

**WRITTEN STATEMENT OF
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BEFORE THE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
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Good morning, Mr. Chairman and distinguished Members of the Committee. I appreciate the opportunity to be here today to discuss the Internal Revenue Service's (IRS) efforts involving the Bank Secrecy Act (BSA). I would also like to thank your Committee staff members who assisted us during the preparation for this hearing.

IRS Enforcement

Under the leadership of Commissioner Everson, we are strengthening the focus on enforcement at the IRS, while maintaining appropriate service to taxpayers. We have four enforcement priorities. We will:

- Discourage and deter non-compliance, with emphasis on corrosive activity by corporations, high-income individual taxpayers, and other contributors to the tax gap;
- Assure that attorneys, accountants, and other tax practitioners adhere to professional standards and follow the law;
- Detect and deter domestic and offshore-based tax and financial criminal activity; and
- Discourage and deter non-compliance within tax-exempt and government entities and misuse of such entities by third parties for tax avoidance and other unintended purposes.

Detecting and investigating money laundering activity is an important part of tax compliance for the IRS. In addition, the failure to file Forms 8300 and criminal violations of the BSA, including the structuring of deposits to avoid currency transaction reporting requirements, often have a direct link to both tax evasion and money laundering. In some cases, because the schemes are sophisticated and because we may not be able to obtain evidence from some foreign countries, it is almost impossible to conduct traditional tax investigations. In these circumstances, money-laundering violations frequently are the only possible means to detect tax evaders.

Money laundering not only is used by domestic and international criminal enterprises to conceal the illegal, untaxed proceeds of narcotics trafficking, arms trafficking, extortion, public corruption, terrorist financing, and other criminal activities; it is also an essential element of many tax evasion schemes. With the globalization of the world economy and financial systems, many tax evaders exploit domestic and international funds transfer methods to hide untaxed income. These schemes often involve the same methods to hide money from illegal sources and to hide unreported income. Both activities generally use nominees, currency, wire transfers, multiple bank accounts, and international “tax havens” to avoid detection.

Money laundering is the financial side of virtually all crime for profit. To enjoy the fruits of their crime, criminals must find a way to insert the illicit proceeds of that activity into the stream of legitimate commerce in order to provide the resources necessary for criminal organizations to conduct their ongoing affairs.

As part of its core tax administration mission, the IRS addresses both the civil and criminal aspects of money laundering. On the civil side, the Department of the Treasury has delegated to the IRS responsibility for ensuring compliance with the BSA for all non-banking and financial institutions not otherwise subject to examination by another federal functional regulator, including Money Service Businesses (MSBs), casinos and credit unions. Under this delegation, the IRS is responsible for three elements of compliance – (i) the identification of MSBs, (ii) educational outreach to all these types of organizations, and (iii) the examination of those entities suspected of noncompliance.

The IRS’ Criminal Investigation (CI) Division is responsible for the criminal enforcement of BSA violations and money laundering statutes related to tax crimes. CI uses the BSA and money laundering statutes to detect, investigate, and prosecute criminal conduct related to tax administration, such as abusive schemes, offshore tax evasion, and corporate fraud. CI also investigates the non-filing of Forms 8300 and criminal violations of the BSA, including the structuring of deposits to avoid currency transaction reporting requirements, which frequently have a direct link to both tax evasion and money laundering.

Recently, the IRS created a new position with responsibility for the coordination of all IRS terrorist financing-related issues which will report directly to the Deputy Commissioner for Services and Enforcement.

BSA Program in IRS’ Small Business/Self-Employed (SB/SE) Division

In further recognition of the importance of the IRS’s role in the fight against terror and money laundering, SB/SE has just established a new organization, the Office of Fraud/BSA, which reports directly to the Commissioner of SB/SE. The director, an IRS executive, will have end-to-end accountability for compliance with BSA including policy formation, operations, and BSA data management. The director’s operational

responsibility will include line authority over all field activities, as well as the data management.

This new Office of Fraud/BSA consists of four territories, with about 310 field examiners reporting to managers located in 33 field offices nationwide. These examiners and their managers are fully trained and are dedicated full-time to the BSA program. Additional support personnel provide assistance to the examiners, including workload identification. Working in close collaboration with Treasury's Financial Crimes Enforcement Network (FinCEN), the IRS also conducts community outreach to ensure that MSBs are aware of their requirements under the BSA.

Bank Secrecy Act Data

The IRS has responsibility for processing and warehousing all BSA documents into the Currency Banking and Retrieval System (CBRS), including Foreign Bank & Financial Account Reports (FBARs), Currency Transaction Reports (CTRs)¹, Forms 8300 (Report of Cash Payments Over \$10,000 Received in a Trade or Business), and Suspicious Activity Reports (SARs)². All BSA forms are processed at the IRS Detroit Computing Center (DCC). Managing the BSA data involves three separate but related functions that include: (i) collecting and inputting BSA data from reporting institutions; (ii) housing and controlling access to the BSA data after it is entered into the central database; and (iii) supporting the IRS and other law enforcement query systems to mine BSA data in support of law enforcement investigations.

Currently, CBRS has approximately 173 million BSA documents on file. These documents are comprised of CTRs, SARs, Forms 8300, CMIRs³, FBARs and various other BSA documents. All documents entered into the CBRS (approximately 14 million annually) are made available, at FinCEN's direction, to other law enforcement agencies (Federal, state, local and international) and regulatory agencies, in addition to the IRS. However, the IRS is the largest user of the CBRS.

Usefulness of Bank Secrecy Act Data

The combined currency information in CBRS is extremely important for tax administration and law enforcement. The information provides a paper trail or roadmap for investigations of financial crimes and illegal activities, including tax evasion, embezzlement, and money laundering. The detailed information in these currency reports routinely is used by IRS CI special agents and Assistant U.S. Attorneys to successfully pursue investigations and prosecutions.

¹ CTRs include FinCEN Form 104 and FinCEN Form 103 (filed by casinos).

² SARs are filed by financial institutions to report suspicious activity.

³ Report of International Transportation of Currency or Monetary Instruments.

In civil matters, the IRS uses the CBRS database to identify cases for potential examination. For example, in many of our offshore trust schemes a search of CTRs can produce a wealth of information. IRS field examiners also access BSA documents to assist in on-going examinations. The CBRS database is used to assist in case building prior to beginning an examination.

Federal and state law enforcement agencies also find the CBRS data useful as evidenced by their participation in each of the 41 IRS hosted Suspicious Activity Report Review Teams (SAR-RTs) located throughout the country in our 34 Criminal Investigation field offices. Nationwide, approximately 345 law enforcement personnel are assigned, either full or part-time, to the SAR-RTs. These teams evaluate and analyze the SARs for case development and field office support. Each month, these SAR-RTs review approximately 12,000 to 15,000 SARs.

IRS Coordination with FinCEN

In carrying out our responsibilities under the Bank Secrecy Act, we are engaged in a close partnership with FinCEN. Currently, the IRS assigns senior analysts to act as the liaisons to FinCEN in both the civil and criminal matters. These individuals address issues ranging from the case support supplied by FinCEN to strategic implementation and interpretation issues pertaining to the Bank Secrecy and USA PATRIOT Act.

Beginning in FY 2003, funding from FinCEN has allowed the IRS to add 82 additional full-time employees (FTEs) to its BSA program. Key areas of coordination include:

- Improving the quality of referrals for enforcement;
- Using data-driven analysis to assist in the risk-based identification of cases as well as to identify geographic locations of potential noncompliance;
- Conducting joint monthly meetings to discuss BSA issues, trends, and examination results;
- Establishing examination priorities;
- Having FinCEN participate in IRS BSA training classes and managers' meetings;
- Incorporating feedback from FinCEN on IRS outreach materials; and
- Establishing production schedules at DCC for new forms and form revisions.

Strategies and Initiatives

We are undertaking several initiatives to enhance the BSA Program:

- **MSB Audits** - We are piloting the examination of MSBs at the entity's corporate headquarters level. Three such examinations are currently underway. Working with the businesses, we are identifying their agents with

the highest risk of noncompliance. This is a new approach for the program that was advocated by FinCEN, which we believe will provide better customer service for the MSBs and maximize our use of resources.

- **Increased Coordination with the States** - We have completed a model Federal/State Memorandum of Understanding (MOU), which provides both the IRS and the participating state the opportunity to leverage resources for examinations, outreach, and training. We expect this MOU, developed jointly with FinCEN, to be available for sharing with the states in the near future.
- **Improved BSA Training** - We have undertaken a major training initiative, including revising the Basic BSA Course to reflect the changes resulting from the USA PATRIOT Act. All personnel are:
 - Instructed on how to access OFAC's (Office of Foreign Asset Control) website to identify individuals and countries which have been placed on OFAC's SDN (Specifically Designated National or Blocked Person) list.
 - Trained to look for transactions going to OFAC blocked countries. Identification of these transactions has resulted in several referrals to IRS' CI organization and one contact to the Terrorist Hotline.
 - Trained to identify unlicensed money transmitters. This year, four continuing professional education (CPE) training classes were provided to IRS field examiners: (i) Suspicious Activity Reports; (ii) Structuring, (iii) Informal Value Transfer Systems, and (iv) Section 352 of the USA PATRIOT Act.
 - Trained in audit procedures to detect structuring.
- **More Effective Case Selection** - We have increased BSA program oversight to ensure the compliance risk case selection tools provided to our field examiners are being used to identify cases. The centralization of case identification that will incorporate leads from the field and CI, as well as CBRS analysis, is scheduled to be in place by the end of the year. This approach will ensure consistency in risk-based case selection.
- **Better Education and Outreach** - Historically, most of our field examiners spent a portion of their time conducting individual outreach visits. Education and outreach now is performed by SB/SE's Taxpayer Education and Communication (TEC) Division, which leverages resources to reach a larger number of covered businesses. We provide keynote speakers, conduct seminars, and provide educational programs relating to check cashers, bankers, tax practitioners, fraud examiners, corporate security personnel, and bank security officers. This outreach and our efforts to contact money service businesses are significant parts of our program to identify and educate MSBs regarding their requirements to register their business with both the state and federal government. The National TEC AML strategy was designed in conjunction with FinCEN, SB/SE, and CI to increase compliance of MSBs

and casinos with the BSA.

- ***Streamlined Quality Review*** - Quality performance measures have been developed, including a centralized review process. The centralized closed case review process will provide headquarters with the ability to identify trends and training needs. Including BSA in our quality review process will ensure a systemic method for making proper use of managerial feedback.
- ***Anticipating Expanded Examination Scope*** - In anticipation of the requirement for the insurance industry to come under section 352 of the USA PATRIOT Act, the IRS is working with the industry and FinCEN to develop an examination plan and a training program for field examiners.

IRS Resources Devoted to BSA

In FY 2004, the IRS devoted 1,112 FTEs to the BSA Program for enforcement, compliance and data management activities. In particular, CI devoted 486 FTEs to BSA enforcement, including 457 FTEs directly related to investigations. The SB/SE Division devoted 414 FTEs for BSA compliance activity, including examinations and outreach/education efforts, and 212 FTE for managing information related to BSA (179 FTE for CTR processing and 33 FTE for program maintenance). Of the above amounts, 82 FTEs were funded by FinCEN, including 64 FTEs for compliance activities, 6 FTEs for outreach and 12 FTEs for managing information related to BSA.

The IRS' total FY 2004 BSA costs will be approximately \$131 million, including direct and indirect costs such as human resources, training, space, and computer support. In FY 2004, CI expects to spend about \$71 million on BSA compliance, including \$67 million directly related to primary and secondary investigations. The SB/SE Division expects to spend \$36 million for BSA compliance activity, including examinations and outreach/education efforts. The IRS expects to spend \$24 million for managing information related to BSA, including \$2.5 million for data services.

Conclusion

As I stated earlier in this testimony, the war on terrorism and the fight against money laundering are top priorities for the Internal Revenue Service. We are prepared to increase our commitment to the BSA Program, and we will continue to coordinate our efforts closely with FinCEN.

Mr. Chairman, I thank you for this opportunity to appear before this distinguished committee and I will be happy to answer any questions you and the other Members of the committee may have.