109024

REPORT BY THE

Comptroller General

OF THE UNITED STATES

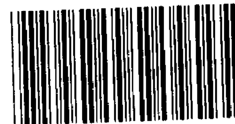
9722

Better Use Of Currency And Foreign Account Reports By Treasury And IRS Needed For Law Enforcement Purposes

Currency reports, foreign trust returns, and foreign bank account reports have not been as useful to the Treasury Department and the Internal Revenue Service, in carrying out their investigative responsibilities, as the Congress might have expected when it established the reporting requirements.

- Currency reports might be more useful if their processing were centralized in the Treasury's law enforcement data system and the Internal Revenue Service made more effective use of that system.
- Foreign trust returns might be more valuable if the Internal Revenue Service established better criteria for ensuring compliance with filing requirements and for evaluating reported information.
- Treasury needs to follow up its efforts to improve the value of foreign bank account data.

GAO conducted this review at the request of the Chairman, Subcommittee on Oversight, House Committee on Ways and Means.



084868

GGD-79-24

APRIL 6, 1979

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

AGC 00038 DTRS
AGC 00004 IRS

B-137762

The Honorable Sam M. Gibbons
Chairman, Subcommittee on Oversight
Committee on Ways and Means
House of Representatives HSE04102

Dear Mr. Chairman:

This report, in response to your request, points out that certain currency and foreign account reports have not been as useful to Treasury and the Internal Revenue Service as the Congress might have expected when it established the reporting requirements.

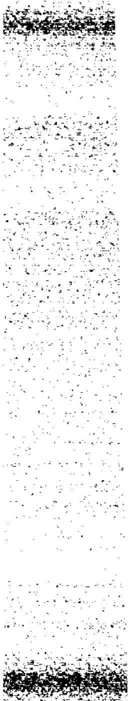
The report contains recommendations to the Secretary of the Treasury and the Commissioner of Internal Revenue for improving the usefulness of the various reports. Treasury and the Internal Revenue Service generally agreed with our recommendations.

As arranged with your Office, we are sending this report to the Chairman of the Subcommittee on Commerce, Consumer, and Monetary Affairs, House Committee on Government Operations, because of the Subcommittee's continuing interest in and oversight reponsibility for certain matters discussed in the report. We are also sending copies to other congressional committees, individual members of the Congress, and other interested parties.

HSE01501

Sincerely yours,

Comptroller General
of the United States



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

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

DIGEST

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

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

GAO reviewed IRS' use of

--currency transaction reports;

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

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

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

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

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

Tear Sheet. Upon removal, the report cover date should be noted hereon.

CURRENCY REPORTS: ACTIONS WHICH MIGHT IMPROVE THEIR VALUE

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

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

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

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

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

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

FOREIGN TRUST RETURNS: BETTER HANDLING NEEDED

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

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

FOREIGN BANK ACCOUNT REPORTS: SOME IMPROVEMENTS MADE

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

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

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

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

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

RECOMMENDATIONS

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

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

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

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

The Secretary should also:

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

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

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

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

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

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

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

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

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

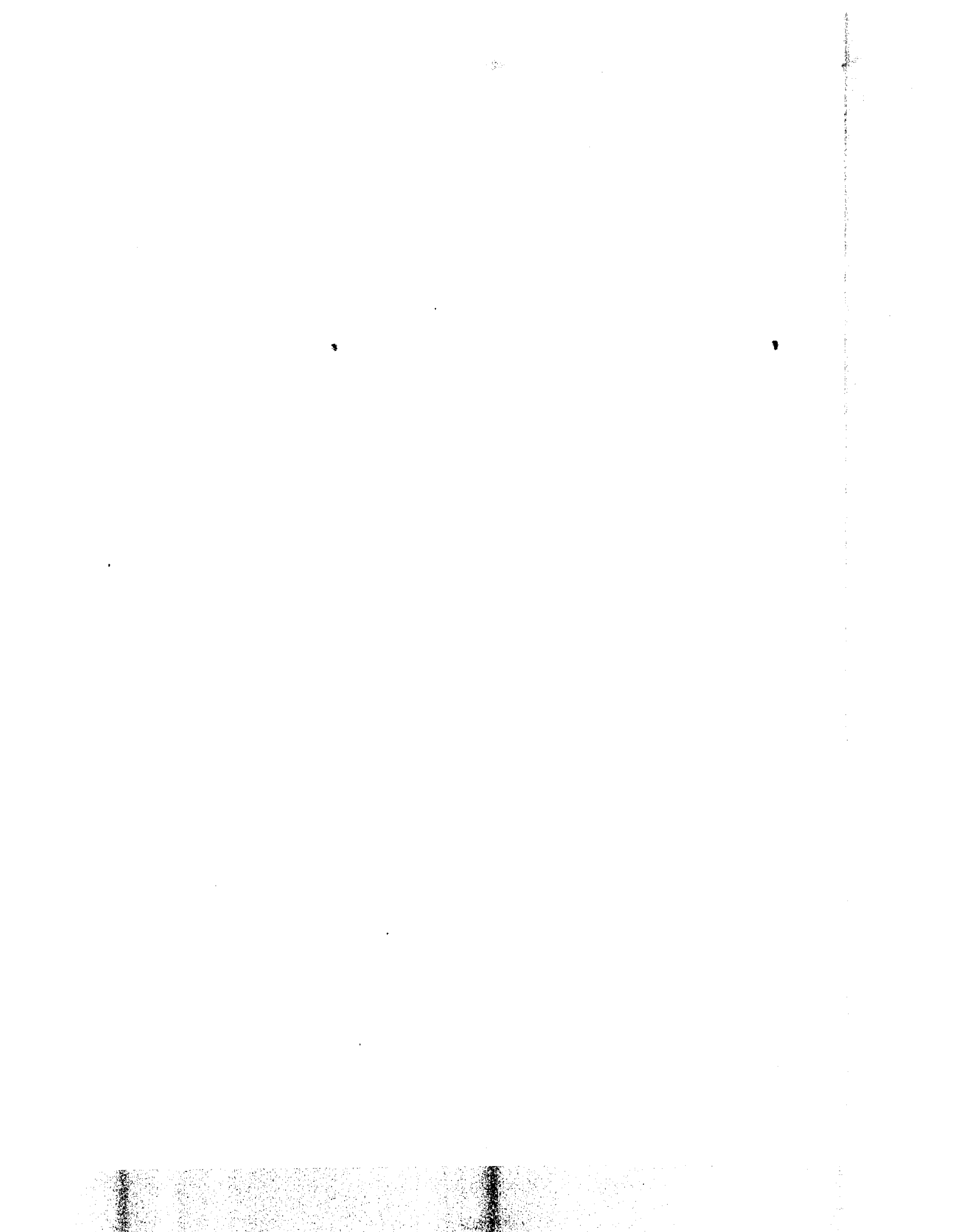
tax laws governing foreign trusts. (See p. 19.)

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

AGENCY COMMENTS

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

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



Contents

		Page
DIGEST		i
CHAPTER		
1	INTRODUCTION	1
	Currency reports required by the Bank Secrecy Act	1
	Foreign trust returns	2
	Foreign bank account reporting requirements	2
2	REVISIONS TO THE METHODS FOLLOWED IN PROCESSING AND USING CURRENCY REPORTS MIGHT IMPROVE THEIR VALUE	4
	How IRS processes currency reports	4
	Currency reports result in few IRS criminal investigations or civil actions	5
	TECS could be used to streamline the processing of currency reports and possibly improve their value	8
	What is TECS?	8
	Processing and use of currency reports could be improved	9
	IRS' Criminal Investigation Division has recognized the merit of TECS but has not used it effectively	11
	Conclusions	12
	Recommendations	13
	Agency comments and our evaluation	14
3	FOREIGN TRUST REPORTING REQUIREMENTS HAVE NOT BEEN EFFECTIVELY IMPLEMENTED	15
	The extent of compliance with foreign trust reporting requirements is unknown	15
	Limited usefulness of form 3520	16
	Revised processing procedures inadequate	17
	Potential problems with form 3520-A	18

		Page
	Conclusions	18
	Recommendations	19
	Agency comments and our evaluation	19
4	SOME ACTION HAS BEEN TAKEN TO MAKE FOREIGN BANK ACCOUNT DATA USEFUL	21
	Action taken on House Government Operations Committee's recommendations	21
	Conclusions	28
	Recommendations	28
	Agency comments and our evaluation	28
5	SCOPE OF REVIEW	30
APPENDIX		
I	Letter dated March 19, 1979, from the Secretary of the Treasury	31

ABBREVIATIONS

CMIR	report of international transportation of currency or monetary instruments
CTR	currency transaction report
GAO	General Accounting Office
IRS	Internal Revenue Service
TECS	Treasury Enforcement Communications System

CHAPTER 1

INTRODUCTION

As requested by the Chairman of the Subcommittee on Oversight, House Committee on Ways and Means, we reviewed the Internal Revenue Service's (IRS') use of

--currency transaction reports (CTRs);

--reports of international transportation of currency or monetary instruments (CMIRs);

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

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

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

To facilitate Federal investigations of certain illegal activities, such as drug trafficking and tax evasion, the Congress enacted several laws requiring individuals, financial institutions, and others to report certain financial transactions to the Government. The Bank Secrecy Act (P.L. 91-508, Oct. 26, 1970) requires that certain transactions involving currency or monetary instruments and foreign bank accounts be reported to the Secretary of the Treasury. Similarly, the Revenue Act of 1962 (P.L. 87-834, Oct. 16, 1962) and the Tax Reform Act of 1976 (P.L. 94-455, Oct. 4, 1976) established filing requirements for information returns on foreign trusts.

While effective use of the various forms will not resolve problems such as drug trafficking and tax evasion, it would provide Treasury, IRS, Customs, the Department of Justice, and other Federal agencies with information that might be useful to them in carrying out their responsibilities.

CURRENCY REPORTS REQUIRED BY THE BANK SECRECY ACT

The Congress expected Federal agencies to use the currency reports required by the Bank Secrecy Act in carrying out their investigative responsibilities. Title II of the act requires that reports be filed on domestic currency transactions and on imports and exports of currency or monetary instruments. Currency is defined as the coin or paper

money of any country which is customarily accepted as money in the country in which it is issued. A monetary instrument is defined as the coin or currency of any country and certain other negotiable instruments.

Financial institutions within the United States generally must file a CTR, IRS form 4789, whenever currency of more than $10,000 is transferred by, through, or to such institutions. A CMIR, Customs form 4790, 1/ generally must be filed by any individual and certain legal entities who transport, mail, or ship on any one occasion an aggregate amount of more than $5,000 in currency or other monetary instruments into or out of the United States.

CTRs are filed with IRS' Philadelphia service center. CMIRs are filed with the Customs Service, which sends information from CMIRs to IRS' Philadelphia service center via magnetic computer tapes.

FOREIGN TRUST RETURNS

IRS forms 3520 and 3520-A are designed to enable IRS to better ensure compliance with the tax laws governing foreign trusts. Form 3520, United States Information Return for Creation of or Transfers to Certain Foreign Trusts, must be filed by U.S. citizens, corporations, and others on or before the 90th day after having established or transferred money or property to a foreign trust. Similarly, form 3520-A, Annual Return of Foreign Trust With U.S. Beneficiaries, must be filed by those who transfer money or property to a foreign trust which has one or more U.S. beneficiaries. Both forms are filed with IRS' Philadelphia service center.

By filing the forms, taxpayers afford IRS the opportunity to ensure the accuracy of their income tax returns. Failure to file the forms, however, may subject an individual to criminal or civil penalties.

FOREIGN BANK ACCOUNT REPORTING REQUIREMENTS

Title II of the Bank Secrecy Act authorized the Secretary of the Treasury to require that certain individuals file reports concerning their relationships with foreign financial institutions. Beginning with certain returns filed for tax year 1970, taxpayers were required to answer either yes or no to a question on the tax return directed at determining

---

1/Effective Dec. 29, 1976, this Customs form replaced IRS form 4790 bearing the same title.

whether they had a foreign bank account. Taxpayers who responded affirmatively were directed to report information on the foreign account on IRS Form 4683, U.S. Information Return on Foreign Bank, Securities, and Other Financial Accounts, to be filed with their Federal income tax return. In 1975, the question was not included on the tax return but certain taxpayers still were required to file form 4683. For tax years 1976 and later, IRS has required taxpayers to advise it whether "* * *at any time during the taxable year, [they] have an interest in or signature or other authority over a bank, securities, or other financial account in a foreign country."1/ If so, in 1976, taxpayers were required to file tax form 4683. This process caused disclosure problems between IRS and other agencies in Treasury; so after 1976, if the taxpayers answered yes to the question, they had to file Treasury Form 90-22.1 with the Treasury Department rather than with their tax returns sent to IRS.

In authorizing the collection of foreign account information, the Congress sought to combat the use of secret foreign bank accounts to hide legal income for tax evasion purposes and to conceal money involved in narcotics trafficking, illegal securities trading, margin violations, and gambling operations.

The Bank Secrecy Act and implementing Treasury regulations make the legal or beneficial ownership of an unreported foreign bank account a crime. Also, the failure to report a foreign bank account that was used to further another violation, especially tax evasion, might be cited as an indication of the willfulness of that violation.

1/ This requirement appears as Part III to Schedule B--Interest and Dividend Income of the Form 1040.

CHAPTER 2

REVISIONS TO THE METHODS FOLLOWED IN PROCESSING AND USING CURRENCY REPORTS MIGHT IMPROVE THEIR VALUE

Contrary to Congressional expectations, currency reports required by the Bank Secrecy Act have been of little use to IRS in carrying out its investigative responsibilities. IRS tries to use currency reports primarily as the bases for initiating investigations but the reports by themselves are not good indicators of tax law violations. The reports might be more valuable if they were all included in the Treasury Enforcement Communications System (TECS). That system would enable IRS to use currency reports and other information contained in the system to improve its evaluations of information it receives and possesses concerning tax law violations.

HOW IRS PROCESSES CURRENCY REPORTS

The Chief of the Criminal Investigation Staff at IRS' Philadelphia service center is responsible for sorting the CTRs received from financial institutions and the CMIRs received from Customs. He then routes them to the appropriate service centers where they are processed in the same manner as information items.

An information item is a tax-related communication received by IRS alleging or indicating that a particular individual or business may have violated the tax laws. IRS receives many of these communications from varied sources, such as Federal agencies, the general public, informants, and IRS employees. Although they contain no specific allegations of tax law violations, CTRs and CMIRs are processed as information items. Over 59,000, or about 24 percent, of the 248,475 information items IRS processed during fiscal year 1978 were CTRs and CMIRs.

The Criminal Investigation Staffs at IRS' 10 service centers evaluate information items to determine their potential for criminal tax investigation. Those items having such potential are forwarded to the affected taxpayer's district office for further evaluation by special agents. Although limited resources preclude IRS from investigating more than a fraction of the information items it receives, an information item ultimately may cause IRS to initiate a detailed criminal tax investigation.

Information items having no potential for criminal tax investigation are made available to representatives of IRS' Examination and Collection Divisions at the appropriate service center. Copies of those items selected by the representatives as having audit or collection potential are forwarded to the affected taxpayer's district office for further evaluation and follow up, if warranted.

Besides evaluating information items for their criminal tax implications, the service centers are responsible for entering certain data from each item into the computerized information item storage and retrieval system maintained by IRS' Criminal Investigation Division. That system is decentralized with each service center's data base maintained independently. Thus, data entered on one service center's information item system is not readily available to other service centers. Data entered into the system includes the taxpayer's name, address, occupation, and social security number and a description of the alleged tax law violation when applicable. Data is retained in the system from 1 to 10 years depending on its source and potential value. All currency reports are retained for 3 years.

Each month, the storage and retrieval system produces two match listings. One identifies each individual and business on whom at least two information items were evaluated during the preceding month. The second identifies each individual and business on whom information items were evaluated during both the preceding month and any prior month.

IRS guidelines require that the service centers reevaluate each information item appearing on either match listing to determine if different dispositions should be made of them. According to the Director of IRS' Criminal Investigation Division, two or more information items together may indicate potential for criminal tax investigation while either item by itself may be meaningless.

CURRENCY REPORTS RESULT IN FEW IRS CRIMINAL INVESTIGATIONS OR CIVIL ACTIONS

Many IRS officials and investigators contend that CTRs and CMIRs, by themselves, are not very meaningful. Our review of random samples of CTRs and CMIRs which had been evaluated by IRS personnel supports that contention. Furthermore, their usefulness is limited when matched only with data contained in one IRS service center's computerized information item system.

We reviewed IRS' disposition of 241 randomly selected CTRs which were processed by five IRS service centers during

fiscal years 1976 and 1977. Criminal Investigation, Examination, and Collection personnel at the service centers evaluated 194 of the 241 CTRs and rejected 155 or 80 percent as having no criminal tax investigation, audit, or collection potential. Forty-seven CTRs were held for evaluation pending the filing of a tax return applicable to the year in which the transaction occurred. Only 39 of the 194 CTRs evaluated were selected and referred to the appropriate district office:

Reason for selection	Number of CTRs selected
Criminal tax investigation potential	1
Collection potential	11
Audit potential	27
Total	39

District criminal investigation personnel were unable to determine the status of the one CTR selected as having potential for criminal tax investigation.

Of the eleven CTRs selected for collection potential, district collection personnel rejected three, used four as the bases for initiating investigations, associated one with an ongoing investigation, and were unable to account for the other three. Two of the four CTR-based investigations produced no additional revenue; the other two CTR-based investigations and the ongoing investigation were still open when we completed our review.

Of the 27 CTRs selected for audit potential, district examination personnel rejected 15, used 9 to initiate audits or to supplement ongoing audits, and were unable to account for the remaining 3. Seven of the nine audits were still open when we completed our review, while the other two resulted in recommended additional tax liabilities of $2,689 and $57.

We also reviewed IRS' disposition of 175 randomly selected CMIRs which were processed by four IRS service centers during fiscal years 1977 and 1978. Criminal Investigation, Examination, and Collection personnel at the service centers evaluated 171 of the 175 CMIRs and rejected 129 or 75 percent as having no criminal tax investigation, audit, or collection potential. One CMIR was transferred to another service center while another three were held for evaluation pending the filing of a tax return applicable to the year in which the transaction occurred. Only 42 of the 171 CMIRs evaluated were selected and referred to the appropriate district office:

Reason for selection	Number of CTRs selected
Criminal tax investigation potential	14
Collection potential	16
Audit potential	12
Total	42

District criminal investigation personnel rejected 11 of the 14 CMIRs received from the service centers, accepted one and later closed it without initiating an investigation, and were unable to account for the other two.

Examination personnel rejected nine CMIRs, associated one with an ongoing audit, and had taken no action with respect to the other two.

Collection personnel opened investigations on the basis of six CMIRs, closed two without conducting investigations, associated one CMIR with an ongoing investigation, and could not account for the other seven. The six CMIR-based investigations were still open when we concluded our review. The other investigation concluded with an IRS determination that additional taxes were due but not collectible.

We also attempted to obtain the September 1977 match listings generated by the computerized information item storage and retrieval system to see if the matching process enhanced the usefulness of currency reports. At the Andover, Fresno, and Kansas City service centers, we reviewed 53 randomly selected sets of computer matched information items. Each set of items contained at least one CTR or CMIR.

We reviewed IRS' disposition of the 53 sets of items the service centers sought to reevaluate. Criminal Investigation, Examination, and Collection personnel at the service centers reevaluated 36 of the 53 sets of items. Sixteen sets of items were held for evaluation pending the filing of tax returns applicable to the years in which the transactions occurred, and we could not determine the dispostion of one set. Thirty, or 83 percent, of the 36 reevaluated sets were rejected as having no criminal tax investigation, audit, or collection potential.

Only six sets of information items were selected as having some potential and were referred to the appropriate district office. Two of the six sets of information items were associated with ongoing criminal tax cases. Two other sets resulted in the initiation of audits which were still open when we completed our review, while another set formed

the basis for an audit in which additional taxes were assessed. IRS personnel were still holding the one remaining set for further evaluation.

The Chief of the Criminal Investigation Staff at the Philadelphia service center informed us that no useable monthly listings had been prepared for September 1977 through January 1978 due to computer problems. At the Austin center, the Assistant Chief said that limited staffing made it impossible to reevaluate items produced through match listings.

Although match listings constitute an effort on IRS' part to associate CTRs and CMIRs with tax fraud allegations it receives, the number of productive matches is small. This may be attributable to the fact that match listings simply associate unproven allegations with other unproven allegations and currency reports. Moreover, match listings are limited in scope to information items processed by particular service centers and therefore are not matched on a national basis. As a result, an allegation IRS receives concerning a particular taxpayer could be entered on one service center's information item system while a currency report pertaining to that taxpayer could be entered on another service center's system. Those two items would not be associated on match listings.

TECS COULD BE USED TO STREAMLINE THE PROCESSING OF CURRENCY REPORTS AND POSSIBLY IMPROVE THEIR VALUE

CTRs and CMIRs have brought about few IRS criminal investigations, tax audits, or collection actions because the reports, by themselves, are not good indicators that taxpayers may have filed erroneous tax returns. Currency reports might be more useful if they were centralized in TECS and used by IRS along with other data in that system to supplement information it receives and possesses indicating possible tax violations.

TECS could also help streamline the processing of currency reports by eliminating unnecessary exchanges of information. IRS' Criminal Investigation Division has recognized the benefits of using TECS. However, IRS has not taken action to ensure that its employees effectively use the system--a step which is necessary if currency reports are going to be included in the system's data base.

What is TECS?

TECS is a computerized information storage and retrieval system designed to assist Federal personnel in carrying out various law enforcement missions. It is operated by the Customs Service under the Treasury Department's supervision.

Besides Customs, the following Federal agencies participate in TECS:

--Bureau of Alcohol, Tobacco and Firearms.

--U.S. Coast Guard.

--Drug Enforcement Administration.

--Immigration and Naturalization Service.

--Internal Revenue Service.

--State Department.

Besides serving as a storage and retrieval system for data entered by the participating Federal agencies on specific individuals and businesses, TECS also serves as a retrieval system for information contained in the Federal Bureau of Investigation's National Crime Information Center. That system contains criminal records and information on stolen property and arrest warrants on certain individuals and businesses. The involved Federal agencies have determined that release of data contained in TECS and in the National Crime Information Center is in accordance with the laws governing citizens' privacy.

Processing and use of currency reports could be improved

In June 1976, Customs and IRS agreed to begin exchanging data from currency reports. In July 1976, Customs began sending IRS magnetic computer tapes containing information from CMIRs and, in October 1976, IRS began sending CTR tapes to Customs.

The exchanges of both CMIRs and CTRs are unnecessary. Besides sending CMIR tapes to IRS, Customs also enters CMIR data on TECS. However, IRS has access to that system. Similarly, IRS enters CTRs on the Criminal Investigation Division's computerized information item storage and retrieval system and also keypunches information from the forms into a separate system which produces the tapes for Customs.

IRS also sends a copy of each CTR to the Treasury Department's Reports Analysis Unit which matches each CTR against country and dollar criteria supplied by the Drug Enforcement Administration. If the CTR matches the criteria, it is referred to that agency. During fiscal year 1978, Treasury referred 1,398 CTRs and 83 CMIRs to the Drug Enforcement Administration.

Most of these data exchanges would be unnecessary if CTRs were entered on TECs thereby enabling Customs and the Reports Analysis Unit to access them directly. Treasury's Reports Analysis Unit could then provide quick responses to other Federal agencies' requests for both CTR and CMIR data to the extent appropriate under the laws governing citizens' privacy.

More important, CTRs might be more useful if they were entered on TECS and IRS made more effective use of that system. Under that concept, IRS could use CTRs as well as CMIRs and other data, which already is on TECS, to supplement information it receives and possesses concerning tax violations rather than using them ineffectively as the bases for initiating investigations.

Specifically, IRS could use TECS as a better means of separating information items with the potential to indicate tax fraud from those without that potential. For example, given an allegation that two individuals had underreported income on their 1978 tax returns, IRS might reasonably use its limited resources to investigate the allegation against an individual with a previous arrest record on whom several CTRs were filed rather than investigating an allegation not supported by other information. If CTRs were included on TECS, IRS' information item evaluators could routinely check allegations IRS receives against the system to determine whether other information, including CTRs, would strengthen them.

IRS' computerized information item storage and retrieval system cannot provide similar assistance to evaluators during the information item evaluation process. That system lacks immediate access capabilities thus precluding IRS' information item evaluators from using currency reports to assist in the initial evaluation process. Moreover, the information item system is service center wide rather than national in scope and it contains only a fraction of the information contained in TECS.

While no assurance exists that CTRs would be more valuable if processed through TECS, they apparently have not been very useful to IRS under its processing procedures. Therefore, some action is needed to improve their usefulness.

In December 1978, the Treasury Department's Deputy Assistant Secretary for Enforcement told us that Treasury plans to enter CTRs on TECS. He indicated that CTR information should be fully incorporated on TECS by November 1979. In doing this, however, Treasury will need to ensure that unnecessary exchanges of information are eliminated and that

IRS effectively uses the system to improve its evaluations of tax fraud allegations.

IRS' Criminal Investigation Division has recognized the merit of TECS but has not used it effectively

In May 1978, the Criminal Investigation Division completed an in-house study of its participation in TECS. The study group found, in canvassing IRS field offices, that

> "Many of the districts reported that TECS was effective and could be made even more effective with increased training of operators, increased awareness of TECS capability on the part of [Criminal Investigation] technical personnel, increased convenience for making queries by special agents and increased data base input by the Service."

The study report listed the following as some of the ways Criminal Investigation personnel could use TECS:

- --Determine identifying data, such as social security or employer identification number.
- --Obtain information relating to investigations conducted by other agencies.
- --Determine ownership of assets, such as automobiles and aircraft.
- --Ascertain a person's criminal history.

In a September 6, 1978, memorandum, the Director of the Criminal Investigation Division requested approval from IRS' Assistant Commissioner for Compliance to take action on the study group's recommendations. In January 1979, the Assistant Commissioner told us that he supports the concept of increased use of TECS by IRS but had not yet approved the recommended actions.

In this regard, the Assistant Commissioner noted that a key aspect of the recommendations is that IRS increase its data base input to TECS. He said that, before approving action on that recommendation, it would be necessary to ensure compliance with the limitations imposed on information exchanges by the Tax Reform Act of 1976, which tightened the rules governing IRS' disclosure of tax data, and the Privacy Act of 1974. The Assistant Commissioner said, however, that CTRs can be entered on TECS

because they are not subject to the disclosure restrictions of the Tax Reform Act of 1976. However, he noted that strict controls are needed before tax data can be entered on TECS, and he indicated that IRS is seeking to determine whether such controls can feasibly be added to TECS.

CONCLUSIONS

IRS has processed CTRs and CMIRs with an aim toward using them as the bases for starting criminal investigations, audits, or collection actions. The reports, however, have not been very useful to IRS largely because the fact that an individual has engaged in a large cash transaction is, in itself, not very meaningful.

Changes to the methodology IRS follows in processing and using CTRs and CMIRs, however, could improve their value. Specifically, IRS could use CTRs and CMIRs to supplement information it receives and possesses regarding tax fraud rather than using them separately as the bases for initiating investigative or other action. For example, in processing and evaluating several information items alleging that certain taxpayers underreported income in a prior year, Criminal Investigation Division personnel could use CTRs and CMIRs as further evidence that particular items have more potential than others. This is important because limited resources preclude IRS from investigating more than a fraction of the information items it receives each year.

The Treasury Department already operates a data storage and retrieval system--TECS--which could provide IRS immediate access to currency reports. CMIR data already is being entered on TECS; however, CTR data is not. If CTRs were entered on TECS and IRS made routine use of the system, IRS would have ready access to currency reports to improve evaluations of specific allegations it receives. At the same time, it could consider other potentially useful information on the system, such as arrest records and records relating to investigations performed by other agencies. Such information would not only assist the Criminal Investigation Division, but it would also enable Examination and Collection personnel to reach more informed decisions on the audit and collection potential of particular information items.

In addition, if CTRs were entered in TECS:

--IRS and Customs would no longer need to exchange CTR and CMIR computer tapes since each agency has access to the system.

--IRS would no longer need to send a copy of each CTR to Treasury for matching against Drug Enforcement Administration criteria because the Reports Analysis Unit would have direct access to the CTR data.

While no assurance exists that CTRs would be more useful if processed through TECS, some action is needed to enhance their value. The Treasury Department already plans to enter CTRs in TECS. In doing so, however, Treasury should ensure that any unnecessary exchanges and processing of currency reports by IRS and other agencies are eliminated. Also, it should ensure that IRS effectively uses TECS to improve its evaluation of allegations of criminal violations of the tax laws. In this regard, as set forth in a study by IRS' Criminal Investigation Division, IRS needs to train its personnel to understand and effectively use TECS.

Once central processing is implemented, Treasury should monitor the usefulness of CTR information to determine whether it has improved. However, it should also determine whether currency reports have other potential uses. If Treasury determines through these efforts that the value of currency reports cannot be improved, it should request the Congress to reconsider the need for the reporting requirements.

RECOMMENDATIONS

We recommend that the Secretary of the Treasury, in implementing the plans to enter CTRs on TECS, should:

--Eliminate unnecessary processing of currency reports by (1) ensuring that all currency reports are filed with the group designated to enter the reports on TECS and (2) eliminating wholesale exchanges of currency reports between IRS, Customs, and Treasury.

--Ensure that IRS uses TECS to improve evaluations of information it receives and possesses concerning possible tax law violations.

In addition, the Secretary should:

--Monitor the use of CTRs, once they are incorporated in TECS, to determine if their value has improved.

--Determine whether currency reports have other potential uses.

If the Secretary determines that the value of currency reports cannot be improved, he should request the Congress to reconsider the need for the reporting requirements.

We recommend that the Commissioner of Internal Revenue provide necessary training and take appropriate steps to ensure that IRS personnel understand and know how to use TECS.

AGENCY COMMENTS AND OUR EVALUATION

By letter dated March 19, 1979, the Acting Secretary of the Treasury, on behalf of Treasury and IRS, generally agreed to implement all our recommendations regarding currency reports.

Treasury intends to eliminate unnecessary processing and wholesale exchanges of currency reports between IRS and the Customs Service as part of its ongoing program to enter CTRs on TECS. However, Treasury first plans to examine whether it is feasible and cost beneficial to have CTRs and other reports filed with and processed by a single organizational unit which would be responsible for entering the reports on TECS.

Although Treasury agreed that it should monitor the use of CTRs and other reports entered on TECS to evaluate their effectiveness as law enforcement tools, Treasury said that currency reports already have proven useful to various Federal law enforcement agencies. We recognize that, in particular instances, currency reports have been useful to other law enforcement agencies; however, we did not assess their overall usefulness since our review generally was limited to evaluating IRS' use of the reports.

Nevertheless, we noted that Treasury has not systematically evaluated the usefulness of the reports to Federal law enforcement agencies. Treasury has not determined whether the benefits outweigh the costs involved--from the Government's standpoint and that of individuals, financial institutions, and others who bear the burden of filing the reports. We believe such an evaluation is necessary to adequately determine the overall usefulness of currency and other reports, such as foreign bank account reports, to Federal law enforcement agencies. This evaluation should be done in determining whether TECS improves the usefulness of CTRs and whether currency reports have other potential uses.

CHAPTER 3

FOREIGN TRUST REPORTING REQUIREMENTS

HAVE NOT BEEN EFFECTIVELY IMPLEMENTED

Despite possible criminal and civil penalties, taxpayers have filed few foreign trust returns. IRS has neither developed a compliance program to ensure that required forms are filed, nor established a method for processing and evaluating the forms designed to maximize their usefulness. As a result, the potential usefulness of the forms is unknown and IRS may not be doing all that it can to promote voluntary compliance in an area where a potentially serious tax revenue shortfall exists.

THE EXTENT OF COMPLIANCE WITH FOREIGN TRUST REPORTING REQUIREMENTS IS UNKNOWN

IRS does not have complete statistics on the number of form 3520s received since 1973. IRS officials estimated, however, that fewer than 100 were filed during fiscal years 1974 and 1975. During calendar year 1977--a year for which IRS gathered statistics--127 form 3520s were filed. Although individuals are subject to criminal and civil penalties for failing to file form 3520, IRS does not have a program designed to ensure compliance with the filing requirement.

IRS officials were unable to estimate how many form 3520s should be filed each year, but they believe that noncompliance with the filing requirement is substantial in light of the number of foreign trusts which apparently exist. IRS' offshore trust coordinator, for example, pointed out that an IRS investigation of taxpayers' accounts at one Bahamian bank disclosed the existence of 300 foreign trusts set up by U.S. citizens. He also noted that one criminal investigation led IRS to evidence of the existence of hundreds of foreign accounts and trusts set up by U.S. citizens.

In an August 1977 memorandum, the Director of the Criminal Investigation Division assessed the situation as follows:

> "We have been informally advised that for the fiscal year ended June 30, 1974 only twenty Forms 3520 were filed at the Philadelphia Service Center. For fiscal year 1975, incomplete estimates only are available which indicate 60-70 forms were filed. These small figures indicate a serious noncompliance problem.

The current method of handling Forms 3520 at the Philadelphia Service Center and the District offices makes it extremely unlikely that viable prosecution cases for failure to file these forms can be sustained. * * * The forms are not assigned DLN [Document locater number] numbers or recorded on the IMF or BMF [individual or business master file]. On several occasions we were requested by the Department of Justice to furnish it with certified copies of Forms 3520, or in lieu thereof, certifications of nonfiling. The method of handling Forms 3520 made it impossible for us to comply with those requests."

The Director's assessment indicates that prosecutions could be sought for failure to file form 3520 if IRS handled the forms differently. Such prosecutions, in our view, would constitute one viable way to seek increased voluntary compliance with the filing requirements.

LIMITED USEFULNESS OF FORM 3520

Before January 1, 1978, Philadelphia service center personnel sorted form 3520s according to each affected taxpayer's IRS district office and forwarded them to the Examination Division's district Returns Program Managers who screen tax returns to determine their audit potential. Returns Program Managers were responsible for associating form 3520 with ongoing audits, where applicable, and evaluating the remaining forms for audit potential.

IRS guidelines did not set forth criteria for evaluating a form 3520's audit potential. Returns Program Managers, therefore, based their evaluations on judgment and experience and generally made no attempt to evaluate the form 3520s for criminal tax and collection potential. As a result, very little use was made of the forms.

The Office of International Operations' Returns Program Manager said he received 38 form 3520s between May 11 and September 30, 1977. Of the 38 forms, he determined that 37 had no audit potential and sent 1 to an Examination Division group manager for consideration. The group manager decided the form 3520 had no audit potential.

The Returns Program Manager in Los Angeles said he had no statistics on form 3520s. Regarding evaluation criteria, he said form 3520s involving over $10,000 prompted him to check associated tax returns for the reporting of trust income. On the basis of that check, he decides whether to refer form 3520s to group managers for audit consideration. He noted,

however, that a form 3520 generally does not contain enough information on which to base an audit. Criminal Invesitgation Division managers were not familiar with the form.

In Boston, the Returns Program Manager told us that he received about five form 3520s during calendar years 1975 through 1977. He said that three form 3520s were forwarded to group managers for their consideration, but he was unable to determine whether audits resulted. Criminal Investigation Division managers were not familiar with the form.

In Chicago, the Returns Program Manager said that he receives about 25 form 3520s each year. He said also that his experience suggests that form 3520s are filed by honest taxpayers. As a result, he does not consider the form a good indicator of audit potential. Criminal Investigation Division managers noted that a form 3520 is a negative indicator of criminal tax potential due to the added difficulties in obtaining information overseas.

In Dallas, the Returns Program Manager stated that he receives an average of one 3520 a month usually involving amounts less than $1,000. The relatively small amounts involved in the trusts led the Returns Program Manager to reject each form as having no audit potential. Criminal Investigation Division managers knew little about form 3520. However, they said that the existence of a foreign trust indicates that it would be more difficult to pursue a criminal tax investigation.

Revised processing procedures inadequate

In January 1978, IRS revised its procedures for handling form 3520s. The revised procedures directed the forms to the Chief, Criminal Investigation Staff at the Philadelphia service center but said nothing about what he was to do with them. In February 1978, the Chief informed us that he had never seen a 3520 and had not received a copy of the revised procedures.

After our discussion with the Chief, IRS again revised its procedures for handling form 3520. The new procedures required retention of the form at the point of receipt in the Philadelphia service center pending issuance of further processing instructions. The Director of IRS' Criminal Investigation Division at the national office informed the Director of IRS' Examination Division that:

> "A review of the forms [3520s] and feedback from our Philadelphia Service Center [Criminal Investigation] Staff convinces us that the forms should not be

initially reviewed by the [Criminal Investigation] Staff at the PSC [Philadelphia Service Center]. The forms lack the type of information needed to make a determination as to possible criminal violations of the internal revenue laws."

In June 1978, the IRS official responsible for developing processing procedures for the form 3520 informed us that a methodology for processing, evaluating, and using the forms was under consideration. On August 21, 1978, however, IRS issued guidelines specifying that Philadelphia service center personnel would again forward form 3520s to District Returns Program Managers which was essentially the same procedure IRS followed in handling the forms before January 1978. The latter guidelines specified no meaningful methodology for evaluating or using the form.

POTENTIAL PROBLEMS WITH FORM 3520-A

Beginning with certain returns filed for tax year 1977, U.S. citizens were required to answer either yes or no to a question on the tax return directed at determining whether they had transferred money or property to a foreign trust having U.S. beneficiaries. Taxpayers who responded affirmatively were alerted to file form 3520-A, if applicable, with IRS' Philadelphia service center. The tax laws authorize criminal and civil penalties for failure to file this form in a timely manner.

Because April 17, 1978, was the filing deadline for most taxpayers required to file 1977 tax returns, the Criminal Investigation Staff at the service center had received few form 3520-As before we completed our review. Thus, we did not evaluate how the forms were being used. We noted, however, that IRS had not established procedures for processing, evaluating, and using the form or for ensuring compliance with the filing requirement.

Similar to the situation with form 3520, the IRS officials responsible for developing processing procedures for the forms informed us in June 1978 that IRS was considering how to best use the form 3520-A. The August 21, 1978, guidelines issued pursuant to form 3520 also applied to form 3520-A. However, as stated above, those guidelines did not specify any meaningful methodology for evaluating or using the forms.

CONCLUSIONS

IRS' handling of forms 3520 and 3520-A has been characterized by indecision. IRS has no program for ensuring compliance with the filing requirements and has not established

a meaningful methodology for evaluating and using the forms. In effect, the few taxpayers who choose to file one of these forms have no assurance that IRS is doing all that it can to identify and pursue those who choose not to file and, thus, are being unreasonably burdened. Unless IRS can rectify the situation, it might be best to relieve the compliant taxpayer of any further burden by simply eliminating the returns and developing alternative methods for ensuring compliance on the part of taxpayers with the tax laws governing foreign trusts.

RECOMMENDATIONS

We recommend that the Commissioner of Internal Revenue determine whether IRS can effectively use foreign trust returns by developing

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

--appropriate evaluation criteria aimed at maximizing the usefulness of the forms.

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

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

--develop an alternative plan of action for ensuring compliance on the part of taxpayers with the tax laws governing foreign trusts.

AGENCY COMMENTS AND OUR EVALUATION

In his March 19, 1979, letter, the Acting Secretary of the Treasury agreed that (1) forms 3520 and 3520-A could better serve Treasury's and IRS' purposes, (2) the forms have not been adequately controlled, (3) guidance on potential usefulness is inadequate, and (4) compliance has not been adequately enforced.

Treasury agreed to:

--Study ways to make the forms more effective.

--Establish processing procedures that will facilitate the forms' retrieval and use.

--Review current evaluation criteria for the forms to determine whether better guidance can be developed to increase their usefulness.

--Take actions to achieve maximum compliance with foreign trust return filing requirements.

CHAPTER 4

SOME ACTION HAS BEEN TAKEN TO MAKE FOREIGN BANK ACCOUNT DATA USEFUL

On May 5, 1977, the House Committee on Government Operations issued a report entitled "Internal Revenue Service and Treasury Department Enforcement of the Foreign Bank Account Reporting Requirements of the Bank Secrecy Act." In general, the Committee concluded that "results of the foreign bank account reporting requirements of the Bank Secrecy Act have not been imposing to date." To remedy that situation, the Committee made 10 recommendations to the Department of the Treasury and IRS. Treasury and IRS have taken some action on the recommendations, but follow-up action is needed.

ACTION TAKEN ON HOUSE GOVERNMENT OPERATIONS COMMITTEE'S RECOMMENDATIONS

In its May 5, 1977, report, the Committee concluded that the value of the foreign bank account question as an investigative tool for IRS and other Federal agencies cannot be determined until the Treasury Department and IRS give the program a full effort. In the Committee's opinion, results of the foreign bank account reporting requirements were not imposing because:

--A low response rate was obtained from individual taxpayers for tax years in which the foreign bank account question was not on the front page of the tax return.

--IRS did not vigorously enforce compliance with the foreign bank account reporting requirement through enforcement or education programs directed at taxpayers who failed to respond to the question.

--Treasury and IRS officials made little effort to disseminate foreign bank account information although the Congress specifically intended that such information would be available to and exchanged among Federal law enforcement and regulatory agencies.

--IRS did not process form 4683s in a manner that would facilitate collection and dissemination of data on foreign bank accounts.

--The Tax Reform Act of 1976 severely restricted IRS' authority to disclose information provided by taxpayers, such as foreign bank account data.

In an effort to make the foreign bank account reporting requirements of the Bank Secrecy Act more effective, the Committee made 10 recommendations to the Treasury Department and IRS. The following is a description of the actions taken in response to each of those recommendations by Treasury and IRS through October 1978.

Recommendation 1

"The implementing Treasury Regulations to the Bank Secrecy Act must be revised to clarify compliance responsibilities within the Department especially as they relate to the office of the Assistant Secretary (EOTA) [Enforcement, Operations, and Tariff Affairs], and the Internal Revenue Service."

With this recommendation, the Committee sought to ensure that the Secretary of the Treasury would, in developing a program aimed at maximizing the usefulness of foreign bank account data, clearly delegate authority and fix responsibilities.

Agency actions

In a letter dated June 28, 1977, the Secretary of the Treasury informed the Chairman of the Subcommittee on Commerce, Consumer, and Monetary Affairs, House Committee on Government Operations, that revisions to the regulations would be "completed and published for comment within the next few months." In a letter dated October 12, 1977, the Secretary informed the Committee Chairman that the revised regulations "will be issued before the end of this year." As of October 13, 1978, the regulations had not been issued.

The Deputy Assistant Secretary for Enforcement, Treasury Department, told us in October 1978 that the regulations had not been issued because they were still under review within the Treasury Department. However, he said, that when issued, they would be responsive to the Committee's recommendation. He emphasized that despite the absence of revised regulations, his office had the necessary authority to take actions designed to maximize the usefulness of information on foreign bank accounts. In this regard, he had established a separate entity, the Reports Analysis Unit, within the Department whose major purpose is to process, analyze, and disseminate currency and foreign bank account reports.

Because the draft regulations were still under review within the Treasury Department, we were unable to evaluate their responsiveness to the Committee's recommendations. Also, we did not evaluate the operations of the Reports Analysis Unit because it was not established until July 1978, shortly before we completed our review.

Recommendation 2

"The implementing Treasury Regulations (31 CFR 103.24) should clearly state the Foreign Bank Account Question is required on all tax return forms (Forms 1040, 1120, 1120S, 1041, and 1065), as well as require the submission of a supplementary tax form (Form 4683)."

Agency actions

In his June 28, 1977, letter to the Subcommittee Chairman, the Secretary of the Treasury indicated that such a revision to the regulations would pose problems primarily because tax information is subject to the disclosure restrictions set forth in the Tax Reform Act of 1976. The act tightened restrictions governing IRS' disclosure of tax information thus raising questions concerning whether IRS could legally disseminate foreign bank account data. Requiring that taxpayers submit a supplementary tax form describing their foreign bank accounts could, therefore, defeat one purpose of the Bank Secrecy Act--dissemination of such information to various Federal agencies.

Subsequently, by converting IRS form 4683 to Treasury form 90-22.1 for tax years beginning after 1976, the Secretary apparently resolved disclosure problems. The Treasury form is designed to collect the same information sought on form 4683 but is to be filed with the Treasury Department rather than with IRS. As of October 13, 1978, however, Treasury had not issued regulations nor taken action to ensure placement of the foreign bank account question on all tax return forms. Treasury and IRS officials told us that competing demands for space on tax return forms and continuing congressional and public interest in tax simplification were factors entering into their decision to reject that aspect of the Committee's recommendation.

Recommendation 3

"The Foreign Bank Account Question (foreign bank, trust, securities and other financial accounts question) should be included on the first page of all tax returns if there is a serious intent

and effort by IRS, Department of Treasury and other Federal agencies to combat the foreign bank account problem."

Agency actions

In his June 28, 1977, letter to the Subcommittee Chairman, the Secretary pointed out that Treasury and IRS take the foreign bank account problem seriously but have not settled on the best method to deal with it. The Secretary noted that disclosure restrictions and tax simplification goals would affect decisions regarding placement of the foreign bank account question on tax returns.

Although disclosure problems apparently no longer exist with regard to Treasury form 90-22.1, competing demands for space on the first page of tax returns and tax simplification concerns led Treasury and IRS to reject this recommendation.

Recommendation 4

"The implementing Treasury Regulations should direct IRS to establish plans and a program to utilize the information obtained through the foreign bank account reporting requirements of the Bank Secrecy Act."

Agency actions

In his June 28, 1977, letter, the Secretary stated that the Treasury Department did not concur with this recommendation. In the Secretary's opinion, internal management procedures, rather than regulations, were needed to plan and implement such a program.

One of the responsibilities of the Treasury Department's newly created Reports Analysis Unit is to establish plans and a program for using information on taxpayers' foreign bank accounts. The Deputy Assistant Secretary for Enforcement told us in October 1978 that the newly established unit had received about 210,000 form 90-22.1s and had entered about half of them on TECS. This will enable Treasury to retrieve foreign account information for use by IRS and other Federal law enforcement agencies.

According to the Deputy Assistant Secretary, both IRS and Customs agents are involved with Treasury personnel in establishing the data base and planning how the computerized information will be used. As of October 1978, however, they were concentrating their efforts on entering information on the data system.

Recommendation 5

> "IRS should implement projects consistent with 4th Amendment Rights to complement other plans relating to the use of foreign bank account information."

With this recommendation, the Committee sought to encourage IRS to use foreign bank account information to initiate major investigative efforts.

Agency actions

IRS headquarters officials told us in October 1978 that foreign bank account information generally is used in conjunction with overall compliance efforts--audits, collection cases, and criminal investigations--rather than as a sole basis for starting such efforts. In this regard, they said that the fact that a taxpayer has a foreign bank account can impact on decisions IRS employees make on a daily basis. But they also noted that foreign bank account information is less meaningful by itself than when associated with other information concerning a particular taxpayer.

IRS headquarters officials stated further that a taxpayer's failure to respond or an inaccurate response to the foreign bank account question could be meaningful when associated with other information. For example, a criminal tax investigation could lead IRS to evidence that a taxpayer has an unreported foreign bank account. This, in turn, could lead to an IRS recommendation that the taxpayer be prosecuted for willfully failing to file the foreign bank account report.

District investigative personnel in Boston, Chicago, Dallas, and Los Angeles told us that foreign bank account information must be associated with other information to be meaningful. They indicated, however, that the fact that a taxpayer has a foreign bank account can complicate matters because it is often difficult to gain access to information concerning the account.

In general, IRS officials do not believe that foreign bank account data can be used as a basic starting point for audits, collection cases, or criminal investigations. Rather, they believe that current compliance efforts, which include occasional special projects involving foreign bank accounts, are further enhanced when foreign bank account data is readily available to IRS personnel. As of October 1978, IRS officials had implemented no changes to their methods for using foreign bank account information.

Recommendation 6

> "The Secretary of the Treasury should encourage and take steps to achieve cooperation between Government agencies in the exchange of information obtained through the Bank Secrecy Act."

Agency actions

In his June 28, 1977, letter to the Chairman of the Subcommittee on Commerce, Consumer, and Monetary Affairs, the Secretary stated that CTR and CMIR information already was being made available to the Drug Enforcement Administration.

In his October 12, 1977, letter to the Chairman, House Committee on Government Operations, the Secretary stated that Treasury had reached an agreement with the Department of Justice whereby foreign financial account information would be furnished to Justice on a selective basis. According to the Secretary, written requests relating to specific individuals would be honored in accordance with the intent of the Bank Secrecy Act and laws governing citizens' privacy.

In October 1978, Treasury's Deputy Assistant Secretary for Enforcement told us that the Reports Analysis Unit had been established with a view toward complying with the Committee's recommendation. The Unit will serve as a focal point for disseminating currency reports and foreign account information, to the extent permitted by law, in accordance with the needs of other Federal agencies. However, the Unit's task of computerizing the backlog of foreign account reports must be completed before data can be disseminated.

Recommendation 7

> "The Assistant Secretary of Treasury (EOTA) should study the informational needs of those agencies concerned with bank secrecy issues and direct the IRS to (a) revise its procedures and Form 4683 in order to overcome problems resulting from [the] Tax Reform Act of 1976 and to provide the information in a form to meet these needs, and (b) maintain this information in such a manner that it can be readily analyzed and provided to other agencies."

Agency actions

The Secretary's decision to substitute Treasury form 90-22.1 for IRS form 4683 apparently resolved dissemination problems related to the disclosure provisions of the Tax

Reform Act of 1976. Treasury then established the previously discussed Reports Analysis Unit which is supposed to begin analyzing and disseminating foreign bank account information, in accordance with the laws governing citizens' privacy, to other Federal agencies once the information is computerized.

Recommendation 8

"IRS personnel involved in recommending criminal actions and Department of Justice personnel involved in criminal prosecutions should consider bringing prosecutions under the provisions of 31 U.S.C. [those sections of the U.S. Code relating to money and finance] in matters involving violations regarding foreign bank, securities and other financial accounts."

Agency actions

On August 2, 1977, the Director of IRS' Criminal Investigation Division issued guidelines alerting special agents to consider recommending criminal prosecutions of taxpayers who did not answer or improperly answered the foreign bank account question. During fiscal year 1978, special agents recommended eight such prosecutions.

Recommendation 9

"As the current information provided IRS by taxpayers regarding foreign bank accounts is not available for dissemination to other agencies because of [the] Tax Reform Act of 1976, the Secretary of the Treasury should devise alternate procedures implemented by amending Treasury Regulations. In the event that this is not feasible, the Secretary should recommend legislation as to remedy the specific problem or to transfer implementing authority or to strike pertinent sections of the law which are impossible or are undesirable to administer."

Agency actions

By substituting Treasury form 90-22.1 for IRS form 4683, the Secretary of the Treasury apparently resolved disclosure problems arising from the Tax Reform Act of 1976 thereby eliminating restrictions on the dissemination of foreign bank account information.

Recommendation 10

> "The Secretary shall report to the Government Operations Committee by the end of fiscal year 1977 the results of Treasury Department's efforts to further the implementation of the foreign bank, trust, securities or other financial account reporting requirement of the Bank Secrecy Act."

Agency actions

The Secretary's October 12, 1977, letter to the Chairman, House Committee on Government Operations was designed to respond to this recommendation.

CONCLUSIONS

Treasury's decision to enter foreign bank account data on TECS was prompted by recommendations made by the House Committee on Government Operations. Those recommendations also prompted other actions by Treasury and IRS, such as resolving disclosure problems caused by the Tax Reform Act of 1976 and establishing the Reports Analysis Unit. Treasury now needs to follow up on those actions by monitoring the effectiveness of foreign bank account data and seeking other ways to improve the usefulness of the data. If Treasury efforts show that the data is not very useful, however, it should request the Congress to reconsider the need for the reporting requirements.

RECOMMENDATIONS

We recommend that the Secretary of the Treasury

--monitor the use of foreign bank account data entered on TECS and

--determine whether foreign bank account information has other potential uses.

If the Secretary determines that computerized foreign bank account data is not useful and foreign bank account data has no other potential uses, he should request the Congress to reconsider the need for the reporting requirements.

AGENCY COMMENTS AND OUR EVALUATION

In his March 19, 1979, letter, the Acting Secretary concurred with our recommendation that Treasury monitor the usefulness of computerized foreign bank account data.

He noted, however, that Treasury had already taken action to disseminate foreign bank account data and that such data already had proven useful to various Federal law enforcement agencies.

We recognize that foreign bank account data has proven useful to various law enforcement agencies in particular instances. However, as we stated on page 14 in connection with currency reports, an overall evaluation of the usefulness of foreign bank account data would be necessary to reach such a conclusion. This evaluation should be done while implementing our recommendations to monitor the use of foreign bank account data on TECS and to determine whether other potential uses exist for the data.

CHAPTER 5

SCOPE OF REVIEW

We reviewed the policies and procedures followed by IRS' Criminal Investigation, Examination, and Collection Divisions, and its Office of International Operations in processing and using each of the above-mentioned financial and foreign account reports. We conducted our work as part of a broad review of IRS' criminal investigation operations at its headquarters in Washington, D.C.; its service centers in Andover, Massachusetts; Austin, Texas; Fresno, California; Kansas City, Missouri; and Philadelphia, Pennsylvania; and its district offices in Boston, Chicago, Dallas, and Los Angeles.

We interviewed officials at IRS, the Treasury Department, the Customs Service, and the Drug Enforcement Administration. We reviewed records related to each report and analyzed samples of the two currency reports required by the Bank Secrecy Act. We limited our review of the usefulness of foreign bank account reports to following up on the recommendations made by the House Committee on Government Operations, in its May 1977 report on the subject.

THE SECRETARY OF THE TREASURY
WASHINGTON 20220

March 19, 1979

Dear Mr. Voss:

We appreciate this opportunity to review and comment upon your draft report entitled, "The Use of Currency and Foreign Account Reports by Treasury and IRS Needs Improvement."

In the draft report, you focused principally upon the utilization of currency and foreign account reports as they relate to the investigation of possible non-compliance with the tax laws. As the following comments indicate, we generally agree with the principal recommendations in the draft report which relate to the utilization of these reports for tax purposes. The report, however, fails to give adequate recognition to the usefulness of these reports to other Federal law enforcement agencies and to the substantial progress that has been made in making these reports available to other government agencies, and in enforcing compliance with the Bank Secrecy Act. Although we recognize that these considerations may have been beyond the scope of GAO's review, we have addressed these issues in our response because we believe their consideration is necessary to present a fair picture of the overall usefulness of these reports for law enforcement and regulatory purposes.

Chapter 2 - Currency Transaction Reports

> "GAO recommends that the Secretary of the Treasury, in implementing the plans to enter currency transaction reports on the Treasury Enforcement Communications System, ensure that unnecessary processing of currency reports is eliminated. Specifically, the Secretary should (1) ensure that all currency reports are filed with the group he designates to enter the reports on the Treasury Enforcement Communications System and (2) eliminate wholesale exchanges of currency reports between IRS, Customs and the Reports Analysis Unit. GAO also recommends that the Secretary ensure that IRS uses the Treasury Enforcement Communications System to improve evaluations of information its receives and processes concerning possible tax law violations."

"In addition, the Secretary should (1) monitor the use of currency transaction reports once they are incorporated in the Treasury Enforcement Communications System to determine if their value has improved and, (2) determine whether currency reports have other potential uses."

"If the Secretary determines that the value of currency reports cannot be improved, he should request the Congress to reconsider the need for the reporting requirements."

"The Commissioner should also provide necessary training and take appropriate steps to ensure that IRS personnel understand the Treasury Enforcement Communications System and know how to use it."

We are in general agreement with these recommendations. A program is already underway to have all currency transaction reports entered on the Treasury Enforcement Communications System as soon as practicable. This process will be supervised by the Reports Analysis Unit, which is soon to be transferred from the Office of the Secretary to the Customs Service. As this is implemented, we will eliminate unnecessary processing and unnecessary wholesale exchanges of currency reports between the Internal Revenue Service and the Customs Service. To accomplish this, the Office of the Assistant Secretary (Enforcement and Operations), with the assistance and cooperation of the Internal Revenue Service and the Customs Service, is considering whether it is feasible and cost beneficial to process currency transaction reports, as well as the other required reports entered on the Treasury Enforcement Communications System in a single organizational unit. We also agree that it may be more efficient for currency transaction reports to be filed with the group designated by the Secretary to enter these reports on the Treasury Enforcement Communications System, and we will examine whether such a change would be feasible.

We agree that the Treasury Department should monitor the use of currency transaction reports and other reports entered on the Treasury Enforcement Communications System to evaluate their effectiveness as law enforcement tools. As explained more fully in our comments on Chapter 4 of the draft report, currency transaction reports and other reports now entered on the Treasury Enforcement Communications System have proved useful to law enforcement and regulatory agencies. While we will continue to monitor their usefulness, we believe the present record shows that the reports have been useful for law enforcement purposes.

We hope that placing these reports on the Treasury Enforcement Communications System will improve their usefulness to the Internal Revenue Service. To that end, the Internal Revenue Service will initiate training programs to ensure the efficient operation and use of the Treasury Enforcement Communications System by its terminal operators. The Internal Revenue Service will also take appropriate steps to notify its Criminal Investigation, Examination, and Collection personnel of the information contained in the Treasury Enforcement Communications System and its potential uses, particularly as it relates to the reports required by the Bank Secrecy Act.

Chapter 3 - Foreign Trust Returns

> "We recommend that the Commissioner of Internal Revenue determine whether IRS can effectively use foreign trust returns by developing (1) a program to ensure maximum compliance with the filing requirements and (2) appropriate evaluation criteria aimed at maximizing the usefulness of the forms."
>
> "If the Commissioner finds that IRS cannot use the forms effectively, he should concurrently (1) request, through the Secretary of the Treasury, that the Congress reconsider the need for the filing requirements and (2) develop an alternative plan of action aimed at ensuring compliance on the part of taxpayers with the tax laws governing foreign trusts."

Section 6048(a) of the Internal Revenue Code requires the grantor or transferor of a foreign trust to file a return within 90 days of the creation of the trust or the transfer of any money or property to the trust. The return in question (Form 3520) is filed with the Internal Revenue Service's Philadelphia Service Center. This requirement was added by the Revenue Act of 1962.

Section 6048(c) requires each taxpayer subject to tax under section 679 (the special "grantor trust" provisions applicable to United States persons transferring property to a foreign trust having United States beneficiaries) to file an annual return with respect to that trust. This annual return (Form 3520-A) must be filed by the transferor with the IRS Philadelphia Service Center within four months and fifteen days following the close of the taxable year of the transferor. This requirement was added by the Tax Reform Act of 1976.

These two filing requirements supplement a third filing requirement which applies to foreign trusts. Section 1491 imposes an excise tax on transfers of appreciated property by a United States person to, *inter alia*, a foreign trust. Section 1494(a) and the regulations thereunder require every person making a transfer described in section 1491 to file a return (Form 926) on the day of the transfer with the Internal Revenue Service's Service Center where the transferor's income tax return is required to be filed. This requirement has been in the law since the enactment of the Internal Revenue Code in 1954, and indeed replaced a similar requirement imposed by the 1939 Code.

The substantive provisions which these provisions accompanied eliminated many tax avoidance opportunities previously available through the utilization of foreign trusts. The identification of foreign trusts was felt to be valuable both in administering these provisions and in identifying trusts used for unlawful tax evasion. We believe these forms can be made to serve those purposes and will study ways to make them more effective.

Your report indicates that the Internal Revenue Service has not maintained adequate processing controls over Forms 3520 and 3520-A. We agree, and are establishing procedures to process those forms that will provide us with the capability to retrieve and utilize these forms. This will enable us to provide the Department of Justice with a certification of nonfiling when we are requested to do so in connection with ongoing criminal prosecutions.

You also recommend that the Internal Revenue Service develop appropriate evaluation criteria in connection with Forms 3520 and 3520-A. We share your concern that Internal Revenue Service personnel be given better guidance on the potential usefulness of these forms and be encouraged to use them in appropriate cases. We question, however, whether fixing national evaluation criteria will achieve this result. However, the Internal Revenue Service will review its current program to determine whether appropriate means can be derived to increase the frequency and quality of use of information obtained from these forms.

You also recommend that the Internal Revenue Service develop a program to assure maximum compliance with the return filing requirements. The Internal Revenue Service agrees that it will review its programs and procedures in this area. A continuing problem in developing an effective compliance program in this area is gaining access to information frequently available only from foreign sources. We are attempting to determine those instances where such information is available as a matter of public record in the foreign country. We are also attempting to gain access to such information under the tax treaties and mutual assistance agreements we have with various nations. In many instances, however, we either have no treaty or assistance agreement with the situs country, or the information that we seek is not available under the provisions of the treaty or agreement, or is only available in a form which limits its usefulness for our purposes. In certain instances, this information is protected under bank secrecy or other laws of the situs country.

Notwithstanding these limitations on availability and the need to recognize the limitations imposed in our dealings with other sovereign states, the Internal Revenue Service will attempt to develop instructions designed to assist its examiners in identifying the returns of beneficiaries and grantors to achieve maximum compliance with these filing requirements. We will also continue our efforts to obtain data available from foreign countries.

Chapter 4 - Foreign Bank Account Data

"We recommend that the Secretary of the Treasury (1) monitor the use of foreign bank account data entered on TECS, and (2) determine whether foreign bank account information has other potential uses."

"If the Secretary determines that computerized foreign bank account data is not useful and foreign bank account data has no other potential uses, he should request the Congress to reconsider the need for the reporting requirement."

In this chapter of the draft report, you discuss ten specific recommendations made to the Department in the report of the House Committee on Government Operations dated May 5, 1977. The Secretary has furnished, to GAO, prior responses to that Committee with respect to those recommendations in letters dated June 28, 1977 and October 12, 1977. Those comments will not be repeated here. However, where additional actions have been taken, those actions will be noted.

The Department agrees that it should continue to monitor the usefulness of foreign bank account data reported on Form 90.22-1. The Department has already undertaken significant actions to ensure that this information, and information contained on other forms required to be filed under the Bank Secrecy Act, are made available to the appropriate Federal law enforcement and regulatory agencies in accordance with formal guidelines and safeguards to be utilized by the user agencies in order to assure appropriate protection for the privacy of individuals.

At present, Reports of International Transportation of Currency or Monetary Instruments (Forms 4790) are entered on the Treasury Enforcement Communications System. We intend to enter both Currency Transaction Reports (Forms 4789) and Reports of Foreign Bank and Financial Accounts (Forms 90.22-1) on that system. However, we have already been analyzing data contained on Forms 4789 and 4790 and, where appropriate, furnished that information to the responsible Federal enforcement agencies.

For example, in fiscal year 1978 alone the Department provided the Drug Enforcement Administration with 1,394 currency transaction reports reflecting reported transactions of $157.5 million. During this same period, we provided the Drug Enforcement Administration with 83 Forms 4790 relating to $6.5 million. A large number of reports were also provided to other offices within the Department of Justice, as well as to certain Congressional committees. Although these reports have already proven useful to various Federal agencies, we believe that placing all three reports on the Treasury Enforcement Communications System will improve their potential usefulness to all Federal law enforcement and regulatory agencies including the Internal Revenue Service.

We also think it is appropriate to note other activities of the Department in this area. The Office of the Assistant Secretary (Enforcement and Operations) has:

- Completed arrangements for dissemination of material to the Department of Justice including the Federal Bureau of Investigation and the Drug Enforcement Administration.

- Sent letters to senior officials of appropriate Federal departments and agencies to make them aware of the data available to them pursuant to the Bank Secrecy Act.

- Established formal guidelines and safeguards for the utilization of report information by user agencies in order to provide appropriate safeguards for the privacy of individuals.

- Established a Reports Analysis Unit in July, 1978 to maximize the effective utilization of data from the required reports. Both the Internal Revenue Service and the Customs Service provided substantial support in the operation of this Unit. The Unit, which will be integrated into the Customs Service on April 1, 1979, will be responsible for coordinating the computerization of all three reports required to be filed under the Bank Secrecy Act. It also acts as a liaison with other Federal agencies, making those agencies aware of the data available and providing them with the data when appropriate.

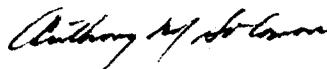
- Worked closely with the various Federal financial supervisory agencies to improve compliance by institutions they supervise with both the reporting and recordkeeping requirements of the Bank Secrecy Act, and has asked those agencies to provide additional data regarding specific violations and areas of noncompliance.

- Recently completed arrangements to have the Federal Deposit Insurance Corporation inspect the uninsured foreign banks operating in the U.S. in order to ensure their compliance with both the reporting and recordkeeping requirements of the Act. In this regard, we recently sent letters to approximately 300 of these institutions informing them that the FDIC will begin inspecting them for compliance with the requirements of the Bank Secrecy Act.

In addition, at the Department's request, the Internal Revenue Service has worked to ensure compliance with the reporting and recordkeeping requirements by "secondary" financial institutions. The Customs Service also has increased its emphasis on enforcement of the Bank Secrecy Act reporting requirements. During fiscal year 1978 Customs made 639 seizures involving more than $12.9 million in cases involving violations of the Bank Secrecy Act. During the same period, there were 36 convictions for criminal violations of the Act.

We recognize that significant work remains to be done. However, we believe that the record to date reflects substantial progress.

Sincerely,



Anthony M. Solomon
Acting Secretary

Mr. Allen R. Voss, Director
General Government Division
United States General
Accounting Office
Washington, D.C. 20548

(268074)

Single copies of GAO reports are available free of charge. Requests (except by Members of Congress) for additional quantities should be accompanied by payment of $1.00 per copy.

Requests for single copies (without charge) should be sent to:

U.S. General Accounting Office
Distribution Section, Room 1518
441 G Street, NW.
Washington, DC 20548

Requests for multiple copies should be sent with checks or money orders to:

U.S. General Accounting Office
Distribution Section
P.O. Box 1020
Washington, DC 20013

Checks or money orders should be made payable to the U.S. General Accounting Office. NOTE: Stamps or Superintendent of Documents coupons will not be accepted.

PLEASE DO NOT SEND CASH

To expedite filling your order, use the report number and date in the lower right corner of the front cover.

GAO reports are now available on microfiche. If such copies will meet your needs, be sure to specify that you want microfiche copies.

AN EQUAL OPPORTUNITY EMPLOYER

UNITED STATES
GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

OFFICIAL BUSINESS
PENALTY FOR PRIVATE USE,$300

POSTAGE AND FEES PAID
U. S. GENERAL ACCOUNTING OFFICE

THIRD CLASS