in cases against major narcotics dealers and other organized criminals. The problem now is to remove the unnecessary restrictions on Federal prosecutors and, at the same time, retain procedures to assure taxpayer privacy. That is the challenge the Congress must confront if it is to maintain the proper balance between citizens' rights and effective, responsible law enforcement.

To that end, the Subcommittee believes the disclosure provisions of the Tax Reform Act should be amended so that tax return or other tax information needed in a legitimate criminal investigation can be obtained quickly and without fighting layers of bureaucracy. All court orders and requests should be made by the Justice Department to add prior legal review to any request for tax information as a further privacy safeguard.

The Subcommittee also finds that the summons provision of the Tax Reform Act is an impediment to good investigative tax work. This provision should be amended. The automatic stay provision should be dropped. In its place a procedure should be installed which would still allow the taxpayer to challenge a summons but would put the burden on him to petition the court and then demonstrate why performance of the summons would be unfair.

(2) The disclosure provisions of the Tax Reform Act have had the unfortunate effect of affording excessive and undeserved protection to criminals. But in the context of criminal investigations, the statute did very little to enhance the privacy of ordinary taxpayers.

Ordinary Americans who run into trouble with the Internal Revenue Service do so by such actions as claiming undeserved deductions or concealing income or by falling behind in their tax payments. The IRS is equipped to detect these types of transgressions and see to it that the questionable practices are made right. The IRS handles these matters by itself. There are no restraints on how IRS can process within the Service an income tax return or tax information regarding an ordinary citizen. The proper IRS officials see the data, an appropriate course of action is decided upon and that course of action is taken. These matters all come under the IRS's General Enforcement Program, or GEP. GEP accounts for 75 percent of IRS investigative budget. The disclosure provisions have little impact on GEP or on the taxpayers audited or investigated under GEP. The FBI, for example, is not called in when a taxpayer claims bogus medical deductions on his return. The IRS can handle that by itself under the general enforcement program. Under GEP, there is no need for interagency exchanges of information or joint task forces. IRS does not

even need the services of Justice Department prosecutors in these cases until they reach the indictment stage.

Where there is a need for the exchange of information, for cooperation, for joint effort, is in IRS's Special Enforcement Program, the SEP. SEP deals with persons who steal for a living, persons who break the law for a living—organized criminals, drug traffickers, smugglers, jewel thieves, persons who bribe public officials and officials who are bribed. Here the disclosure provisions of the Tax Reform Act are a barrier to effective law enforcement. Drug trafficking is against the law. It is also against the law not to pay taxes on income from the sale of illicit drugs. To put together a successful prosecution against the drug trafficker, interagency cooperation is required. Information must be exchanged. IRS needs to know what the Drug Enforcement Administration is planning. DEA needs similar information from IRS. Because of the disclosure provisions, and IRS' strict interpretation of them, the needed exchange of information is severely restricted or does not occur at all. This is more evidence of the necessity of amending the law and the need for a change of attitude at IRS.

Moreover, when viewed in light of the two different approaches IRS uses to investigate tax evasion, it is apparent with regard to criminal investigation that the ordinary taxpayer's privacy has not been enhanced by the Tax Reform Act. Investigation of the average American's tax return goes on as it did before the statute was passed. Those persons who have benefited from the disclosure provisions of the law are persons suspected of being major criminals.

(3) Some people believed that the disclosure provisions of the Tax Reform Act would somehow encourage compliance with the Internal Revenue Code. The theory went that as taxpayers were assured of additional privacy in their tax returns, they would be more inclined to report their income fully and accurately. The theory did not hold. According to IRS, compliance has not increased since passage of the Tax Reform Act. For whatever reasons, more Americans are failing to adhere to Federal tax laws. Making the situation worse is that because of the disclosure provisions—and because of IRS unwillingness to cooperate with other law enforcement agencies—fewer organized criminals and drug traffickers are being brought to justice, either on tax charges or on non-tax violations.

(4) The organized crime strike forces were supposed to bring together the best investigative and prosecutorial resources of the Federal Government. The idea was to mount a comprehensive attack on organized criminals, drug traffickers included. The concept, initiated in the early 1960's, has proven to be successful. One of the principal participants in the strike forces was the IRS. With their background in financial investigation, with their exceptional ability to trace the movement of funds, analyze ledgers and contrast lifestyle with income, IRS personnel were valuable and essential investigators in many successful prosecutions. Unfortunately, the situation has changed. Since enactment of the Tax Reform Act, IRS special agents may be assigned to strike forces but they cannot really participate. In some instances, they cannot even speak up. They cannot tell prosecutors and investigators what cases IRS is working on. They cannot help

to identify organized criminals. Several witnesses told of how IRS personnel attend strike force meetings, listen to what others have to say but must themselves remain silent, fearing that they might violate the Tax Reform Act's disclosure provisions. The Subcommittee finds this regrettable. Some of the most capable people have been removed from the Government's efforts to control organized crime. It is not surprising that some investigators and prosecutors resent IRS agents and find the Service's predicament to be causing morale problems in the law enforcement community.

(5) IRS witnesses consistently maintained they are devoting sufficient resources to high-level drug traffickers and organized crime cases. When challenged with respect to their efforts against drug traffickers, IRS witnesses told Senators that the IRS had obtained convictions against 22 high-level drug dealers in fiscal year 1979. The Subcommittee asked for more information on these convictions.

IRS's witnesses, including Commissioner Jerome Kurtz, explained that more information would be turned over later. But no such information was supplied to the Subcommittee. Instead, IRS first used the disclosure provisions of the Tax Reform Act as justification for not releasing information on the 22 convictions. The trials are a matter of public record. Releasing the names of the convicted persons to the Subcommittee would not invade the privacy of the tax violators. In the face of further requests by the Subcommittee for this information, Commissioner Kurtz said in a letter to the Chairman that several of the convictions were not high-level traffickers. Then Thomas J. Clancy, Director of the IRS Criminal Investigator Division, advised the Subcommittee by letter that the figures IRS initially submitted were not accurate. He said that some of the 22 convictions did not even involve narcotics and others on the list of 22 were "weak speaking solely in terms of the narcotics connection."

IRS officials, in sworn testimony, used the claim of 22 convictions to demonstrate that IRS is doing its share of major investigations. The Subcommittee finds that the 22 convictions claim was inaccurate and totally misleading. It should also be noted that even if the number 22 is accurate, it does not represent an especially good record of high level drug convictions.

Regarding organized crime investigations, when the General Accounting Office criticized IRS for reducing participation in the Justice Department strike forces by 50 percent, IRS responded again by submitting statistics. According to IRS, the Service was as active as ever in its own organized crime program but its cases were not processed through the strike forces. However, the Justice Department, which prosecutes all Federal crimes, has no record of the IRS organized crime cases. When asked by the Subcommittee to supply the names of the organized crime figures convicted as a result of this program, IRS witnesses said they were unable to provide this information. Again, the reason IRS claimed it was not submitting the names of convicted organized crime figures was the same they had submitted on drug dealers—that such information "may not be a matter of public record and therefore not properly disclosable."

IRS is aware that by withholding such information from the Subcommittee it forecloses comprehensive Congressional review of its special enforcement program dealing with organized crime figures

and high-level drug traffickers. Such a thorough review by the Subcommittee is essential to determine if IRS is properly allocating its resources and giving sufficient priority to drug and organized crime investigations. More importantly, without this information, the Subcommittee cannot make a complete evaluation of the effectiveness of the special enforcement program.

By its own admission, IRS does not maintain the most reliable or comprehensive statistics concerning its participation in organized crime and major narcotics cases. IRS can do a better job in collecting and collating such information—both for its own purposes and to assist the Congress in carrying out its oversight responsibility.

(6) To assure that the disclosure provisions of the Tax Reform Act are adhered to by IRS, the Congress included strong civil and criminal penalties in the statute. In civil proceedings, the agent may be sued. In criminal cases, the penalties are five years in prison or $5,000 fine, or both. Witnesses before the Subcommittee said these penalties have had a chilling effect upon the law enforcement community. IRS officials have been strict in their interpretation of the disclosure provisions. They do not wish to be sued, to pay a fine or to go to jail. As a result of these normal concerns, some regrettable actions have resulted—and the disclosure provisions have been blamed. In one case an informant was cooperating with the FBI on a criminal investigation. Two men identifying themselves as IRS special agents approach the informant's mother and asked for her son's whereabouts. The woman told them. Then she told the FBI what had happened. Concerned for the safety of its informant, the FBI asked IRS if the two men actually worked for IRS. IRS officials refused to say, citing the Tax Reform Act as justification for their silence. This kind of problem should not exist. Law enforcement work is difficult enough. Investigators should not be forbidden to use common sense and good judgment because of a law that is subject to various interpretations.

Accordingly, the Subcommittee finds that Federal investigators who in good faith believe what they are doing is in keeping with the terms of the Tax Reform Act's disclosure provisions should not be held liable if later what they did is found to be in violation of the statute. In criminal proceedings, it is essential that a good faith defense be written into the law. If the agent was working in good faith, thinking he was carrying out the disclosure provisions legally, he should be able to defend himself by pointing out he did what he did because he thought it was lawful and with no malicious intent. In addition, in cases of inadvertent disclosure, the Government should be civilly liable instead of the IRS employee.

(7) One of the negative effects resulting from the Watergate era was that many Government intelligence gathering projects were considered to be suspect. As one witness, former Assistant Treasury Secretary David R. MacDonald, put it, in some people's minds any intelligence file was assumed to be another "enemies list". He said the path of least resistance was to simply cut back all intelligence gathering programs and avoid the potential criticism. As MacDonald and other witnesses said, that was the path taken by the Internal Revenue Service. IRS intelligence programs, once considered essential to investigations of tax crimes, were reduced, publicly criticized by senior IRS

officials and decentralized. In the political environment of Watergate, such a decision may have been understandable, but it was not the proper course. For IRS to deliberately undermine its intelligence capability is to undermine its capability to investigate persons who do not pay taxes on illicitly earned income. The decision to undercut its intelligence system was a bad decision.

But what happened five years ago is of less importance than what is happening today. IRS still has a decentralized intelligence system which is inadequate to investigate the interstate and international business dealings of organized crime and major drug traffickers. Intelligence gathering is greatly handicapped by the decentralization. Intelligence developed in San Francisco, for example, may seem trivial in San Francisco, but coupled with more intelligence developed in Boston, may become important. But without a central file and without experienced personnel to evaluate it, the linkage of the San Francisco information to the Boston data will never be made. It is unfortunate that IRS policymakers have not come to the same conclusion on their own. IRS should have a centralized intelligence system for its Special Enforcement Program and should put in place administrative controls to protect against potential abuses.

(8) Most of the illicit drugs coming into the United States pass through Florida. Charles Kimball of Miami, an economist and real estate analyst, has made several valuable studies of the impact of the drug traffic on the Florida economy. Kimball found that drug money has had an inflationary impact. This is because drug traffickers realize big profits and wish to invest their money in legitimate enterprises. A favorite target is the real estate market. This has caused homes and buildings in the Miami and Ft. Lauderdale areas to increase in value faster than they would have without the infusion of drug money. Drug traffickers also invest in legitimate businesses. Because their money is plentiful and their primary concern is to cleanse or launder it, they are not particularly interested in a reasonable profit. They settle for less, considering it a small price to pay for laundering their cash. The negative result is that legitimate businessmen cannot compete. The infusion of drug money into the marketplace causes inflation, instability and uncertainty.

Kimball's studies are very useful, but he is only one man, working in a field ripe for further study. The Federal Government should be doing the kind of investigation Kimball is doing. It is estimated that the illicit drug traffic in the United States is a $40 billion to $60 billion business. It is having an effect not only upon the Florida economy but on the Nation's. The Government should learn more about how this money is invested, where it is invested, where it comes from, and what happens to the enterprises that serve to legitimize this money. The Government should also seek to establish how much of this drug money is lost to the U.S. Treasury because rarely are taxes paid on it. With more information, the Government can prepare to offset the negative impact of these illicit dollars. There is some urgency on this problem. Kimball testified that unless something is done to slow down the massive infusion of drug money into the Florida economy, the State will become dependent on the narcotics money.

Similarly, Diego C. Asencio, the American Ambassador to Colombia, told the Subcommittee what the drug trade has done to that South American nation. Colombia produces or ships most of the marijuana and cocaine that are smuggled into the United States. This thriving business has brought billions of dollars into the Colombian economy. But the result has not been a positive one for the country. It has only aggravated its economic problems. The relative few who engage in the drug exporting business flaunt their wealth, causing deep resentment among the poor in this underdeveloped nation. Inflation, already a serious problem, is made worse by the American dollars coming in illicitly. Attempts to control inflation by monetary policy are not working because of the huge drug economy. Government economists have no control over it. With so much money in circulation, the traditional values of the Colombian people are questioned. That much money can also find its way into politics and government, posing a temptation to public officials that some may not be able to resist, Asencio said. Moreover, he said, should the Colombia coffee crop suffer a setback, the nation could become dependent on the drug trade.

The Subcommittee does not wish to draw any parallels where only superficial similarities exist. The United States and Colombia are distinctly different nations and have sharply different problems. However, the dangers cited by Asencio—inflation, public corruption, economic dependence on the drug trade—are dangers that the U.S. Government should be studying.

In addition, the Government should make a special effort to assess the role of offshore entities in the economic activities of the bigtime drug traffickers. It is well known that organized criminals hide their illicit profits in and invest through offshore entities because of the privacy and tax benefits these entities offer. The Government should conduct a study as to whether it is in the nation's interest to give offshore entities tax benefits on profits made from American investments.

(9) Because of Florida's proximity to Colombia and certain Caribbean drug staging areas and because of the State's long coastline, it is the embarkation point for most of the marijuana and cocaine coming into the United States. The Federal Government has the special responsibility to assist this State as it tries to control the massive infusion of drugs. Federal authorities are obliged to help Florida in every way possible. There should be a Federal interagency task force set up whose mission would be to identify those areas where Federal assistance would be appropriate when requested by the State. A comprehensive program of assistance should then be initiated.

(10) One of the most effective ways of immobilizing major drug syndicates is for IRS to use its power to make taxpayer year terminations and jeopardy assessments. In simple terms what happens is that IRS investigators make the judgment that the owners of an enterprise or an entity have absolutely no intention of paying their taxes. Once that judgment is made, IRS arbitrarily declares the tax year to have ended. An assessment is made of how much money is owed, the tax bill is served, the property is seized.

IRS, feeling there had been abuses of the jeopardy and termination program, abandoned it during the Wategate era. The General Accounting Office in 1979 said there had been abuses in the past, but GAO recommended that IRS reactivate the program. The Subcommittee agrees. IRS should guard against abuses in the future. In the past, IRS policymakers, alarmed by Watergate, were too quick to give up on programs because mistakes were made. Mistakes will occur in every program. But the program is basically a sound one, abuses were infrequent and many major drug syndicates were immobilized because of it. No one would encourage IRS to get back in the termination and jeopardy business without sufficient preparation and planning and concern for people's rights. But the Subcommittee does encourage IRS to reactivate this valuable program.

(11) When the IRS completes a criminal tax investigation, the Service must make an important decision. Is the evidence of a crime of sufficient consequence to justify referring the investigative files to the Justice Department with the recommendation that the case be prosecuted? If the answer is yes, the case is referred to the Tax Division of Justice. From then on, the decision to prosecute is up to the Justice Department. But what happens when IRS decides that the case is not strong enough to prosecute? Prior to the enactment of the Tax Reform Act, IRS still referred the file to the Justice Department. Instead of sending it to the Tax Division with a recommendation to prosecute, the case was sent to the Criminal Division. It was hoped that the Criminal Division could make use of the files by incorporating them into another investigation. In that manner, the Justice Department, which has the Government's responsibility for prosecution of all crimes, could exercise a kind of check and balance on what cases are prosecuted. In addition, the Justice Department could try to combine this information with evidence from other agencies to determine if it could be used in another tax prosecution or in another non-tax case.

Ultimately, the decision as to the prosecutive potential of the investigation rested with the Justice Department. This is the way it should be. Now, however, with the Tax Reform Act's disclosure provisions, the IRS refuses to refer such cases to the Criminal Division. This is wrong. IRS ought to be able to go back to its pre-Tax Reform Act procedure of referring its criminal tax cases to the Criminal Division when it is the Service's judgment that the investigation will not constitute a strong prosecution. The legal experts at the Department should be able to get together with their counterparts at IRS and devise a procedure enabling this information to be exchanged in accordance with the restraints imposed by the disclosure provisions. If no satisfactory procedure can be arrived at, then the only hope is for prompt passage of legislation amending the Tax Reform Act. Until that amendment is passed, an effort should be made to work within the law and achieve the desired goal of having the Justice Department make the final say as to the merit of an investigative case file.

(12) The Subcommittee examined the Bank Secrecy Act. Signed into law in 1970 by President Nixon, the Bank Secrecy Act requires that banks report to the Government all cash deposits of $10,000 or

more; and that persons transferring $5,000 or more in cash or monetary instruments in or out of the United States file currency transaction reports with the Government. The Subcommittee has only one criticism. That criticism is that the Government has not utilized or enforced the law. Few officials of the Government even recognized what a valuable law enforcement tool the Bank Secrecy Act gave them. This lack of appreciation for the value of the statute was particularly true at the Treasury Department which was responsible for analyzing and distributing the currency transaction reports to appropriate law enforcement agencies.

The two overriding facts about all major drug syndicates are that they make large amounts of cash quickly and regularly—and they seek to quickly get that cash into some form of legitimate banking channels. Using the most obvious banking vehicle available to them, big drug syndicates sometimes simply deposit their cash in savings and checking accounts, usually under assumed names. They may also transfer their money to foreign accounts, either through the banking system itself through wire transfers and other devices or by travelling abroad and depositing the money directly into a foreign bank or investing it in an offshore entity. Technically, all of these methods but wire transfers are covered by the Bank Secrecy Act reporting requirements—if only the Government will use them.

Instead, the Government has made poor use of the statute and the documentation it generates. The currency reports of unusual cash deposits filed by banks, for example, reportedly drew dust and little else at Treasury from 1970 to 1979. Nine years went by and literally nothing was done with them. Treasury says it is now devoting proper attention to these reports. The Department should make appropriate use of the currency reports. In those few instances where the reports have been referred to the appropriate law enforcement agencies, they have proven to be of great value, just as the Congress intended. It would be most unfortunate if this tool was not utilized to the fullest extent possible.

In the course of its investigation, the Subcommittee developed information suggesting that the Bank Secrecy Act could be improved in three areas. It is the Subcommittee's belief that these proposed changes in the statute are intelligent and constructive responses to demonstrated needs and that they are deserving of review by the appropriate committees of Congress.

The first proposed amendment is based on the contention that more incentives are needed to encourage persons to come forward to report violations of the Bank Secrecy Act. It is felt that the statute will be enhanced when authorities can offer some inducement to private citizens to cooperate. The law could be changed, for instance, so that rewards payable from seized funds are given to informants whose information leads to the confiscation of large amounts of monies in violation of the Bank Secrecy Act.

The second proposed amendment has to do with the search and seizure authority of the U.S. Customs Service. Constitutionally, Customs has the authority to search travellers at the U.S. border without a search warrant for all contraband, from jewels to narcotics. However, the Bank Secrecy Act calls for a search warrant to be

issued for search of persons believed to be violating the reporting requirements of the statute. This proposal would eliminate the search warrant requirement and allow Customs its traditional and constitutional search authority.

The third proposed amendment redefines a technical but important distinction. As the law now reads, a violator of the reporting requirements is technically not breaking the law until he actually physically moves the unreported cash outside the United States. Unfortunately, once he is outside the United States, Federal jurisdiction no longer holds. This proposal would redefine the violation as occurring when the would-be violator attempts to avoid the reporting requirements. If, for example, a traveller seeks to board a foreign-bound airplane at an American airport while carrying $50,000 in unreported cash, he would at that point be in technical violation of the law and liable for apprehension.

(13) The Government should do more to urge judges to impose more realistic bails in narcotics cases. A 1977 study by DEA showed that 71 percent of DEA's most serious defendants were released on bails of $10,000 or less. More than half of these defendants were free on bond for seven months to a year. There were wide discrepancies in average bail amounts for the same drug offense. Nearly half of the charged traffickers were recidivists or foreigners in this country illegally.

Judges set bonds and they should be urged to be more realistic in setting the bail level. In addition, Federal prosecutors should share the burden. They must take the time to inform the court of the extent of the alleged trafficker's financial resources. For a big drug dealer doing a business of several million dollars, a $10,000 bail, or even a $100,000 bail, will serve as insufficient reason for showing up for trial. If the Government has a strong case against him, the alleged drug trafficker may decide to forfeit bail and flee. The loss of the money is a small price to pay for circumventing a prison sentence.

There is evidence that all too often accused drug offenders get right back into trafficking upon their release on bail. DEA Administrator Peter Bensinger told the Subcommittee that the seasoned, successful drug trafficker, confronted by an uninformed or lenient judge, may obtain his freedom by meeting a small bail and be back in his high finance trafficking lifestyle "without missing a beat." This is just the kind of abuse of the bail system that prosecutors and judges should seek to avoid.

(14) Similarly, sentencing is often too light when accused drug traffickers are found guilty. The Subcommittee heard one official complain that in his State—Florida, where tougher sentencing policies are in force—drug suspects begged authorities to try them in Federal court because there they felt they would be dealt with more leniently. As for sentencing policies, the Controlled Substances Act of 1970 provides for a maximum penalty of 15 years' imprisonment per count for first offenses, and 30 years' imprisonment per count for second offenses. Judges rarely give sentences that tough, however. A DEA study showed that of 919 defendants convicted of serious drug offenses in 1976, 24 percent received probation. Sixty-one percent received sentences of three years or less. And 81 percent received sentences of six years or less. Actual time served averaged 43.2 percent of the sentence imposed.

Looking at these and other incarceration figures, the General Accounting Office concluded that the trend toward probation and short sentences for serious drug offenses "continues to negate the deterrent effect of prosecution." The Subcommittee agrees with GAO on this point and finds that there should be stiffer sentencing for serious drug offenders.

(15) The crime of drug trafficking is much too serious an offense for the Department of Justice to continue its policy of "dual prosecution" in narcotics cases without increased coordination with IRS. The dual prosecution policy at Justice says, in general, that a person will not be tried for two similar and related but separate crimes stemming from the same series of actions. In effect, the policy requires that all offenses arising from a single transaction, such as drug trafficking and tax evasion on the ensuing profits, will be tried together—or, in the absence of trying them together, the first prosecution will be sufficient. For example, a major narcotics trafficker, the subject of a comprehensive tax case, might also have been charged with a misdemeanor violation of simple possession of a small amount of drugs. While the IRS works up the far more serious tax case, the man is tried on the misdemeanor. He is convicted and given a light sentence. Meanwhile, the IRS completes its tax evasion investigation and refers it to the Tax Division of the Justice Department for prosecution. Justice declines on the tax evasion charges because of the dual prosecution policy.

The Subcommittee finds that this policy subverts the notion of even-handed justice. It is inefficient and wasteful of Government resources. And it gives major drug dealers an advantage they do not deserve. Criminals should be charged with both crimes when both crimes are serious. When one crime is less serious than the other, as in the above example, the accused offender should not be relieved of responsibility for the more serious offense just because he has been convicted of the other.

Not all the blame for this lack of coordination between Justice and IRS rests with the dual prosecution policy. Because of the disclosure provisions of the Tax Reform Act, and because of the IRS attitude that makes communication even more difficult than the statute requires, prosecutors are not talking to revenue collectors. Prosecutors may not even know which tax cases are being developed at IRS. In certain instances, there may be some merit to a policy that encourages the trying of offenders for one crime rather than two. But common sense would require that if that is so, the more serious of the offenses should be tried. The Subcommittee finds that the barriers to communication that exist between Justice and IRS make common sense judgments difficult to arrive at. Prosecutors may ask, "If we don't know about the big tax case being developed, why not go ahead with the smaller drug case we do know about?" It is disturbing to learn that so little communication goes on between IRS and Justice, two of the most important components of the executive branch. This is all the more reason to amend the Tax Reform Act—and, all the more reason for IRS to change its attitude and start cooperating more.

(16) During the hearings, several witnesses said the United States armed services could assist civilian law enforcement agencies in combatting the drug traffic. This is particularly true regarding the use of

electronic detection equipment such as radar. Often military installations are better equipped with sophisticated equipment to trace the movements of high performance aircraft and fast moving ocean vessels as they ship drugs along, across or near the border. Witnesses testified that some of this military equipment is being used by civilian authorities. But, because of its interpretation of the doctrine of Posse Comitatus, the military has not allowed its personnel to operate this equipment and has been reluctant to provide civilian authorities drug information which it gains through routine defense-related activities.

One witness, Florida Attorney General Jim Smith, said he does not favor use of military resources in civil law enforcement except in "the most dire circumstances." But, he said, so serious is the drug problem that such extreme circumstances exist now. The Subcommittee finds that both Congress and the Executive Branch should take a serious look at the Posse Comitatus doctrine and its effect on narcotics enforcement. The Executive Branch has the power to remove many administrative obstacles to the cooperation between drug enforcement officials and the military, and it could improve the current situation considerably without any legislative action. The Subcommittee recognizes that any substantial change in the laws governing military involvement in civilian law enforcement must be treated as a step of utmost gravity in a democratic society. Nevertheless, the Congress also should make a thorough examination of the problems posed by the Posse Comitatus doctrine, and carefully consider legislative proposals aimed at redressing these problems.

VIII. RECOMMENDATIONS

(1) The Subcommittee recommends that the Tax Reform Act's disclosure provisions be amended so that appropriate law enforcement agencies have more ready access to tax information and other evidence for use in legitimate investigations and prosecutions of non-tax crimes. The proposed legislation should also amend the summons provision of the Tax Reform Act so that the taxpayer would be notified that his recordkeeper has been issued a summons; however, instead of being able to invoke a stay automatically, the taxpayer would have to go to court and present a legal basis for quashing the summons. If the taxpayer fails to present a convincing argument, the summons would be affirmed and his recordkeeper would be compelled to turn over his documents to IRS.

(2) The Internal Revenue Service has not lived up to its responsibility to try to collect taxes from organized criminals and narcotics traffickers. The IRS also has not met its responsibility to cooperate and to work closely with other law enforcement agencies which are trying to build conspiracy and financial investigation cases against organized criminals and drug traffickers. The IRS has been unsuccessful in these matters for two reasons. The first is the disclosure provisions of the Tax Reform Act. The second is an attitude at IRS that encourages enforcement of tax collection regarding taxpayers who earn their income honestly but discourages the pursuit of persons who earn their livelihood illegally and pay little or no taxes on this income. As noted in the first recommendation, the Subcommittee proposes that the Tax Reform Act be amended so that needless restrictions on the use of IRS personnel and information can be removed. The Subcommittee also recommends that IRS accept its responsibility to collect taxes from all taxpayers, including drug traffickers and organized criminals. That is the first step—to make an affirmative commitment to the goal of enforcing the tax laws equitably. It is not a fair tax system that only taxes people who earn their incomes honestly. And it will not be a fair system until organized criminals and drug traffickers are punished for not paying their taxes as well.

Equipped with modern, computerized technology, IRS has devised sophisticated detection systems for flagging anomalies in tax returns. The discriminate function formula, perfected to a high degree, is a solid, reliable defense against the taxpayer whose deductions are out of line or who is trying to conceal income. Having such a system in place is commendable. The average, law-abiding taxpayer should be encouraged to comply with the Internal Revenue Code. If he does not comply, he should be caught, and IRS has a system for catching him. It is the Subcommittee's recommendation that the IRS develop an equally effective system for detecting persons who do not file returns at all, persons whose work is illegal and who also ought to be made to pay their taxes.

(3) Justice Department officials told the Subcommittee that the Department would like to work out a national strategy with IRS on pursuing organized criminals and drug traffickers. The Subcommittee recommends that such a strategy be developed. IRS also should map out its own national strategy and draft its own set of priorities and goals in organized crime and drug investigations. Its leadership should immediately move to do away with the confusion and misconceptions resulting from its strict interpretation of the Tax Reform Act by meeting with IRS agents in the field and instructing them on what can and cannot be done under the Act.

Furthermore, IRS should conduct an accurate investigation of the amounts of legal and illegal unreported income to enable the Service to allocate resources properly.

(4) The Subcommittee recommends that IRS be reorganized. Responsibility for the criminal investigation and intelligence gathering functions should be removed from the Assistant Commissioner for Compliance. It is recommended that a new Assistant Commissioner position be created. It should be the sole duty of this Assistant Commissioner to oversee the criminal investigation and intelligence gathering activities of IRS. This official should be on a par with other Assistant Commissioners and should report directly to the Commissioner of Internal Revenue. This reorganization will provide a chain of command in the criminal division reaching the Commissioner so that he can obtain adequate information in criminal as well as civil matters.

(5) The IRS is requested to submit within 60 days of the issuance of this report a statement as to what action it will take in response to each of this report's findings, conclusions and recommendations for corrective action.

The following Senators, who were Members of the Permanent Subcommittee on Investigations at the time of the hearings, have approved this report:

Sam Nunn
Henry M. Jackson
Thomas F. Eagleton
Lawton Chiles
John Glenn
Jim Sasser
Charles H. Percy
Jacob K. Javits [1]
William V. Roth, Jr.
William S. Cohen [2]

The Members of the Committee on Governmental Affairs, except those who were members of the Senate Permanent Subcommittee on Investigations at the time of the hearings, did not sit in on the hearings on which the above report was prepared. Under these circumstances, they have taken no part in the preparation and submission of the report except to authorize its filing as a report made by the subcommittee.

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[1] See additional views of Senator Javits on page 133.
[2] See additional views of Senator Cohen on page 135.

ADDITIONAL VIEWS OF MR. JAVITS

The Subcommittee is to be commended for putting together a comprehensive study of law enforcement problems in the narcotics enforcement area. Drug traffickers are among the most vicious criminal elements in our society, and every effort must be made to uproot them. Testimony at the Subcommittee hearings has convinced me that we are not making the best possible use of law enforcement agencies in this area, and that better coordination and more resources are necessary.

I am concerned, however, that the Subcommittee majority, in their zeal to combat drug trafficking, has made some suggestions that may be unwise in terms of civil liberties. I refer particularly to changes suggested to the Tax Reform Act regarding disclosure of taxpayer information.

The IRS is a unique agency in the Federal Government. Because of the importance of its revenue collecting functions, it was granted powers far broader than those granted other law enforcement agencies. For example, as the ACLU recently pointed out in testimony before the Senate Finance Committee, opposing changes in the Tax Reform Act, "The IRS may, without a subpoena or a warrant, or any showing of probable cause, require an individual to divulge information." That sort of power would be anathema to our system of government in other settings.

Further, unlike any other Federal law enforcement agency, the IRS has detailed records on nearly every citizen, including the vast majority of citizens who have never violated any law. These records go far beyond the information provided on tax returns, and may include information on many of the most intimate details of a person's life.

Not surprisingly, the existence of this large pool of confidential data has proved to be very attractive to law enforcement personnel. There is no question that its ready availability makes the job of law enforcement investigations an easier one. Prior to 1976, there were no standards governing the dissemination of this information to law enforcement and other government personnel. This lead to a number of abuses, including attempts by the White House during the Watergate years to use tax information against ideological opponents, and those on the famous "enemies" list.

The Tax Reform Act of 1976 was an attempt to rectify that situation. Underlying its passage was a recognition that:

(1) The IRS's primary mission is the collection of revenue in a fair and equitable manner.

(2) In order to carry out this mission, the IRS is permitted to compel the disclosure of information the individual would not otherwise divulge. This extraordinary intrusion into personal privacy is justifiable, but it is also the reason for extraordinary precautions against nonconsensual dissemination of these data.

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(3) The effectiveness of our tax system depends, in large measure, on voluntary taxpayer cooperation. The incentive to cooperate may be greatly lessened if taxpayers fear that their tax returns and supporting data will be generally available.

These general principles still hold true.

I agree with Senator Nunn that we must strike the proper balance between the needs of the law enforcement community and the taxpayer's rights of privacy. In my view, that balance requires a recognition that Congress conferred the extraordinary power to compel disclosure on the IRS because of the agency's unique role in the collection of revenue and that Congress never intended that the IRS function primarily as a general criminal law enforcement agency. I do not believe the American people would support use of the IRS as an investigatory vehicle for other law enforcement agencies which were not given such broad power.

Experience under the Tax Reform Act, and testimony before the Subcommittee indicates that some changes in the Act may be warranted. But any attempt to balance privacy and law enforcement interests must in my opinion, retain the following elements.

(1) Access by a Federal agency to information supplied to IRS by a taxpayer or his representative must be subject to court review. Only a court has the necessary objectivity to determine whether society's interest in access to confidential information in a given case outweighs the taxpayer's expectation of privacy for the information he gives the IRS.

(2) The standard for obtaining a court order should include a finding, as does current law, that there is a reasonable cause to believe that a specific crime has been committed. To lower that standard could open up tax records to "fishing expeditions".

(3) Disclosure to law enforcement agencies should be limited to Federal criminal law enforcement investigations, and there should be strict controls on redisclosure of information released to those agencies.

(4) The Subcommittee record argues for a change in the summons provisions of the Tax Reform Act, which permits a taxpayer to stay a summons merely by writing a letter. However, it must be recognized that the IRS has resources that far outweigh those of the individual taxpayer. Any shift of the burden in a stay proceeding from the IRS to the taxpayer must be accompanied by protections at least as great as those contained in the Right to Financial Privacy Act.

ADDITIONAL VIEWS OF MR. COHEN

I would like at this time to commend the Subcommittee leadership for presenting in this report a most complete review of the problems involved in the prosecution of narcotics traffickers; some of these problems relate not to the increasing deviousness and ingenuity of drug dealers, itself a significant problem, but to a law passed by the Congress itself, the Tax Reform Act of 1976.

In its findings, the Subcommittee notes that "the American people have no patience for excuses and explanations as to why Federal efforts cannot substantially reduce the drug trade." The statement is most ironic, since, in its report, the Subcommittee has patiently, and in excruciating detail, laid out the reasons why, under current laws and policies, more drug traffickers are not investigated, apprehended, and effectively prosecuted. In so doing, the Subcommittee fulfills an important obligation to the Congress and to the public.

While long on description of the current problem, the report is short on recommendations, especially in regard to specific ways to change the Tax Reform Act's provisions regarding the disclosure of information in the possession of the Internal Revenue Service to law enforcement agencies.

This is appropriate as well. While it is clear that problems exist in the current statute, much work remains to be done before specific statutory changes should be made. Last March, I, along with several of the other Members of the Subcommittee, co-sponsored legislation that would make changes in the Tax Reform Act's disclosure sections. At the time I announced my support for these proposals, however, I noted my concern as to whether certain of the proposed new definitions of IRS information could, as written, "withstand attempts of overzealous law enforcement officials to circumvent the requirement for court review of requests for tax returns." In light of this concern, I fully expected at that time that Congress's consideration of the proposed changes would be—and should be—cautious and deliberative.

I continue to believe so. Recently, a report by the General Accounting Office echoed several of my concerns with ambiguities that remain in the proposals, the thrust of which I, and the GAO, support. Continued and persistent work will be necessary to perfect the proposed changes in the Tax Reform Act.

In spite of the frustration we all feel at seeing narcotics trafficking erode our economy and our society as a whole, we must recognize that statutory changes generated by the need to address this Nation's serious drug problems will of necessity apply generally, and that the protection of privacy interests could be jeopardized by imprecise legislative language, just as the public safety has been jeopardized by ambiguities in the original disclosure provisions.

It is with these additional views that I endorse this report of the Permanent Subcommittee on Investigations.

APPENDIX

§ 6103. Confidentiality and disclosure of returns and return information

(i) Disclosure to Federal officers or employees for administration of Federal laws not relating to tax administration.—

(1) Nontax criminal investigation.—

(A) Information from taxpayer.—A return or taxpayer return information shall, pursuant to, and upon the grant of, an ex parte order by a Federal district court judge as provided by this paragraph, be open, but only to the extent necessary as provided in such order, to officers and employees of a Federal agency personally and directly engaged in and solely for their use in, preparation for any administrative or judicial proceeding (or investigation which may result in such a proceeding) pertaining to the enforcement of a specifically designated Federal criminal statute (not involving tax administration) to which the United States or such agency is or may be a party.

(B) Application for order.—The head of any Federal agency described in subparagraph (A) or, in the case of the Department of Justice, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General, may authorize an application to a Federal district court judge for the order referred to in subparagraph (A). Upon such application, such judge may grant such order if he determines on the basis of the facts submitted by the applicant that—

(i) there is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed;

(ii) there is reasonable cause to believe that such return or return information is probative evidence of a matter in issue related to the commission of such criminal act; and

(iii) the information sought to be disclosed cannot reasonably be obtained from any other source, unless it is determined that, notwithstanding the reasonable availability of the information from another source, the return or return information sought constitutes the most probative evidence of a matter in issue relating to the commission of such criminal act.

However, the Secretary shall not disclose any return or return information under this paragraph if he determines and certifies to the court that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

(2) Return information other than taxpayer return information.—Upon written request from the head of a Federal agency described in paragraph (1) (A), or in the case of the Department of Justice, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General, the Secretary shall disclose return information (other than taxpayer return information) to officers and employees of such agency personally and directly engaged in, and solely for their use in, preparation for any administrative or judicial proceeding (or investigation which may result in such a proceeding) described in paragraph (1) (A). Such request shall set forth—

(A) the name and address of the taxpayer with respect to whom such return information relates;

(B) the taxable period or periods to which the return information relates;

(C) the statutory authority under which the proceeding or investigation is being conducted; and

(D) the specific reason or reasons why such disclosure is or may be material to the proceeding or investigation.

However, the Secretary shall not disclose any return or return information under this paragraph if he determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation. For purposes of this paragraph, the name and address of the taxpayer shall not be treated as taxpayer return information.

(3) Disclosure of return information concerning possible criminal activities.—The Secretary may disclose in writing return information, other than taxpayer return information, which may constitute evidence of a violation of Federal criminal laws to the extent necessary to apprise the head of the appropriate Federal agency charged with the responsibility for enforcing such laws. For purposes of the preceding sentence, the name and address of the taxpayer shall not be treated as taxpayer return information if there is return information (other than taxpayer return information) which may constitute evidence of a violation of Federal criminal laws.

§ 7609. Special procedures for third-party summonses

(a) Notice.—

(1) In general.—If—

(A) any summons described in subsection (c) is served on any person who is a third-party recordkeeper, and

(B) the summons requires the production of any portion of records made or kept of the business transactions or affairs of any person (other than the person summoned) who is

identified in the description of the records contained in the summons,

then notice of the summons shall be given to any person so identified within 3 days of the day on which such service is made, but no later than the 14th day before the day fixed in the summons as the day upon which such records are to be examined. Such notice shall be accompanied by a copy of the summons which has been served and shall contain directions for staying compliance with the summons under subsection (b)(2).

(2) Sufficiency of notice.—Such notice shall be sufficient if, on or before such third day, such notice is served in the manner provided in section 7603 (relating to service of summons) upon the person entitled to notice, or is mailed by certified or registered mail to the last known address of such person, or, in the absence of a last known address, is left with the person summoned. If such notice is mailed, it shall be sufficient if mailed to the last known address of the person entitled to notice or, in the case of notice to the Secretary under section 6903 of the existence of a fiduciary relationship, to the last known address of the fiduciary of such person, even if such person or fiduciary is then deceased, under a legal disability, or no longer in existence.

(3) Third-party recordkeeper defined.—For purposes of this subsection, the term "third-party recordkeeper" means—

(A) any mutual savings bank, cooperative bank, domestic building and loan association, or other savings institution chartered and supervised as a savings and loan or similar association under Federal or State law, any bank (as defined in section 581), or any credit union (within the meaning of section 501(c)(14)(A));

(B) any consumer reporting agency (as defined under section 603(d) of the Fair Credit Reporting Act (15 U.S.C. 1681a(f)));

(C) any person extending credit through the use of credit cards or similar devices;

(D) any broker (as defined in section 3(a)(4) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(4)));

(E) any attorney; and

(F) any accountant.

(4) Exceptions.—Paragraph (1) shall not apply to any summons—

(A) served on the person with respect to whose liability the summons is issued, or any officer or employee of such person,

(B) to determine whether or not records of the business transactions or affairs of an identified person have been made or kept, or

(C) described in subsection (f).

(5) Nature of summons.—Any summons to which this subsection applied (and any summons in aid of collection described in subsection (c)(2)(B) shall identify the taxpayer to whom the summons relates or the other person to whom the records pertain and shall provide such other information as will enable

the person summoned to locate the records required under the summons.

(b) Right to intervene; right to stay compliance.—

(1) Intervention.—Notwithstanding any other law or rule of law, any person who is entitled to notice of a summons under subsection (a) shall have the right to intervene in any proceeding with respect to the enforcement of such summons under section 7604.

(2) Right to stay compliance.—Notwithstanding any other law or rule of law, any person who is entitled to notice of a summons under subsection (a) shall have the right to stay compliance with the summons if, not later than the 14th day after the day such notice is given in the manner provided in subsection (a)(2)—

(A) notice in writing is given to the person summoned not to comply with the summons, and

(B) a copy of such notice not to comply with the summons is mailed by registered or certified mail to such person and to such office as the Secretary may direct in the notice referred to in subsection (a)(1).

(c) Summons to which section applies.—

(1) In general.—Except as provided in paragraph (2), a summons is described in this subsection if it is issued under paragraph (2) of section 7602 or under section 6420(e)(2), 6421(f)(2), 6424(d)(2), or 6427(g)(2) and requires the production of records.

(2) Exceptions.—A summons shall not be treated as described in this subsection if—

(A) it is solely to determine the identity of any person having a numbered account (or similar arrangement) with a bank or other institution described in subsection (a)(3)(A), or

(B) it is in aid of the collection of—

(i) the liability of any person against whom an assessment has been made or judgment rendered, or

(ii) the liability at law or in equity of any transferee or fiduciary of any person referred to in clause (i).

(3) Records; certain related testimony.—For purposes of this section—

(A) the term "records" includes books, papers, or other data, and

(B) a summons requiring the giving of testimony relating to records shall be treated as a summons requiring the production of such records.

(d) Restriction on examination of records.—No examination of any records required to be produced under a summons as to which notice is required under subsection (a) may be made—

(1) before the expiration of the 14-day period allowed for the notice not to comply under subsection (b)(2), or

(2) when the requirements of subsection (b)(2) have been met, except in accordance with an order issued by a court of competent jurisdiction authorizing examination of such records or with the consent of the person staying compliance.

(e) Suspension of statute of limitations.—If any person takes any action as provided in subsection (b) and such person is the person with respect to whose liability the summons is issued (or is the agent, nominee, or other person acting under the direction or control of such person), then the running of any period of limitations under section 6501 (relating to the assessment and collection of tax) or under section 6531 (relating to criminal prosecutions) with respect to such person shall be suspended for the period during which a proceeding, and appeals therein, with respect to the enforcement of such summons is pending.

(f) Additional requirement in the case of a John Doe summons.—Any summons described in subsection (c) which does not identify the person with respect to whose liability the summons is issued may be served only after a court proceeding in which the Secretary establishes that—

(1) the summons relates to the investigation of a particular person or ascertainable group or class of persons,

(2) there is a reasonable basis for believing that such person or group or class of persons may fail or may have failed to comply with any provision of any internal revenue law, and

(3) the information sought to be obtained from the examination of the records (and the identity of the person or persons with respect to whose liability the summons is issued) is not readily available from other sources.

(g) Special exception for certain summonses.—In the case of any summons described in subsection (c), the provisions of subsections (a) (1) and (b) shall not apply if, upon petition by the Secretary, the court determines, on the basis of the facts and circumstances alleged, that there is reasonable cause to believe the giving of notice may lead to attempts to conceal, destroy, or alter records relevant to the examination, to prevent the communication of information from other persons through intimidation, bribery, or collusion, or to flee to avoid prosecution, testifying, or production of records.

(h) Jurisdiction of district court.—

(1) The United States district court for the district within which the person to be summoned resides or is found shall have jurisdiction to hear and determine proceedings brought under subsections (f) and (g). The determination required to be made under subsections (f) and (g) shall be made ex parte and shall be made solely upon the petition and supporting affidavits. An order denying the petition shall be deemed a final order which may be appealed.

(2) Except as to cases the court considers of greater importance, a proceeding brought for the enforcement of any summons, or a proceeding under this section, and appeals, take precedence on the docket over all cases and shall be assigned for hearing and decided at the earliest practicable date.

Added Pub.L. 94–455, Title XII, § 1205(a), Oct. 4, 1976, 90 Stat. 1699, and amended Pub.L. 95–599, Title V, § 505(c)(6), Nov. 6, 1978, 92

Stat. 2760; Pub.L. 95–600, Title VII, § 703(*l*)(4), Nov. 6, 1978, 92 Stat. 2943.

Codification. Section 1205(a) of Pub.L. 94–455 redesignated former section 7609, relating to cross references as 7611 of this title.

1978 Amendment. Subsec. (c)(1). Pub.L. 95–600 substituted "6427(f)(2)" for "6427(e)(2)".

DEPARTMENT OF THE TREASURY,
INTERNAL REVNUE SERVICE,
Washington, D.C., March 28, 1980.

Hon. SAM NUNN,
Chairman, Senate Permanent Subcommittee on Investigations, Committee on Governmental Affairs, United States Senate, Washington, D.C.

DEAR MR. CHAIRMAN: As you know, during the hearing on December 14, 1979, concerning law enforcement impediments with respect to narcotics profits, we agreed to furnish your Committee a list of names of those twenty-two persons convicted in Fiscal Year 1979 of tax violations who were included in our High-Level Drug Leaders Tax Enforcement Project. As explained in our meeting of March 19, 1980, further concerns about the legality under IRC 6103 of releasing names along with the characterization of those persons as drug dealers precludes our release of that particular listing. We are concerned because the characterization of persons as drug dealers may be based on non-public information subject to IRC 6103 non-disclosure requirements. As promised at our meeting, though, enclosed is a listing of all of our Fiscal Year 1979 convictions.

Our division, as with the IRS generally, is a highly decentralized organization. Cases are selected for investigation by our field people; and information regarding those cases is entered by them into our management information system. The placement of a case into our High-Level Drug Leaders Tax Enforcement Project is a determination that may be made when a case is initiated or when information is later developed which warrants such classification. Those judgments are made by special agents, their supervisors, and division-level managers in our district offices throughout the country.

While we do not now mantain centralized case files in our divisions' headquarters office, we did review those old files that existed, and we reviewed the files of our Chief Counsel's office on the twenty-two convictions referred to at the public hearings. That review permitted my staff to make some judgments about the narcotics involvement of the twenty-two persons convicted of tax-related crimes after being included in the project. As I indicated at our March 19 meeting, three of the twenty-two cases should not have been included in the project because the field investigation failed to develop information establishing narcotics involvement. On the other hand, that review convinced me that ten to twelve of those convictions involved high-level drug leader cases, while the remainder involved persons whose narcotics activity had been established but not necessarily at very high levels.

After our meeting, I asked members of my staff to review the available materials again and seek, where necessary, additional information to assist in judging whether the cases in the project were appropriately included. As a result of this review, senior members of my staff have concluded that our field people were generally justified in their desig-

nations of individuals as project targets based on the information available to them at the time the cases were initiated—whether initiated under our earlier narcotics project or the subsequent high-level project. In some cases our investigative work did not prove the narcotics allegations or even develop specific evidence of narcotics trafficking during the years included in our investigations. However, this is an expected result when cases for tax purposes are developed by indirect methods of proof (i.e., net worth, expenditures, and bank deposits).

In our review of the twenty-two convictions, we found that nine cases were developed under our former narcotics project and were completed investigations which were in the review process prior to July 1976, when our new high-level project began. All three of those that I believe inappropriate for inclusion in our high-level project were among those early cases, as were five additional cases in which the narcotics trafficking evidence or data was weak. Only one of those nine early cases concerned an individual whose narcotics connection was considered strong. None of those nine persons were classified as DEA–I by the Drug Enforcement Administration (DEA); but since these are older cases, they may have preceded the DEA's classification system. Although our records are not complete on this point, we have found documentation on five of those early cases which indicates that they were evaluated and approved for inclusion in our former project by the Target Selection Committee. In summary, based on this second review, we believe that those three cases which I questioned earlier should not have been included in the project. While the evidence on some of the other cases is weak speaking solely in terms of the narcotics connection, we believe our field people were justified in including them in the project.

We are quite concerned that our resources in this area be applied to the investigation of significant narcotics traffickers and financiers. We are conducting a review of all cases presently in our case inventory and those in the review pipeline. If the cases do not meet our high-level requirements, they will be removed from this project. Since we have established resource application goals for projects activity, these adjustments should result in additional efforts to identify and investigate high-level subjects.

If you would like any additional information or explanation, I would be pleased to furnish it.

Sincerely,

THOMAS J. CLANCY,
Director, Criminal Investigation Division.

Enclosure.

U.S. SENATE,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
SENATE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS,
Washington, D.C., March 31, 1980.

Mr. THOMAS J. CLANCY,
Director, Criminal Investigation Division, Internal Revenue Service, Department of the Treasury, Washington, D.C.

DEAR TOM: I am responding on behalf of Senator Nunn relative to your letter of March 28, 1980 concerning IRS convictions of narcotics dealers.

As you know, the Permanent Subcommittee on Investigations requested IRS to furnish it with the names of those persons convicted of IRS charges in the IRS programs dealing with narcotics and organized crime. The Subcommittee requested this identification for the period 1971 to the present. At our December, 1979 hearing, Commissioner Kurtz agreed to furnish these names. In addition, there were numerous references by IRS to 22 convictions of high-level narcotics traffickers IRS had obtained in 1979.

In my opinion, nothing in 26 U.S.C. 6103 prevents or prohibits IRS from disclosing names of persons convicted of IRS violations in any particular program. The Subcommittee has not requested any information concerning the classification of individual taxpayers. We only seek the names of persons convicted under each program. This, of course, is public record information.

While we appreciate the computer listing of all IRS convictions for 1979, I feel that this list is not adequate for two reasons:

(1) The list is extensive and it will be extremely difficult for other Executive Branch agencies to check out each name on the list for narcotics or organized crime backgrounds. This is especially true when another Government agency; namely, IRS already has categorized the names and the Permanent Subcommittee on Investigations merely wants to check the names in these categories. I feel that this is a project which will take a significant amount of time when no logical reason exists for such a procedure.

(2) The computerized list for 1979 does not address the SEP results in terms of convictions since 1971.

Apparently, even from your own review, there is a question as to the classification of taxpayers placed in SEP groups, such as narcotics and organized crime. As part of our oversight responsibility, it is essential that the Permanent Subcommittee on Investigations determine the allocation of IRS resources and the results of that allocation in SEP cases. As you know, the Subcommittee's December hearing, as it related to IRS issues, dealt with the impediments resulting from the Tax Reform Act and the alleged de-emphasis by the IRS with respect to narcotics and organized crime cases.

Therefore, I would request from IRS legal counsel a written opinion concerning any specific prohibition in 26 U.S.C. 6103 which prevents IRS from supplying us with the appropriate information.

I do not believe that a logical and rational interpretation of 26 U.S.C. 6103 leads to the conclusion that the names of persons convicted in public forums, in particular IRS programs, should be withheld from the Subcommittee.

Thank you for your assistance.

Sincerely,

MARTY STEINBERG,
Chief Counsel.

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